ALLEN & OVERY

Structuring investments in 2022 time to rethink

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Following the disruption caused by COVID-19, governments are seeking to bolster national budgets. Regulators are under pressure to look more closely at the returns earned by infrastructure assets. There is a trend towards economic nationalism in many countries. Some sectors can also expect significant regulatory intervention as the world seeks to keep '1.5 alive'.

Together, these factors may lead to a more uncertain environment for infrastructure investment globally as we move into 2022. Traditionally we have looked to investment treaties to provide protection against unlawful State intervention (whether it is licence withdrawal, tariff reform, extreme tax hikes or something else). This protection is perhaps more important than it has ever been.

At the same time, the landscape for protecting foreign investment using investment treaties has become more complex. In this document, we highlight five recent developments relevant to the protection of foreign investment in infrastructure assets. But there are ways we can help. We would be pleased to put you in touch with our market-leading team of investment-treaty specialists to discuss these issues, or more generally how investments can be structured to guard against political risk.

The European Court of Justice (ECJ) seeks to kill off arbitration of intra-EU investment disputes

On 2 September 2021, the ECJ delivered its judgment in *Republic of Moldova v Komstroy LLC* (Case No C-741/19) holding (albeit *obiter*) that intra-EU arbitration under the Energy Charter Treaty (or ECT) is incompatible with EU law (even though neither the investor nor the State was from the EU).

This decision goes a stage further than the ECJ's ruling in the *Achmea* case in 2018, which held, in a much criticised judgment, that EU investors could not have recourse to arbitration under a bilateral investment treaty (**BIT**) between two EU Member States. The ECJ said that arbitration under so-called 'intra-EU' BITs was contrary to EU law.

Until *Komstroy*, it was not clear whether the ECJ would follow the same reasoning for claims under the ECT by an EU investor against another EU Member State, not least because the EU itself is a party to the ECT, as are non-EU States. *Komstroy* shows that the ECJ is equally hostile to arbitration claims within the EU under the ECT (with a reasoning, which, much like that in *Achmea*, is unsatisfactory).

The result is, in short, a complicated one for protecting intra-EU investment. Arbitral tribunals have, to date, rejected the ECJ's position in both cases, but their awards will be hard to enforce in the EU given the ECJ's position. Now, following the *Komstroy* ruling, we even see the Netherlands seeking an injunction from the German courts to prevent German energy investors from pursuing claims against the Netherlands under the ECT.

EU investors seeking treaty protection (or investors outside of the EU that have previously structured investments in reliance on intra-EU protection under the ECT) should consider other options for protection for both existing and future investments in the EU.

We would be happy to discuss how to go about this.

The end of intra-EU bilateral investment treaties?

On 2 December 2021, the European Commission opened infringement proceedings against seven EU Member States (Austria, Sweden, Belgium, Luxembourg, Portugal, Romania and Italy) for failing to terminate their intra-EU BITs. The decision follows the ECJ's judgment in *Achmea* and the ratification by all other EU Member States (except Finland) of a multilateral treaty terminating their intra-EU BITs as of 29 August 2020. The EU Commission commenced infringement proceedings against Finland in May 2020. In essence, the European Commission is looking to eliminate all intra-EU bilateral investment treaties.

The termination of intra-EU BITs has consequences for both existing and future investments by EU investors into other EU states (and investors outside the EU who had previously structured investments in reliance on intra-EU BITs).

We can explain what other options you have to protect your investments.

The EU and the UK agree a new Trade and Cooperation Agreement

On 1 January 2021, the Trade and Cooperation Agreement between the EU and the UK provisionally entered into force. While the Agreement offers certain (limited) protections to "covered enterprises" of a UK investor in the EU (and vice versa), it does not contain a dispute settlement provision. This means that investors do not have the option of direct recourse against the EU/UK for a breach of the Agreement's provisions. Only the EU and UK can bring claims under the Agreement.

EU entities having invested in the UK should, therefore, consider other options.

We can advise you on suitable investment structures to ensure your investments are safeguarded against unlawful State intervention.

The United-States-Mexico-Canada Agreement (USMCA) replaces the North American Free Trade Agreement (NAFTA)

On 1 July 2020, USMCA entered into force replacing NAFTA. Unlike under NAFTA, under USMCA, investors from Canada do not have recourse to ISDS against the US and Mexico and investors from US and Mexico do not have recourse to ISDS against Canada (the ISDS mechanism – which is, in any event, more restrictive than under NAFTA – is limited to claims brought by investors from the US or Mexico against those States). In other words, investors from Canada in the US and Mexico and investors from the US and Mexico in Canada have no means of directly enforcing the protections offered under USMCA. Those investment protections also differ from those under NAFTA.

Annex 14-C of the USMCA permits new claims under NAFTA to be brought by investors until 30 June 2023 provided that the claims relate to "legacy investments" (those being investments acquired by investors prior to the termination of the NAFTA).

Investors holding longer-term investments, or making new investments, which would previously have relied on NAFTA may be advised to consider other structuring or restructuring options for protection.

We can discuss this with you.

The reform of investment treaties

The perception by some States that the investor-State dispute resolution system is overly favourable to investors has led to various initiatives for treaty reform. As a result, some new treaties, such as the Asia-Pacific Regional Comprehensive Economic Partnership, do not contain any investor-State dispute mechanism, while others provide for a bespoke dispute resolution mechanism different to the standard investor-State arbitration procedure (e.g. the EU-Canada Comprehensive Economic Trade Agreement), revised investment protection standards (the USMCA, as noted above), and even investor obligations (e.g. the Morocco-Nigeria BIT). The effect is a broad range of differences in the standards of protection available in different treaties and, to the extent that available treaties impose investor obligations, a potential need for enhanced due diligence (especially for brownfield investments).

In structuring an investment for protection, it is always important to consider the specific wording of the treaties available.

We can advise you on whether the scope of the protections offered is adequate, or whether alternative investment structures (which would make available different treaties) would be preferable. We can also keep you up-to-date on relevant structuring developments, including, for example, the ongoing discussions regarding the reform of the ECT.