

Japan's International Investment, Evolving Treaty Practice and Arbitration Related to Corruption and Illegality

Luke NOTTAGE/Nobumichi TERAMURA*

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I. INTRODUCTION

Japan emerged from the 1980s as one of the world's largest outbound investors. Yet inbound Foreign Direct Investment (FDI) flows and stock remain one of the lowest relative to Gross Domestic Product (GDP). This is despite formal regulations long being comparatively liberal (Part II. below) and Japan being a stable and transparent democracy with very little corruption for many decades (Part III.).

Japan was slow to expand its international investment agreement or treaty program, while its treaty drafting practice has been flexible (Part IV.1.), including regarding investor-state dispute settlement (ISDS). However, from the turn of the century it began concluding Free Trade Agreements

* Respectively: Professor, University of Sydney Law School; Assistant Professor, Institute of Asian Studies, Universiti Brunei Darussalam, Affiliate, Centre for Asian and Pacific Law at the University of Sydney (CAPLUS).

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(FTAs) mostly including Investment Chapters to both liberalise and protect cross-border investments with preferred states. In addition, Japan accelerated signings of Bilateral Investment Treaties (BITs) especially since the Second Abe Administration (2012–2020).

From around 2007, most of Japan's international investment agreements (IIAs) started to include express provisions requiring host states to address corruption. This comparatively unusual innovation may help Japan's many outbound investors, especially as they venture into less well-governed FDI destinations. By contrast, Japanese treaties remain more inconsistent in including and drafting express legality provisions (requiring covered investments to be made in accordance with host state law, or such like, to secure treaty protections). This practice may also assist Japan's outbound investors, and thus indirectly serve the national interests of Japan, as host states abroad can less likely resist ISDS arbitration claims by alleging that investments were made due to bribery or other serious investor illegality. In addition, not always including an explicit illegality provision should not be too disadvantageous for Japan directly if it instead is the host state in an inbound ISDS claim. This is because Japan has comparatively little corruption and a transparent legal regime for foreign investors, making it less likely that the latter will engage in bribery or other serious misconduct, making an express legality provision crucial for Japan as respondent state (Part IV.2.).

Japan has also been comparatively slow to experience treaty-based ISDS claims, both inbound and outbound, for various reasons (Part V.). If and when more claims arise, in particular, Japan may become an even more active player in innovating around treaty drafting impacting on corruption and ISDS arbitration (Part VI.).

II. FOREIGN INVESTMENT IN AND OUT OF JAPAN

Japan emerged as a major outbound investor from the 1980s, although it had earlier begun making investments into destinations like Australia mainly to secure long-term supplies of resources. Japan's successful exporters of manufactured goods (such as automobiles and electrical products) led to trade friction with the EU and especially USA. This prompted Japanese firms to set up factories there as well as in lower-cost manufacturing hubs such as Malaysia and Thailand.¹ Cross-border trade and related investment also increased for Japan's financial services providers, for example into

1 See generally S. HAMAMOTO/L. NOTTAGE, *Foreign Investment in and out of Japan: Economic Backdrop, Domestic Law, and International Treaty-Based Investor-State Dispute Resolution*, *Transnational Dispute Management* 8 (2011) 1.

Hong Kong and Singapore, as the Japanese economy itself also became more services-oriented, and the yen appreciated strongly (until the Plaza Accord of 1985) alongside an asset bubble (until 1990). From the 1990s, Japanese manufacturers and related firms also began investing strongly into mainland China and then Vietnam, as those economies also liberalised. Since the turn of the century, Japan has started to diversify further its FDI destinations, including into the Middle East, Africa and Latin America.² Overall, by 2021, Japan's FDI stocks abroad amounted to 37% of GDP, but inbound FDI stock was only 5%.³

As the country was rebuilt after World War II with considerable government intervention generally, Japan's FDI regulations remained very restrictive until 1980, centred on ex ante licensing for foreign capital.⁴ However, the regime was then progressively liberalised, moving to a system based primarily on ex post notification of investments. Inbound FDI began to pick up from the late 1990s amidst a banking crisis and significant deregulation of financial markets (see *Figure 1*).⁵

The Koizumi government (2001–2006), in particular, set ambitious targets to further encourage inbound FDI. The aim was to revitalise the Japanese economy that had stagnated over the 1990s after the asset bubble collapsed. But this initiative was somewhat belated and had to compete with other countries' more active and long-standing solicitation of inbound FDI, so results were mixed.

In 2020, the Foreign Exchange and Foreign Trade Act was amended to strengthen FDI screening measures to protect national security, like measures introduced in the USA and EU. Extra sectors including notably those related to information and communication technology have been added to "Designated Business Sectors" that require prior rather than ex post notification, and these are further divided into "Non-core" and "Core" sub-sectors. Foreign institutional investors are permitted "blanket exemptions" to the new prior notification requirements for both sub-sector investments if the investors do not plan to become board members or otherwise actively manage the target companies. Others, including sovereign wealth funds, might be granted a "regular exemption" after entering into a

2 JETRO, Japan's Outward FDI by Country/Region (Balance of Payments Basis, Net and Flow), Japanese Trade and Investment Statistics (2022) at https://www.jetro.go.jp/ext_images/en/reports/statistics/data/country1_e_21cy_r.xls.

3 OECD, FDI Stocks as percentage of GDP (n.d.), at <https://data.oecd.org/chart/6Y4J>.

4 R. W. RABINOWITZ, Japan's Foreign Investment Law of 1950: A Natural History (2003).

5 HAMAMOTO/NOTTAGE, *supra* note 1; B. E. ARONSON, Reassessing Japan's "Big Bang": Twenty Years of Financial Regulatory Reform, in: George/Gerteis (eds.), Japan since 1945: From Postwar to Post-Bubble (2013) 158–179.

Memorandum of Understanding with the Japanese government, but not regarding investments in the “Core” sub-sector (such as nuclear power etc.) reaching a 10% foreign investment threshold or where the foreign investor is state-owned. For all foreign investments, moreover, the threshold for the Act applying has been lowered, notably by applying the regime to acquisitions of 1% or more of equity in listed companies rather than 10%. Despite such tightening and related higher due diligence costs and possible delays for foreign investors, it is unclear whether they will be significantly adversely impacted by the Foreign Exchange and Foreign Trade Act reform.⁶

Another new law, also related to growing national security concerns and with some parallels in other jurisdictions, may also impact on the relative attractiveness of Japan as a destination for FDI. The Economic Security Promotion Act 2022 established systems for the stable supply of critical materials, stable provision of services using critical infrastructure, provision of support for the development of critical technologies and secret patent protection.⁷

Overall, as of 2020, Japan’s formal regulatory regime remained relatively more open to FDI than the average in the OECD (0.5 compared to 0.6) on the OECD FDI Restrictiveness Index.⁸ The comparatively low levels of inbound compared to outbound investment are due instead to broader regulatory and practical issues, such as labour laws and practices and other structural features of Japan’s socio-economic environment (see *Figure 2*).⁹

