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The EU-Chile Advanced Framework Agreement, ISDS, and the Big Bad Dilemma

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The European Commission has published the Trade and Investment pillar of the Advanced Framework Agreement between the European Union (EU) and Chile (the Agreement), as politically concluded. This seeks to modernise the EU-Chile Association Agreement. Undoubtedly, it represents a success for the EU, as it reinvigorates its trade and investment agenda, particularly in light of Germany's recent ratification of the EU-Canada Comprehensive Economic and Trade Agreement following clarifications on the fair and equitable treatment (FET) standard. At the same time, it adds steam to the reform of the investment arbitration regime, with a view to ensuring greater rule of law standards and compatibility with state action to combat climate change.

Investment Protection and ISDS under the EU-Chile Advanced Framework Agreement

The text of the investment pillar of the EU-Chile Agreement is largely similar to agreements which the EU has concluded with Canada, Vietnam, Singapore and Mexico. Some key provisions are highlighted below.

First, in Article 10.2, the parties (which include the EU and its Member States) 'reaffirm' their right to regulate 'to achieve legitimate policy objectives', public health, education, climate change, data protection and consumer protection. Though this provision may not be actionable *per se*, it is central to the EU's approach to investment protection, as it presents the EU and its Member States' right to regulate as unrestricted in principle. This is only subject to limited exceptions by virtue of their commitments under the Agreement.

Secondly, the EU-Chile Agreement seeks to define investment protection standards in clearer terms. This would be beneficial from a legal certainty perspective, as, for instance, a breach of the FET standard would only be found to have taken place in the event there is denial of justice, a fundamental breach of due process, manifest arbitrariness, targeted discrimination or abusive treatment of investors (Article 10.15(2)). At the same time, the relatively limited scope of the FET standard allows parties to enjoy a greater degree of regulatory autonomy, without fear, save for the circumstances enumerated above, of breaching international obligations. Expropriation is similarly clarified under Article 10.17, and is not treated as impermissible if, for instance, it is carried out 'for a public purpose'.

Perhaps more boldly, the investment pillar of the EU-Chile Agreement continues the EU's long-standing efforts to reform the investor-State dispute settlement (ISDS) regime. Like previous EU-concluded agreements, it seeks to establish a bilateral Investment Court System (ICS), which arguably possesses increased rule of law safeguards. Firstly, the ICS will consist of a Tribunal of First Instance (Article 10.33) and an Appeal Tribunal (Article 10.34). The establishment of an appellate mechanism aims at enhancing consistency among arbitral awards and legal certainty with regards to the interpretation of investment protection standards. Importantly, it is envisaged to be permanent, and tribunal members will be remunerated by a monthly retainer fee as opposed to *ad hoc* payments. The above arguably aim at disincentivising the proliferation of arbitral proceedings. Secondly, members must satisfy significant expertise (Articles 10.33(4) and 10.34(4)) and ethics (Article 10.35) requirements, which approximate those found in ordinary courts and echo international discussions on arbitrators' Code of Conduct.

At the same time, the EU-Chile ICS also satisfies particular EU objectives, relating to the EU's relationship with its Member States and the autonomy of the Union legal order. Firstly, as both the EU and its Member States are parties to the Agreement, the ICS provides a mechanism for determining whether the respondent to arbitral proceedings should be a particular Member State or the Union itself (Article 10.27). This would allow the EU itself to determine who the respondent to proceedings should be, in accordance with EU law. That is, it would ensure that neither third-country investors nor arbitrators can determine, in effect, whether a policy area falls under EU or its Member States' competence. Secondly, Article 10.37 provides that the ICS tribunals would apply the Agreement itself, and relevant international law, and will only 'consider, when relevant, the domestic [including EU] law of a Party as a matter of fact', following the 'prevailing interpretation' given to it by the relevant domestic institutions. This has been accepted by the Court of Justice of the EU as constitutionally tenable in Opinion 1/17, as it does not undermine the so-called autonomy of the EU legal order (para 131). While the ICS thus clearly satisfies the above EU red line, it also ensures that the interpretative and jurisdictional integrity of Chilean law is respected.

