Where does Brexit leave investment protection?

Tom Jones

14 January 2021

European Commission president Ursula von der Leyen and the UK's prime minister Boris Johnson (Credit: AFP via Getty Images / Shutterstock)

In the wake of the UK-EU trade deal, practitioners say questions remain over the investment protections in the agreement and the fate of the UK’s bilateral investments treaties with EU member states.

On 24 December, the UK and EU signed their Trade and Cooperation Agreement (TCA) – which will govern their relationship following the UK’s exit from the trading bloc.

The treaty applies provisionally from 1 January, when the transition period provided under the Withdrawal Agreement came to an end. It will fully enter into force once the European Parliament and the Council of the EU have ratified the text.

The 1,246-page TCA contains hundreds of new provisions regulating trade, transport, fisheries, law enforcement and – importantly for arbitration practitioners – investment protection and dispute settlement. As lawyers, governments and business have scrambled to interpret what the trade deal means, one thing has become clear: it is unlike any other the EU has struck before.

Inadequate investment protection?
“The TCA’s investment protection provisions fall short of what investors might have hoped for,” says Fietta counsel Laura Rees-Evans. It is a view shared by many practitioners and trade experts.
Investment in the TCA is governed by Part Two, Heading One, Title II. In terms of substantive protections, it merely provides a guarantee of non-discrimination – with each party promising to provide investors of the other party with treatment no less favourable than that accorded to its own investors or to investors of a third country. It also includes a denial of benefits clause.

However, in stark contrast to the other treaties the EU has recently signed, there are no provisions on fair and equitable treatment, full protection and security or expropriation.

Access to the treaty’s substantive protections is also restricted by the TCA’s narrow definition of “investor”, which requires substantive business operations in the investor’s home state and therefore creates an additional jurisdictional hurdle for investors to meet.

“Put simply – the TCA is a poor equivalent of the Canada-EU Trade Agreement (CETA)” says Paschalis Paschalidis, a former référendaire at the Court of Justice of the European Union (CJEU) who is now senior associate at Shearman & Sterling in Paris.

**No CJEU, no ISDS**

UK prime minister Boris Johnson set out several “red lines” in the negotiations with the EU, including “no role for the European Court of Justice in the UK” and “no obligation for the UK to continue to be bound by EU law”.

That demand appears to have been met by Part Six of the TCA, which provides that any disputes under the agreement are subject to a “state-to-state” arbitration mechanism.

In addition, save for some limited exceptions, the TCA is not invocable before the courts of the UK and the EU and does not create rights other than between the treaty signatories. This means that EU and UK courts will have no jurisdiction to resolve disputes under the TCA.
The dispute settlement mechanism in the TCA is separate from the one contained in the Withdrawal Agreement, which addresses a wide range of issues relating to the divorce between the UK and the EU. The panel of 25 arbitrators that will hear disputes under the Withdrawal Agreement was named last month. A similar panel will be formed to hear disputes arising out of the TCA, although that list has not been published yet.

Importantly, the TCA does not provide for any form of investor-state dispute settlement (ISDS) and the most-favoured-nation clause explicitly excludes ISDS from its scope. That stands in contrast to CETA and the EU’s recent trade agreements with Singapore and Vietnam – which all provide for investor-state disputes to be resolved by a permanent investment court.

Investors who feel there has been a breach of the TCA will therefore have to convince the UK or EU to take on their case in an arbitration against the other treaty party.

In a blog post for Kluwer, three Linklaters lawyers note that investors will have the possibility to file amicus curiae submissions once an arbitration is instituted. The arbitration tribunal shall consider those submissions but is not obliged to address them.

A future “mixed” investment agreement?
There are reasons for the limited substantive investment protection and the lack of an ISDS mechanism in the TCA, according to Nikos Lavranos, founder of NL-Investment Consulting in Brussels and secretary-general of the European Federation of Investment Law and Arbitration, a pro-ISDS think-thank.