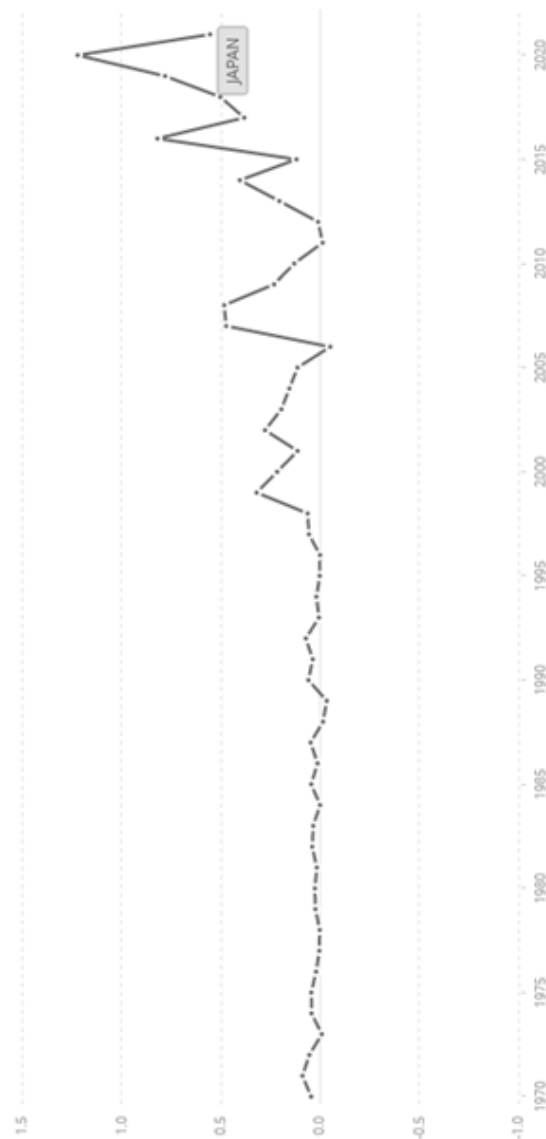
6 J. YAMAZAKI/Y. TSURUMAKI, Foreign Direct Investment: Changes in Japan, Latest Thinking (24 July 2020), at <https://www.kwm.com/au/en/insights/latest-thinking/fdi-japan.html>. Related to the COVID-19 pandemic, Designated Business Sectors have also been expanded to include e.g., ‘Manufacturing of medicines for infectious diseases and highly controlled medical devices’.

7 K. ITABASHI *et al.*, Japan: New Act on the Promotion of Japan’s Economic Security Enacted, Global Compliance News (10 July 2022), at <https://www.globalcompliance.com/2022/07/10/new-act-on-the-promotion-of-japans-economic-security-enacted240622/>.

8 OECD, FDI Restrictiveness (n.d.), at <https://data.oecd.org/chart/6Y4K>.

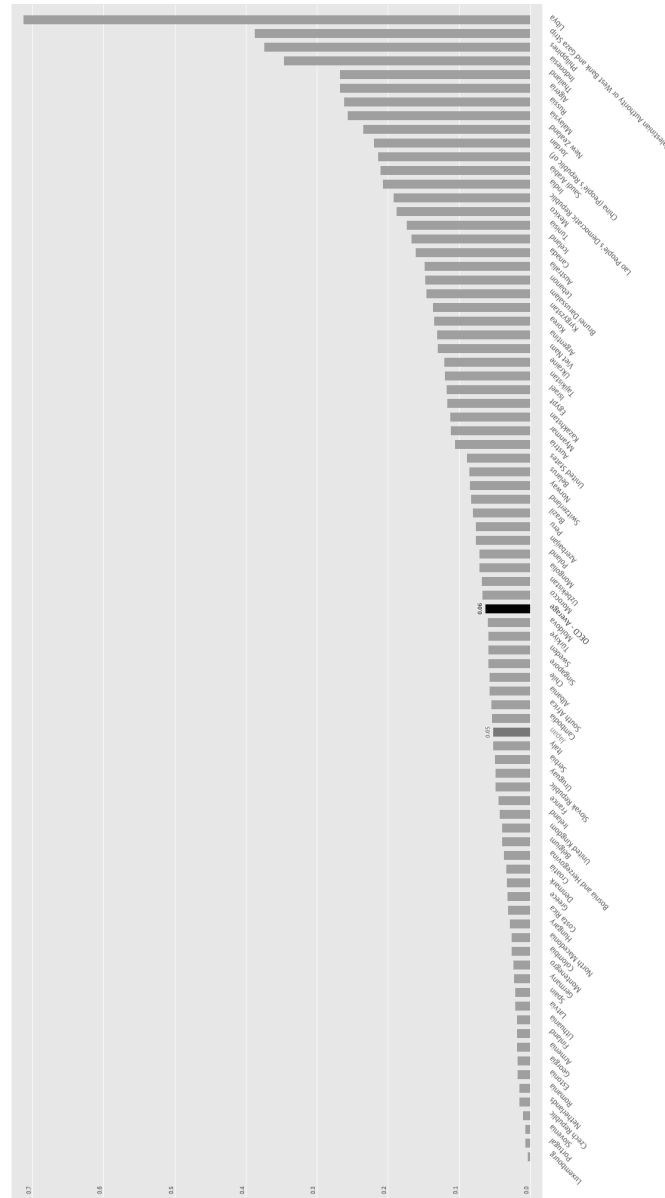
9 See generally e.g., U.S. Department of U.S.D.O. STATE, 2022 Investment Climate Statements: Japan (n.d.), at <https://www.state.gov/reports/2022-investment-climate-statements/japan/>.

Figure 1: Japan's Inbound FDI as Percentage of GDP (1970–2021)¹⁰



¹⁰ WORLD BANK, Foreign Direct Investment, Net Inflows (% of GDP) – Japan (2023), at <https://data.worldbank.org/indicator/BX.KLT.DINV.WD.GD.ZS?end=2021&locations=JP&start=1970&view=chart>.

Figure 2: Japan Compared on the OECD FDI Restrictiveness Index (2020)¹¹



11 OECD, FDI Restrictiveness. <https://data.oecd.org/chart/6Y4K>, accessed 31 January 2023.

III. CORRUPTION

Corruption and bribery are demonstrably less prevalent in Japan compared to almost all other countries in Asia. For instance, the Corruption Perception Index 2022 ranked Japan as the 5th least corrupt country in the Asia-Pacific region, after New Zealand, Singapore, Hong Kong and Australia (in that order).¹² Moreover, the World Justice Project Rule of Law Index evaluated Japan as the country with the third highest rule of law index in the East Asia and Pacific region (following New Zealand and Australia).¹³ The Index is based on various factors, such as the absence of corruption in participating countries, measured by assessing whether: (1) 'government officials in the executive branch do not use public office for private gain'; (2) 'government officials in the judicial branch do not use public office for private gain'; (3) 'government officials in the police and the military do not use public office for private gain'; and (4) 'government officials in the legislative branch do not use public office for private gain'.¹⁴ Japan obtained the 4th highest score for the overall absence of corruption factor.¹⁵

The performance of Japan in those international rankings on corruption is impressive. Yet they nevertheless imply that the country is not corruption-free (as indeed other high-achievers in Asia and beyond). As mentioned below, there are still significant prosecutions for bid-rigging and around government procurement generally in Japan, which can implicate bribery.