The EU's Investment Agenda and the Great Balancing Act

The Agreement suggests that reports of the death of the EU's investment agenda are greatly exaggerated. Indeed, the EU-Chile Agreement may signal that the EU is recalibrating its strategic priorities. Broader geopolitical circumstances rather emphasised the importance of guaranteeing supply chains of sensitive raw materials, in this instance lithium. However, as far as the EU is concerned, it appears that achieving greater market access is not incompatible with a reformed investment protection framework, including the introduction of the ICS model. The Commission is thus able to claim that its reform drive does not pose an obstacle to its investment agenda, but rather constitutes a core element of it, as the EU-Chile Agreement would replace older-generation bilateral investment treaties (BITs) with 16 Member States. In simpler terms, it may be offered as an antidote to the prevailing narrative of protectionism.

However, additional objectives are also sought to be balanced, beyond institutional reform and improved market access conditions. In particular, the Agreement is accompanied by a Joint Interpretative Declaration, which emphasises that, pursuant to the Paris Agreement, the parties will adopt measures which are 'designed and applied to combat climate change or address its present or future consequences'. The investment protection provisions of the EU-Chile Advanced Framework

Agreement 'shall be interpreted and applied by the [ICS] Tribunal […] in a way that allows the Parties to pursue their respective climate change mitigation and adaptation policies'. This responds to well-known concerns regarding the appropriateness of traditional ISDS at the time of a climate crisis. Indeed, the Joint Declaration suggests that the EU-Chile Agreement and, more broadly, the ICS paradigm, is able to satisfactorily reconcile effective climate change policies with recourse to ISDS.

The above points to a challenging, multi-dimensional balancing act for the EU's investment agenda: between international engagement and protection of domestic interests; between reforms and market access; and between investment protection and climate action. The EU-Chile Agreement, and the sensitive context in which it is concluded, attempts to make sense of the Commission's conception of the EU's trade and investment policy as 'open, sustainable and assertive', which *prima facie* strikes as a contraction in terms.

Reform or Die?

It would be an understatement to note that the EU's assertive policy measures in the field of investment arbitration, particularly following *Achmea* and *Komstroy*, has been criticised, as it has pursued the termination of intra-EU ISDS on the basis of BITs and the multilateral Energy Charter Treaty (ECT). Yet, pushback against the very existence of ISDS is strong, not least because the risk of liability under investment treaties is perceived as curtailing state (and EU) ambitions to combat climate change. This has compelled several EU Member States (including Poland, the Netherlands, Spain, France, Germany, Slovenia, and Luxembourg) to exit the ECT, notwithstanding the reforms negotiated by the EU aiming at its modernisation.

Against such a background of competing criticisms that the EU is both doing too much (that is, limiting ISDS) and not enough (that is, maintaining a form of ISDS), the conclusion of the EU-Chile Agreement adds steam to efforts to reform the ISDS system. Importantly, as with similar EU-concluded agreements, Article 10.36 provides that both the EU and Chile will 'endeavor to cooperate for the establishment of a multilateral investment tribunal and appellate mechanism for the resolution of investment disputes'. This endorses, in principle, the policy proposal relating to a multilateral investment court, including a standing appellate mechanism, which is currently discussed by Working Group III of the United Nations Commission on International Trade Law.

In this sense, the Agreement is not only to be taken as a success for the EU's investment agenda, but also as a recognition that the way for the ISDS mechanism to survive is through bold reforms. Though ratification hurdles must be overcome, as the Advanced Framework Agreement requires both EU and national ratification, its conclusion suggests that the discourse on ISDS has not yet settled. Notwithstanding disagreements on particular policy directions, it now seems undisputed that reversion to traditional ISDS is not a credible option. This gives rise to the pressing if unsophisticated dilemma of 'reform or die'. In light of the substantive and institutional provisions discussed above, the EU-Chile Agreement should be welcomed by those on the reform side.

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