

Balancing Economic Security and Investment Protection, Part I

Dispute Resolution & Competition Law/International Trade Newsletter

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1. Introduction

On 20 June 2023, the Commission of the European Union (“EU”) published a proposed “European Economic Security Strategy” (“**Strategy**”).² As part of this Strategy, the EU plans to “review the Foreign Direct Investment Screening Regulation” and “fully implement the EU’s export control regulation on dual use items and make a proposal to ensure its effectiveness and efficiency.”³

This two-part newsletter intends to analyze ways in which the new EU policy may affect Japanese businesses from the viewpoint of the Japan-EU Economic Partnership Agreement (“EPA”) which affords Japanese investors in the EU certain protections. The second part of the newsletter will address international recourse Japanese businesses might have against such policy, referring to recent developments in investor-state dispute settlement (“ISDS”) related to economic security.

2. Overview of the EU strategy

The Strategy identifies four economic security risks which the EU faces: risks to the resilience of supply chains, including energy security; risks to the physical and cyber security of critical infrastructure; risks related to technology security and technology leakage; and risks of weaponization of economic dependence or economic coercion. It also sets out a three-pronged approach to risk mitigation, i.e., by promoting economic infrastructure, competitiveness, and growth, protecting against economic security risks, and collaborating on economic security.

The Strategy envisages a variety of measures to be enacted, such as the establishment of a list of technologies of economic security importance and of a framework for assessing risks to the EU’s economic security, the revision of inward Foreign Direct Investment screening rules, and the full implementation of the EU’s export control rules on dual-use goods. It proposes a risk assessment methodology which is to serve as a basis for future discussions with Member States and the European Parliament on of risk reduction and economic security in the EU.⁴

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² https://ec.europa.eu/commission/presscorner/detail/en/IP_23_3358

³ Strategy, part 3.3, “next steps”.

⁴ The details of the strategy have been analyzed in depth in a newsletter article in Japanese published by Nishimura & Asahi, which can be accessed at [this link](#).

Although the EU does not expressly state that its approach is aimed at countering any specific economy, it follows a global trend towards reaffirming and strengthening states' abilities to regulate in the public interest and goes a step further by strengthening their economic resilience and reducing their economic dependency, in a manner that is less encumbered by such states' obligations towards foreign investors.⁵

At the same time, because the EU measures do not explicitly target any particular economy or state, the provisions could theoretically affect businesses from any economy or state, including companies incorporated in Japan and doing business in Europe.

Therefore, Japanese businesses will want to closely monitor the development of such measures. Indeed, their economic activities in the EU could be hindered, or even restricted, if they are designated as technologies of economic security importance by upcoming legislation in application of the EU's new policy.⁶

At the same time, Japanese businesses might be able to rely on the protection afforded by the substantive principles and provisions of the EPA, which recently entered into force and aims to facilitate trade and investment between the EU and Japan.

3. Overview of the EPA

The EPA entered into force on 1 January 2019. It aims at "strengthening [the contracting Parties'] economic, trade and investment relations" by "establish[ing] clear and mutually advantageous rules governing trade and investment between the Parties and [] reducing or eliminat[ing] barriers thereto."⁷

This international treaty contains various chapters, including chapters on Trade in Services, Investment Liberalisation and Electronic Commerce (Chapter 8), Transparency (Chapter 17), and Good Regulatory Practices and Regulatory Cooperation (Chapter 18).

The EPA reflects the contracting parties' intention to ensure the openness of services markets. Notably, the EPA provides for clauses which promote regulatory cooperation activities under Article 18.12. To achieve this objective, the EPA establishes mechanisms to, among others, maintain internal coordination processes or mechanisms to foster good regulatory practices,⁸ make internal processes and mechanisms public,⁹ communicate in advance planned regulatory measures,¹⁰ open such planned regulatory measures to public

⁵ Crina Baltag and others, *Recent Trends in Investment Arbitration on the Right to Regulate, Environment, Health and Corporate Social Responsibility: Too Much or Too Little?*, ICSID Review - Foreign Investment Law Journal, 2023, 1, p. 2.

⁶ This topic was explored in more depth in a newsletter published by Nishimura & Asahi, which can be accessed at [this link](#).

⁷ EPA, Preamble.

⁸ EPA, Article 18.4.

⁹ EPA, Article 18.5.

¹⁰ EPA, Article 18.6.

consultation,¹¹ perform and publish impact assessments of such planned measures,¹² and establish of a Committee on Regulatory Cooperation.¹³ It is important to note that Article 17.7 of the EPA provides for the contracting parties' commitment to "cooperate, where appropriate, in bilateral, regional and multilateral fora on ways to promote transparency in respect of international trade and investment."

The EPA also contains various clauses providing for, among others, the contracting parties' rights to fulfil their respective legitimate or public policy objectives and their obligations under international agreements in pursuit of certain objectives such as the protection of public morals, human, animal or plant life or health, safety, the environment, financial stability, and energy security, among others.¹⁴ That said, the EPA provisions, which recognize the rights of Japan and the EU to pursue their respective legitimate policy objectives, do not specify how such rights are to be balanced against the objective of reducing or eliminating barriers to trade and investment between the two parties. Answering this question requires a careful analysis of the legal nature and legal consequences of such provisions.¹⁵

Japan and the EU have not included an investor-state dispute settlement ("ISDS") mechanism in the EPA. The EPA only contains a state-to-state dispute settlement mechanism, which applies to, among others, Chapter 8 on Investment Liberalisation and Electronic Commerce.¹⁶

However, recent global developments on ISDS in the context of economic security may provide some guidance to regulators on how to strike a balance between the right to regulate in the interest of economic security and their treaty obligations and political commitments to promote and protect foreign investments.¹⁷ We will address these developments in the second part of this newsletter.

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¹¹ EPA, Article 18.7.

¹² EPA, Article 18.8.

¹³ EPA, Article 18.14.

¹⁴ See for example Articles 4.2 para. 4, 8.1 para. 2, 8.3 para. 2, and 18.1 para. 2.

¹⁵ Lars Markert, The Crucial Question of Future Investment Treaties: Balancing Investors' Rights and Regulatory Interests of Host States, in: Marc Bungenberg, Jörn Griebel and Steffen Hindelang (eds), *European Yearbook of International Economic Law 2011*, Special Issue: International Investment Law and EU Law (Springer 2011) 150, pp. 164-167.

¹⁶ See Chapter 21 (Dispute Settlement).

¹⁷ Lars Markert, The Crucial Question of Future Investment Treaties: Balancing Investors' Rights and Regulatory Interests of Host States, in: Marc Bungenberg, Jörn Griebel and Steffen Hindelang (eds), *European Yearbook of International Economic Law 2011*, Special Issue: International Investment Law and EU Law (Springer 2011) 150, p. 158.