1. Domestic Bribery

We may classify domestic bribery in Japan into bribery of public officials, private commercial bribery and political contribution by foreign citizens or foreign companies.¹⁶ Different statutory norms apply to these three types.

First, on the bribery of public officials, Article 198 of the Penal Code¹⁷ sets out punishments for bribers. It penalises giving, offering and promising bribes to public employees with imprisonment for not more than three years or a fine not more than 2,500,000 JPY (equivalent to around 19,500 USD/

12 TRANSPARENCY INTERNATIONAL, Corruption Perception Index 2022 (2023). The Index ranked Japan the 18th least corrupt country (among 180 countries) in the world.

13 WORLD JUSTICE PROJECT, Rule of Law Index® 2022 (2022) 24.

14 WORLD JUSTICE PROJECT, *supra* note 13, at 16.

15 WORLD JUSTICE PROJECT, *supra* note 13, at 103.

16 Y. TAKAMIYA *et al.*, The Anti-Bribery and Anti-Corruption Review: Japan, The Law Reviews (8 November 2022), at <https://thelawreviews.co.uk/title/the-anti-bribery-and-anti-corruption-review/japan#:~:text=A%20person%20who%20gives%20C%20offers,to%20entities%20such%20as%20companies>.

17 刑法 *Keihō*, Act No. 45/1907.

17,000 EUR).¹⁸ ‘Public employee’ means ‘a national or local government official, a member of an assembly or committee, or other employees engaged in the performance of public duties in accordance with laws and regulations’.¹⁹ This comprises not only current public officials but also resigned and prospective public officials should they are bribed in relation to their duties.²⁰ Article 197 of the Penal Code provides penalties for bribees who are such public officers. If found guilty of accepting, soliciting or promising to accept a bribe in relation to their professional duties, their term of imprisonment is to be not more than five years.²¹ However, longer imprisonment up to seven years will apply if the current public employee has agreed to perform a specific act as per the request of the briber.

The Penal Code is silent on the definition of bribe. However, other statutory norms provide guidance on what may constitute a bribe under Japanese law. For instance, the National Public Service Ethics Act²² (NPSEA) obliges the national public officials at the headquarters of the government, who are at the rank of assistant director or higher, to report quarterly to the head of their ministry or his/her agent any gift, entertainment and other benefits of more than 5,000 JPY (around 39 USD/35 EUR) in value they have received.²³ Moreover, the National Public Service Ethics Code²⁴ (the Ethics Code) generally prohibits national public officials from accepting any gifts or benefits from their interested parties, including but not limited to those who conduct businesses under licenses or permissions or with subsidies in relation to those public officials’ duties.²⁵ Thus, the provision of any gift or benefit to civil servants could constitute bribery of national public officials under the Japanese legal system.

Secondly, certain statutes contain rules regulating private commercial bribery in specific circumstances. For instance, Article 967 of the Companies Act²⁶ provides that a corporate director who has accepted, solicited or promised to receive property benefits in relation to his or her duties is to incur imprisonment for not more than five years or a fine of not more than 5,000,000 JPY (around 38,000 USD/35,000 EUR). In contrast, the offeror of the bribe is to be imprisoned for not more than three years or fined not

18 Article 198 is applicable to those Japanese nationals who have bribed Japanese public employees abroad: Article 3(vi) of the Penal Code.

19 Article 7(1) of the Penal Code.

20 TAKAMIYA *et al.*, *supra* note 16.

21 Articles 197 and 197-3 of the Penal Code.

22 国家公務員倫理法 *Kokka kōmu-in rinri-hō*, Act No. 129/1999.

23 Article 6(1) of the NPSEA.

24 国家公務員倫理規程 *Kokka kōmu-in rinri kitei*, Cabinet Order No. 101/2000.

25 Articles 2(1) and 3 of the Ethics Code.

26 会社法 *Kaisha-hō*, Act No. 86/2005.

more than 3,000,000 JPY (around 23,300 USD/21,000 EUR). Similar penalties apply to shareholders who have accepted, solicited or promised to accept property benefits concerning their rights as shareholders and those who have offered or promised to offer the benefits (Article 968 of the Companies Act). Depending on the facts and circumstances, private commercial bribery may fall within other criminal offences, such as breach of trust under Article 24 of the Penal Code.

Thirdly, the Political Funds Control Act²⁷ prohibits politicians from accepting political contributions from foreign persons, entities, associations or any other organisations whose majority members are foreign persons or entities (excluding Japanese entities listed consecutively for not less than five years).²⁸ Those who have committed this offence would be punished with imprisonment for not more than three years or a fine of not more than 500,000 JPY (around 3,900 USD/3,500 EUR).²⁹ However, no obvious rule imposes a penalty to foreigners and foreign entities who have offered or have promised to offer political contributions to Japanese politicians.

Overall, Japanese law is therefore rigorous concerning the bribery of public officials, private commercial bribery and political contributions by foreign citizens or foreign companies (albeit less comprehensively so perhaps for that last type). However, high-profile corruption cases have been reported from time to time. A notorious example historically was the Lockheed bribery scandal over the 1970s and 1980s, in which Kakuei TANAKA was eventually found guilty of accepting bribes over All Nippon Airways' purchase of commercial aircrafts from the Lockheed Corporation during his tenure as Prime Minister.³⁰ In 2021, the Tōkyō District Court convicted another parliamentarian, Tsukasa AKIMOTO, for bribery charges. This concerned 500.com, a Chinese gambling company,³¹ which reportedly bribed several parliamentarians to obtain permission to open casinos in Japan.³²

27 政治資金規正法 *Seiji shikin kisei-hō*, Act No. 194/1948, as amended by Act No. 135/2007.

28 Article 22-5.

29 Article 26-2(3).

30 M. M. CARLSON, Corruption, Leadership, and the Limits of Political Reform in Japan, *Public Administration and Policy* 25 (2022) 124.

31 M. YAMAGUCHI, Japan Ex-Official Gets Prison Term in Casino Bribery Case, AP News (7 September 2021), at <https://apnews.com/article/business-japan-9fb4b85edbfb1b55ceb076340acc314>.