“We know from the CJEU’s decision in the EU-Singapore case that investment protection and ISDS are within the competence of EU member states – and can therefore only be dealt with in mixed agreements signed with the EU and those states.

“The TCA is only a trade agreement between the EU and the UK, not the other EU member states. CETA and the EU’s recent trade agreements with Singapore
and Vietnam are mixed agreements and that is why they contain more substantive investment protection,” he says.

Rees-Evans agrees that any ISDS mechanism in the TCA would have required ratification from each EU member state – which was “probably unachievable in the short time available.”

Might the UK and the EU try and negotiate an additional mixed agreement in the future with more substantive investment protections and an ISDS mechanism? “It is perfectly possible,” Lavranos says, pointing to the EU-Singapore Investment Protection Agreement – a formally separate treaty from the EU-Singapore Free Trade Agreement.

However, Rees-Evans notes that, unlike the UK-Japan trade agreement, the TCA “contains no indication that the UK and EU intend in the longer term to negotiate any comprehensive investment mechanism.”

**Will the UK’s BITs with member states survive?**
Another uncertainty is the status of the UK’s 11 remaining bilateral investment treaties with EU member states, which are not specifically mentioned in the TCA.

In 2019, the UK was among the 28 EU member states that signed a declaration committing to terminate all BITs signed between them following the Achmea judgment – which found ISDS provisions in such a treaty to be incompatible with EU law.

However, when 23 EU countries signed a plurilateral treaty to terminate their intra-EU BITs, the UK did not sign the agreement. The European Commission launched infringement proceedings against the UK in May last year – with those proceedings yet to reach the CJEU.

So are the UK’s BITs with EU member states still in force? Perhaps for now, but Paschalidis is pessimistic about their fate. He says that if the case did end up before the CJEU, the court would find the ISDS provisions of these BITs to be incompatible with EU law. The judgment would still be binding on the UK under the terms of the Withdrawal Agreement.
While it may be possible for the BITs to survive as “supplemental agreements” under the TCA, the treaty would require that they are interpreted as not conferring rights on investors, he says.

“Thus, although still alive, these BITs are probably at their end of their life expectancy.”

Lavranos takes a very different view. He says that EU law no longer binds the UK, and therefore the country’s BITs with member states have effectively become “extra-EU BITs”. Therefore, the principles of the Achmea judgment “do not and should not apply”.

He adds that the political declaration that the UK signed, committing to terminate its BITs with member states, is “not a legally binding document” and the Withdrawal Agreement does not contain any specific obligations about BITs. “I don’t think you can be legally forced to terminate your own international agreements.”

Lavranos says the UK government “sees value in maintaining these BITs and rightfully so”. There is a treaty with Hungary – a country that has been strongly criticised in recent years for undermining the rule of law – and agreements with countries like Romania that still face corruption issues.

His view is shared by Andrea Carlevaris, a partner at BonelliErede in Rome and a former secretary-general of the ICC International Court of Arbitration, who agrees that the UK’s BITs with EU member states have become extra-EU BITs and therefore remain in force.

As a result, he believes the UK is “likely to become an attractive destination for European investors, who, by relocating to the UK, may regain investment protection under UK’s existing and future BITs with EU member states.”

Ultimately, Rees-Evans says that the TCA “raises more questions than it answers” on the UK’s BITs with EU member states.
Unlike the EU’s other recent investment agreements, the TCA does not purport expressly to terminate any existing BITs between the Parties. In my view, it is unlikely that they have been impliedly terminated by the TCA under Article 59 of the Vienna Convention.”

While it is “not inconceivable” that the Commission will pursue the infringement proceeding all the way to the CJEU, she said it would be “very difficult to predict the ultimate result.”

“In the meantime, cross-border investors will either take their chances with the remaining BITs, notwithstanding their uncertain status and future, or will seek to restructure their investments through other jurisdictions with whom investment protection is stronger than it is in the TCA and clearer than it is under the UK’s (formerly intra-EU) BITs.”