32 M. POLLMANN, Foreign Bribery Scandal Muddies Japan's Casino Legalisation Gamble, *The Diplomat* (10 January 2020), at <https://thediplomat.com/2020/01/foreign-bribery-scandal-muddies-japans-casino-legalization-gamble/>; D. AKIMOTO, Power and Money in Japanese Politics, *The Diplomat* (13 February 2020), at <https://thediplomat.com/2020/02/power-and-money-in-japanese-politics/>.

More recently, the Japan Times reported on 21 October 2022 that “[t]he Tokyo Olympics bribery scandal, centred on a key former Dentsu executive and Tokyo [Olympics] Organising Committee member, continues to expand with no end in sight”.³³ Therefore, domestic corruption is still occasionally an on-going problem for Japan.

2. *Foreign Bribery*

Japan ratified in 1998 the OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions (the OECD Convention). The country then amended the Unfair Competition Prevention Act³⁴ (UCPA), to criminalise bribery of foreign public officials. In particular, Article 18(1) of the UCPA provides that:

“No person may give, or offer or promise to give, any money or other benefit to a Foreign Public Official, etc. in order to have them act or refrain from acting in relation to the performance of official duties, or in order to have the Foreign Public Officials, etc., use their position to influence another Foreign Public Official, etc. to act or refrain from acting in relation to the performance of official duties, in order to make any wrongful gain in business with regard to international commercial transactions.”

“A Foreign Public Official, etc.” means virtually anyone who engages in public service for a foreign national or local government or international organisation, and who participates in business affairs involving the interest of such a government or organisation.³⁵ “International commercial transactions” comprise economic activities beyond national borders such as cross-border trade and foreign investment.³⁶ Therefore, the UCPA bars Japanese individuals from bribing any persons working for the public interest of a foreign government or international organisation, in relation to their business operations.

As a penalty for foreign bribery, a person who has violated Article 18(1) of the UCPA is to be punished with imprisonment with labour for not more than five years or a fine not exceeding 5,000,000 JPY (around 38,000 USD/35,000 EUR) or both.³⁷ Moreover, if the person is a representative, agent, employee or any other staff member of an entity, and if s/he has committed the offence in relation to the entity’s business operation, the entity is also to be penalised with a fine of not more than 300,000,000 JPY (around

33 E. JOHNSTON, Tokyo Olympics Bribery Scandal: Investigation Ensnarers Stuffed-Toy Maker and Ad Firms, The Japan Times (21 October 2022), at <https://www.japantimes.co.jp/news/2022/10/21/national/tokyo-olympics-bribery-scandal-explainer/>.

34 不正競争防止法 *Fusei kyōsō bōshi-hō*, Act No. 47/1993.

35 Article 18(2) of the UCPA.

36 TAKAMIYA *et al.*, *supra* note 16.

37 Article 21(2) of the UCPA.

2,300,000 USD/2,000,000 EUR). These penalty provisions do suggest that Japan adopts a tough stance towards foreign bribery.

In fact, over the years, the courts in Japan have indeed found a number of Japanese businesspersons and entities guilty of committing bribery of public officials – across the Philippines, Vietnam, China, Indonesia, Thailand and Uzbekistan.³⁸ Nevertheless, the OECD's report in 2019 was critical of Japan's efforts and capacity to detect foreign bribery. It claimed that '[o]nly 46 foreign bribery allegations involving Japanese nationals and companies have been uncovered [between 1999 to 2019]', suggesting that the number is 'particularly low given the size of Japan's economy and its exposure to high-risk countries and sectors'.³⁹ In addition, Transparency International's recent 14th report independently assessing enforcement of the OECD Anti-Bribery Convention, based on investigations and cases prosecuted between 2018 and 2021, puts Japan in the bottom tier of 20 out of 47 jurisdictions. This tier is characterised as having "little or no" enforcement, including also China and Hong Kong, South Korea and Singapore among other major exporters.⁴⁰

IV. INVESTMENT TREATY PRACTICE AND INNOVATIONS⁴¹

1. *Japan's Investment Treaty Practice Generally*

Japan's treaty program has unfolded in several phases: (i) limited and varied BITs through to around 2001, (ii) more expansive and consistent BITs plus some FTAs (influenced by US-style drafting) from 2002, and (iii)

38 TAKAMIYA *et al.*, *supra* note 16.

39 OECD, Implementing the OECD Anti Bribery Convention – Phase 4 Report: Japan (2019), at <https://www.oecd.org/corruption/OECD-Japan-Phase-4-Report-ENG.pdf>.

40 TRANSPARENCY INTERNATIONAL, Exporting Corruption (2022) at <https://www.transparency.org/en/publications/exporting-corruption-2022>, 58. It found Japan had only commenced two investigations and two prosecutions, concluding two cases with sanctions between 2018 and 2021. However, Transparency International also noted that enforcement activity had dropped world-wide over this period, linked to (but sometimes pre-dating) the COVID-19 pandemic. The comparative report also does not try to measure the extent to which low enforcement may be due to generally low levels of foreign corruption undertaken anyway by firms within that jurisdiction. The latter may arguably be correlated with their own data on perceptions of corruption in each jurisdiction, which is very low for Japan, although it is also possible that Japanese firms rarely bribe domestically but do so more in their overseas ventures.

41 This Part updates and adapts part of L. NOTTAGE, International Commercial and Investor-State Arbitration: Australia and Japan in Regional and Global Contexts (2021) 297–306. See also generally the coding of substantive protections and procedural rights, as well as brief commentary on Japan's investment treaties, in

comparatively active and somewhat more consistent conclusion of both type of treaties especially since 2013.

First, between 1978 and 2001, Japan signed only eight standalone BITs, despite its growing outbound FDI presence and the global proliferation of BITs from the 1990s, and Japan seems to have been more reactive or even “passive” in responding to drafting proposals from the various counterparties.⁴² The paucity and variety of BITs reflected Japan’s preference for multilateral initiatives, partly to protect itself against bilateral pressures, notably from the US and then the EU, over their respective trade deficits with Japan. Consistently with this general preference, Japan was one of the relatively few non-European or Central Asian states to sign in 1994 the multilateral (but sector-specific) Energy Charter Treaty (ECT).

As a second phase, after the collapse of negotiations in 2000 for a new World Trade Organization (WTO) round that aimed to add extra investment commitments multilaterally, following the suspension of negotiations in a few years earlier for the OECD’s Multilateral Agreement on Investment, Japan started to conclude FTAs. It experimented first with Singapore (signed in 2002), then concluded 12 more FTAs through to the end of 2012. Most of these FTAs focused on Asia, where Japan was concentrating much trade and investment, and it also concluded a trilateral investment treaty with China and Korea (supplementing earlier BITs). Japan also kept signing standalone BITs over this period (ten through to 2012, but with FTAs with Vietnam and Peru folding in their BITs) with Asia-Pacific states. These BITs also began to include pre-establishment National Treatment (market access liberalisation) commitments, not just protections for investments once made (as in the first phase of BITs). Influenced by the drafting of largely US-style drafting, Japan’s “new generation” BITs were epitomised by the Cambodia-Japan BIT signed in 2007.⁴³ Japan’s more active and consistent negotiation and drafting of international investment agreements, despite not publicising a Model BIT like many other large economies, was also prompted by Japan’s balance on investment (earnings from overseas investment) basically equalling its balance on goods (net income from goods and services) by 2001, and then the acceleration of ISDS cases world-wide.

L. MARKERT/S. ISHIDO, *Investment Treaty Arbitration: Japan*, *Global Arbitration Review* (29 July 2022), at <https://globalarbitrationreview.com/insight/know-how/investment-treaty-arbitration/report/japan#69C2CE75910EBC3DA967DBB6666172352881A7DE>.

42 S. HAMAMOTO, *A Passive Player in International Investment Law: Typically Japanese?*, in: Bath/Nottage (eds.), *Foreign Investment and Dispute Resolution Law and Practice in Asia* (2011) 53–67.

43 S. HAMAMOTO/L. NOTTAGE, *Japan*, in: Brown (ed.), *Commentaries on Selected Model Investment Treaties* (2013) 347–392.

In the third phase after Prime Minister Shinzo ABE won a general election in late 2012, Japan signed even more BITs (18 through to 2022) extending also to emerging or prospective investment destinations in Central Asia, the Middle East and Africa. FTA signings were fewer. Bilateral FTAs were concluded with Australia (2014) and Mongolia (2015), but Japan also then signed mega-regional treaties. These were the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), an FTA with the EU combined with a parallel investment (but only for liberalisation commitments with inter-state arbitration), and the Regional Comprehensive Economy Partnership (“ASEAN+5” RCEP).

In ISDS reform discussions multilaterally through the United Nations since late 2018 and to “modernise” the ECT, Japan has emerged (with other large net capital exporting states) as a proponent of targeted improvements rather than wholesale change. As evident also by not concluding an investment protection agreement with the EU, Japan has resisted even the EU’s hybrid “investment court” procedure, which allows the foreign investor still to initiate a direct arbitration claim against the host state, but with the latter plus home state pre-selecting “judges” assigned then randomly to hear the claim and any appeal for serious error of law or even fact.

Even in the second and third phases, Japan has been quite flexible in its IIA negotiations and drafting. For example, its FTA with the Philippines signed in 2006 did not provide for ISDS, although Japan typically presses for and achieves this procedure enhancing protections for its outbound investors. This seems to have been due to the latter’s early experience resisting inbound ISDS arbitration claims, and probably also helps explain why Japan’s FTA with the Association of Southeast Asian Nations (ASEAN) signed initially in 2008 exceptionally omitted an investment chapter altogether.

Yet Japan by then had signed BITs and/or FTAs providing for ISDS-backed commitments with almost all other ASEAN member states, and Japan then negotiated an investment treaty with Myanmar in 2013 (after its partial regime change) as well as later renegotiating the ASEAN FTA to include an investment chapter with ISDS. Similarly, Japan took the long view in negotiating its FTA with Australia, omitting ISDS upon signing in 2014 (largely due to Australian domestic politics) but obtaining ISDS-backed commitments anyway after the CPTPP came into force from 2019. Japan was also likely agreeable to RCEP omitting ISDS (for now), as it is mostly available anyway under at least one investment treaty signed by Japan (and indeed among almost all pairs of RCEP member states⁴⁴).

44 L. NOTTAGE/B. JETIN, *New Frontiers in Asia-Pacific Trade, Investment and International Business Dispute Resolution*, in: Nottage *et al.* (eds.), *New Frontiers in Asia-Pacific International Arbitration and Dispute Resolution* (2021) 1–38.

Likewise for substantive provisions, even over the last decade during the third phase, Japan's BITs and FTAs still display significant diversity.⁴⁵ For example, most Japanese treaties include pre-establishment (liberalising) National Treatment and Most-Favoured Nation treatment as well as prohibitions on performance requirements; but such liberalisation commitments are missing from the BITs with Papua New Guinea (signed in 2011), trilaterally with China and Korea (2012), Saudi Arabia (2013) and some others. Not all treaties providing for post-establishment protection expressly define investors to include those who 'seek to make' investments (as well as those who are 'making' or have 'made' investments). Japan's recent treaties adopt a broad US-style definition of 'investment', but they differ for example regarding express references to public debt. Commitments around Fair and Equitable Treatment are still worded in various ways (sometimes but not always including references to the customary international law standard). Umbrella clauses are included in the trilateral investment treaty (signed in 2012) and the BIT with Myanmar but not in Japan's BIT with Saudi Arabia.

Japan's recent treaties more consistently add a US-style definition of indirect expropriation, which first appeared in the BIT with Peru (2008). They also have started to add commitments by host states not to lower regulatory standards when promoting inbound investments, regarding protection of the environment (mentioned in the trilateral treaty with China and Korea) but also often for the protection of public health and safety.

ISHIKAWA, reflecting also on her experience in Japan's investment treaty negotiations, suggests that such variations, albeit framed around a largely US-style treaty template since the turn of the 21st century, may be due to Japan not publishing a Model BIT, but are more importantly due to:⁴⁶

- 'the relative bargaining power of the negotiating parties, which is influenced by the strength of the government of the time;
- the existence of a pressing need for early conclusion of the treaty; and
- the economic and political situations of both negotiating parties.'

Overall, HAMAMOTO observes that Japan tends now to include 'pro-investor provisions in treaties concluded with states from which Japan re-

45 See especially S. HAMAMOTO, *Debates in Japan over Investor-State Arbitration with Developed States*, CIGI (Centre for International Governance Innovation) Investor-State Arbitration Series (2016) at https://www.cigionline.org/static/documents/isa_paper_no.5.pdf (with a version also in DE MESTRAL (ed.), *Second Thoughts: Investor-State Arbitration between Developed Democracies* (2017)).

46 T. ISHIKAWA, *A Japanese Perspective on International Investment Agreements: Recent Developments*, in: Chaisse/Nottage (eds.), *International Investment Treaties and Arbitration across Asia* (2018) 513–543.

ceives a small amount of investment'.⁴⁷ By contrast, with the CPTPP and the trilateral treaty with China and Korea for example, Most-Favoured Nation clauses are made expressly inapplicable to ISDS, indirect expropriation provisions have detailed restrictions, and umbrella clauses were limited (in the trilateral treaty) and omitted in the CPTPP.

2. *Japan's Treaty Provisions Impacting on Corruption and Illegality*

a) *Anti-Corruption Obligations on States*

Despite such ongoing variability in Japan's recent international investment agreements, reflecting arguably the negotiating dynamics and underlying economic interests, it is notable that, beginning with its BIT with Cambodia signed in 2007, we find often a provision along the following lines (Article 10):

"Each Contracting Party shall ensure that measures and efforts are undertaken to prevent and combat corruption regarding matters covered by this Agreement in accordance with its laws and regulations."

A mostly identical and occasionally similar provision is contained in Japan's BITs with 22 out of 26 BITs signed by Japan since 2007, suggesting Japan is the party regularly pressing for them. The wording is also in the BITs with Laos, Uzbekistan and Peru in 2008, Papua New Guinea and Colombia (2011), Kuwait and Iraq (2012), Myanmar and Mozambique (2013), Kazakhstan (2014), Ukraine, Uruguay and Oman (2015), Armenia, United Arab Emirates, Argentina,⁴⁸ and Jordan (2018), Cote d'Ivoire and Morocco⁴⁹ (2020), Georgia (2021) and Bahrain (2022).⁵⁰ The provision is omitted only in the BITs with Saudi Arabia (2013), Iran and Kenya (2016)

⁴⁷ HAMAMOTO, *supra* note 45, 8.

⁴⁸ Cf T. GAZZINI, Second Generation IIAs: Japanese Perspective, Kluwer Arbitration Blog (12 March 2022), at <https://arbitrationblog.kluwerarbitration.com/2022/03/12/second-generation-ii-as-japanese-perspective/>, asserting (emphasis added):

"Unlike some recent treaties, such as ECOWAS Supplementary Act or the Canadian European Treaty Agreement (CETA), *the treaty between Japan and Argentina remains almost silent on non-investment issues* and thus ignoring one of the main sources of criticism moved against investment agreements. This is unsatisfactory for two main reasons. On the one hand, the treaty could have rebalanced the relationship between investors and the Host State by introducing some obligations upon the former, especially regarding social and environmental impact, *corruption* and corporate governance. On the other hand, a modern investment treaty cannot neglect the interests and rights of other stakeholders."

⁴⁹ However, the Morocco BIT (Art. 7) somewhat waters down the provision further by specifying that the states "shall endeavour: to ensure that measures and efforts are undertaken to prevent and combat corruption".

and Israel (2017), with the first three of these not scoring well on indices measuring corruption.⁵¹ Similarly for other international investment agreements, we find this provision in bilateral FTAs with the Philippines (2006) then Thailand (2007), India and Peru (2011) and Mongolia (2015), and quite similarly in the RCEP (Art 17.9) as well as a rather different variant in the investment treaty with the United Kingdom (2020, Art 17.9) and an entire chapter 26 on “transparency and anti-corruption” in the CPTPP.⁵² Yet Japan’s preferred anti-corruption provision is completely omitted in Japan’s FTAs with Brunei (2007), Vietnam (2008), even Switzerland (2009) and the trilateral investment treaty with China and Korea (2012).

Arguably, negotiating counterparties with higher levels of domestic corruption are reluctant to include this sort of provision when pressed by Japan as they fear that it could bolster ISDS claims by Japanese investors based on violations of Fair and Equitable Treatment commitments. Another concern could be that this provision requires them as host states to more actively enforce anti-corruption laws, even though the wording “measures and efforts” can be interpreted quite restrictively and they depend on what “laws and regulations” are (re)enacted by the host state. The provision may also be resisted because it does not help much in resisting an ISDS arbitration claim if there is suspected bribery. This is because it does not impose directly any obligations on foreign investors not to engage in corrupt practices, even though some other provisions may arguably require or imply this (for example through complying voluntarily with CSR standards, or the express legality provisions analysed below). Overall, Japan’s comparatively unusual innovation in seeking to incorporate this sort of anti-corruption requirement in almost all its BITs since 2007, as well as (less successfully) in other international investment agreements, is consistent with its position as a large net FDI exporting state.

b) Explicit Legality Requirements on Foreign Investors

Japan’s IIA practice regarding express legality provisions is more complex, but also arguably favours its outbound investor interests. ISDS tribunal

50 Texts of these BITs and FTAs with investment chapters can be found via UNCTAD, International Investment Agreements Navigator: Japan (n.d.), at <https://investmentpolicy.unctad.org/international-investment-agreements/countries/105/japan>.

51 In 2021 Saudi Arabia was ranked 54 world-wide for resisting corruption, but Iran was ranked 147 and Kenya ranked 123, compared to Israel ranked 31: TRANSPARENCY INTERNATIONAL, *supra* note 12.

52 See generally e.g., Y. YAN, The Inclusion of Anti-Corruption Clauses in International Investment Agreements and Its Possible Systemic Implications, *Asian Journal of WTO & International Health Law and Policy* 17 (2022) 141.

rulings and authoritative commentary show that such a provision is crucial to defending a claim where the investor has allegedly engaged in bribery or other serious illegal behaviour. Treaties without such provisions make it much harder for the tribunal to decline jurisdiction overall or even deem some claims inadmissible, although there may still be scope to find for the host state on the merits or at least reduce damages or other relief sought due to proven investor misconduct.⁵³ Yet Japan's international investment agreements have only gradually started to make such provisions explicit. Instead, we find four types of provisions.

First, BITs from the first phase, such as the pioneering BIT with Egypt (1977, Article 2.1), include instead a provision such as this:

"Each Contracting Party shall within its territory promote as far as possible investment by nationals and companies of the other Contracting Party and admit such investment in accordance with the applicable laws and regulations of the former Contracting Party."

This does not expressly put any obligation on the foreign investor to make (let alone operate) investments in accordance with the host state's laws, including those against corruption, in order to benefit from treaty protection for covered investments. Accordingly, the UN Conference on Trade and Development (United Nations) codes this BIT as not containing an express "in accordance with host State laws" requirement.⁵⁴ The same applies for Japan's ensuing three BITs, with Sri Lanka (1982), China (1988) and Turkey (1992).

By contrast, its BIT with Hong Kong (1997) is coded as containing the legality requirement for treaty protection,⁵⁵ and this does indeed seem more implicit in a second type of provision found in Article 10:

53 See generally C. REICHENBACH, *The Corruption Defence and the Jurisdictional Consequences of Corruption Allegations in International Law and Investment Arbitration*, in: Sachs *et al.* (eds.), *Yearbook on International Investment Law & Policy* 2020 (2022); N. TERAMURA *et al.*, *Bribery and Other Serious Investor Misconduct in Asian Investment Arbitration*, in: Teramura *et al.*, *supra* note *, with manuscript available via <https://japaneselaw.sydney.edu.au/2022/03/corruption-and-illegality-in-asian-investment-arbitration/>.

54 UNCTAD, *International Investment Agreements Navigator: Egypt – Japan BIT (1977)* (n.d.), at <https://investmentpolicy.unctad.org/international-investment-agreements/treaties/bilateral-investment-treaties/1358/egypt---japan-bit-1977->. See also A. REINISCH, *How to Distinguish 'in Accordance with Host State Law' Clauses from Similar International Investment Agreement Provisions?*, *Indian Journal of Arbitration Law* 7 (2018) 70. However, in *Fynderdale Holding BV v The Czech Republic* (PCA Case No. 1018-18, Award of 29 April 2021, <https://www.italaw.com/cases/4750>) at paragraphs 553–554, the tribunal interpreted a similar provision (Article 2) of the Dutch/Czechoslovakia BIT (1992) as requiring investments to be legal to qualify for treaty protection.

“This Agreement shall apply to all investments and returns of investors of one Contracting Party made within the area of the other Contracting Party in accordance with the applicable laws and regulations of the other Contracting Party, whether made before, on or after the date of entry into force of this Agreement.”

The BITs signed with Bangladesh, Pakistan and Russia (1998) revert to the wording of the 1977 BIT with Egypt. But the BIT with Mongolia (2001) – and many others subsequently – include only a provision such as Article 9, constituting a third form of wording:

“The present Agreement shall also apply to all investments and returns of investors of either Contracting Party acquired within the territory of the other Contracting Party in accordance with the applicable laws and regulations of such other Contracting Party prior to the entering into force of the present Agreement.”

The United Nations codes such a provision as not constituting an express “in accordance with host State laws” requirement.⁵⁶ It is admittedly not as arguable as in Article 10 of the Hong Kong BIT, and the United Nations coding may be influenced by the Article 1(1) of the Mongolia BIT (and others subsequently) not adding an “in accordance with laws” provision to the definition of covered “investments”. However, it could be contended that this provision does amount to a legality requirement, because it would make little sense to cover past investments (before the treaty came into force) only if made in accordance with host state laws, yet cover foreign investments made afterwards even in violation of host state laws.

The clearest and most explicit legality provision appears initially in Japan’s BIT with Iran (2016), in the third phase outlined in Part IV.1. above, specifically in the definitional Article 1.1:

“Article 1.1: The term “investment” refers to every kind of asset, invested directly or indirectly by an investor of a Contracting Party in the Territory of the other Contracting Party in accordance with the laws and regulations of the other Contracting Party, including the following: ... “.

The United Nations codes this fourth type of provision as an explicit legality provision, and a similar provision is found in most subsequent BITs, namely with Israel (2017), Jordan and Argentina (2018), Morocco (2020) and Georgia (2021). But this formulation is not found in the BITs with

55 UNCTAD, International Investment Agreements Navigator: Hong Kong, China Sar – Japan BIT (1997) (n.d.), at <https://investmentpolicy.unctad.org/international-investment-agreements/treaties/bilateral-investment-treaties/1865/hong-kong-china-sar---japan-bit-1997->.

56 UNCTAD, International Investment Agreements Navigator: Japan – Mongolia BIT (2001) (n.d.), at <https://investmentpolicy.unctad.org/international-investment-agreements/treaties/bilateral-investment-treaties/2153/japan---mongolia-bit-2001->.

Armenia and UAE (2018) and Cote d'Ivoire (2020, Article 27(3)) reverting instead to the third type of wording as in the 2001 BIT with Mongolia mentioned above) or Japan's most recent BIT with Bahrain (2022, reverting to the first type above similar to Japan's pioneering 1977 BIT with Egypt).

Legality provisions in Japan's other international investment agreements are also variable or quite often missing altogether. For example, the trilateral investment treaty with China and Korea (2012) has only the first type of formulation. The Energy Charter Treaty (1994) had no explicit provision, although the 2022 "modernised" version being assessed by member states amidst considerable controversy does add that it covers energy-related investments "made or acquired in accordance with the applicable laws" of the host state.⁵⁷

The first of Japan's many FTAs with an explicit legality requirement is that signed with Indonesia (2007), with Article 58(f) stating that:

"the term "investments" means every kind of asset invested by an investor, in accordance with applicable laws and regulations, including, though not exclusively [...]"

The FTA with India (2011) instead states in Article 83.2:

"An investor of a Party whose investments are not made in compliance with the laws and regulations of the other Party which are consistent with this Agreement shall not be entitled to submit an investment dispute to conciliations or arbitrations referred to in paragraph 4 of Article 96."

The latter article provides for ISDS. Even if an ISDS arbitration tribunal loses jurisdiction to resolve a dispute where the foreign investment is shown to be tainted by corruption, however, an inter-state arbitration tribunal presumably may consider investment disputes under Chapter 14 (Articles 133–142).

Among Japan's regional FTAs, although adding ISDS is to be further discussed (Article 10.18), the RCEP does already include an explicit legality provision in Article 10.1(a):

"covered investment means, with respect to a Party, an investment in its territory of an investor of another Party in existence as of the date of entry into force of this Agreement or established, acquired, or expanded thereafter, and which, where applicable, has been admitted, by the host Party, subject to its relevant laws, regulations, and policies".

Overall, how should we assess this greater disparity in Japan's international investment agreement drafting – even in quite recent treaties – regarding a clearly expressed legality requirement? These are most likely to benefit

57 See revised Article 1(6) and generally T. FISHER, *The Modernised Energy Charter Treaty: The New Text*, Kluwer Arbitration Blog (15 October 2022), at <https://arbitrationblog.kluwerarbitration.com/2022/10/15/the-modernised-energy-charter-treaty-the-new-text/>.

states that are less well governed and suffer more corruption than Japan. Accordingly, we would expect such counterparty states to press for them, although some (more developing) countries may still not be so familiar with the intricacies of international investment treaties and therefore may not be able to realise these provisions' importance or lack the negotiating power to press for them.⁵⁸

It seems that Japan either was not so aware of the provision's significance or, more plausibly given its extensive experience in negotiating treaties especially over the last decade or two, that it was not pressing as hard for an explicit legality provision in treaties even recently. Furthermore, the outcome and patterns outlined above would arguably be in Japan's overall national interest, given that it remains overwhelmingly a net capital (and especially FDI) exporter, including into many poorly governed states. The paucity or variability of explicit legality provisions could therefore assist Japan's outbound investors, if host states resist ISDS arbitration claims by alleging that investments were made due to bribery or other serious investor illegality. At the same time, not always including an explicit illegality provision should not be too disadvantageous for Japan if it instead is the host state in an inbound ISDS claim. This is because Japan has little corruption, and a transparent legal regime for foreign investors. Accordingly, they should less likely engage in bribery or other serious misconduct, so Japan will have less need to invoke an explicit legality provision to resist the inbound claim.

V. INVESTMENT ARBITRATION CASES INVOLVING JAPAN

The somewhat cynical perspective on Japan's investment treaty practice regarding the quite limited incorporation of explicit legality provisions depends on the extent to which there are outbound and especially inbound treaty-based ISDS claims. If many foreign investors commence ISDS arbitration claims against Japan, more opportunities arise for Japan as host state to want to assert a defence based on bribery or (more likely) other serious illegality on the part of the investor, and such a defence will become much more effective if explicit legality provisions are contained in the relevant treaties.

58 On how sophisticated developing countries have been when negotiating treaties, compare with more pessimistic view of Lauge POULSSON with the view (linked to some seemingly careful treaty drafting around ISDS by Thailand) of L. NOTTAGE, *Rebalancing Investment Treaties and Investor-State Arbitration: Two Approaches*, *Journal of World Investment and Trade* 17 (2016) 1015; L. NOTTAGE, *Rebalancing Investment Treaties and Investor-State Arbitration in the Asian Region*, in: Mohan/Brown (eds.), *The Asian Turn in Foreign Investment* (2021) 379–398.

However, in practice, there is only one known inbound ISDS treaty-based claim against Japan, filed by Shift Energy Japan KK in 2020 under the 1997 BIT with Hong Kong.⁵⁹ As this is not one of Japan's newer treaties (increasingly building in transparency provisions around ISDS), but instead only providing for United Nations Commission on International Trade Law Arbitration Rules filings, there is almost no public information available. On 3 February 2021 one commercial reporting service stated that the case seems to be in relation to measures taken by Japan.⁶⁰

"[...] in the renewable energy capacity sector [...] initiated by two Hong Kong entities active in the solar energy sector. A tribunal is fully constituted to hear the claim [...].

Japan introduced a subsidy program to support renewable energy with feed-in tariffs in 2012. Since that time, however, the state has gradually scaled back the tariffs' levels – which reached a reported two-thirds of their initial levels following the most recent changes [...]. Industry reporting suggests that photovoltaic firms operating in Japan have been financially challenged as a result of the steady decrease in the levels of tariffs.

To date, Japan has yet to publicly acknowledge the new arbitration claim or divulge further details about it. It is also unclear if the country faces additional such claims, either in the renewable energy sector or in other contexts.

The country has been one of the more avid pursuers of new investment treaties over the last two decades, signing more than 25 new treaties (and negotiating others) in that span. [...] Japan has been a conservative voice in the ongoing ISDS reform discussions at the United Nations Commission on International Trade Law and in the context of the Energy Charter Treaty modernization negotiations, with the country often downplaying the extent of problems with investment treaties, and stressing the bilateral tools and drafting techniques that can be used by concerned states to address any perceived problems (while opposing a sweeping multilateral set of reforms).

With the country now facing at least one investment treaty arbitration, it remains to be seen what impact, if any, this will have on Japan's treaty practice and its posture in reform discussions."

On 3 March 2021 the service further reported that Japan's first inbound claim was:⁶¹

59 UNCTAD, Investment Dispute Settlement Navigator: Shift Energy V. Japan (n.d.), at <https://investmentpolicy.unctad.org/investment-dispute-settlement/cases/1194/shift-energy-v-japan>.

60 IAREPORTER, Japan Faces Its First Known Investment Treaty Arbitration, as UNCITRAL Tribunal Is Quietly Put in Place to Hear Asian Energy Investors' Claims, Investment Arbitration Reporter (3 February 2021), at <https://www.iareporter.com/articles/japan-faces-its-first-known-investment-treaty-arbitration-as-uncitral-tribunal-is-quietly-put-in-place-to-hear-asian-energy-investors-claims/>.

61 IAREPORTER, Identity of Hong Kong-Based Investor Bringing First Treaty-Based Claim against Japan Is Revealed; Names of Arbitrators Also Come to Light, Investment Arbitration Reporter (3 March 2021), at <https://www.iareporter.com/articles/identity-of-hong-kong-based-investor-bringing-first-treaty-based-claim-against-japan-is-revealed-names-of-arbitrators-also-come-to-light/>.

“initiated by a pair of claimants related to a Hong Kong entity, Shift Energy. The arbitration is proceeding under the United Nations Commission on International Trade Law Arbitration Rules, but it is being administered by the International Centre for the Settlement of Investment Disputes. We have further confirmed that a tribunal is already in place to hear the claims: Andres Rigo Sureda is sitting as chair, while the parties nominated Stanimir Alexandrov (claimants’ appointee) and Zachary Douglas (Japan’s appointee). The case is still at an early stage and no hearing has yet been held on jurisdictional or merits questions. The claimant is represented by DLA Piper, while Japan relies on counsel from Foley Hoag.”

A short commentary on 11 March 2023, focusing on a successful outcome in an outbound claim by a Japanese investor, mentions (without further details) that Japan has successfully defended this inbound claim brought by Shift under the Japan-Hong Kong BIT.⁶²

Over the last few years since this case was filed, there seem to have been no further inbound claims and Japan has not backtracked from its comparatively active promotion of ISDS-backed international investment agreements over the last decade (as outlined in Part IV.1. above). The Japanese government also does not have a tradition of negotiating investment treaties with foreign investors, as in other (more developing) countries in Japan, which might include an arbitration clause generating a contract-based claim. Until there is significantly more FDI into Japan, particularly into sensitive sectors where foreign investors are more likely to suffer loss, and there are more inbound ISDS claims under treaties, we may continue to see Japan not pressing hard for consistent and clear express legality provisions in their international investment agreements.

However, if counterparties themselves start pressing for such provisions, Japan may well include them given its longstanding tradition of being quite open to proposals and related rewording of its treaty provisions (as also noted in Part IV.1. above) and/or to maintain public trust in the ISDS-supported system of international investment law. This shift towards more explicit legality provisions will be more likely if Japan’s outbound investors bring ISDS cases mostly against more developed states (where corruption is less prevalent than developing countries, so defences based on them are less likely). So far, that pattern holds true for Japan, although the United Nations reported only six claims brought by Japanese investors by the end of 2022.

62 M. McERLAINE, Japanese Renewable Investor Obtains Damages Award over Spanish Regulatory Reforms, Kluwer Arbitration Blog (11 March 2023), at <https://arbitrationblog.kluwerarbitration.com/2023/03/11/japanese-renewable-investor-obtains-damages-award-over-spanish-regulatory-reforms/>.

Table 1: Japanese Outbound ISDS Claims (31 January 2023)⁶³

No	Year of initiation	Short case name	Summary	Outcome of original proceedings	Respondent state	Home state of investor
1	2020	<i>Marco Trading v China</i>	<i>Investment:</i> Investments in a large-scale property development project	Discontinued	China	Japan
2	2020	<i>Mitsui v Spain</i>	<i>Investment:</i> Investments in the construction and operation of a solar power plant at Palma del Río in the Córdoba region, via joint venture enterprise Guzmán Energía. <i>Summary:</i> Claims arising out of a series of energy reforms undertaken by the Government affecting the renewables sector.	Pending	Spain	Japan
3	2018	<i>Itochu v Spain</i>	<i>Summary:</i> Claims arising out of a series of energy reforms undertaken by the Government affecting the renewables sector, including a 7 per cent tax on power generators' revenues and a reduction in subsidies for renewable energy producers.	Pending	Spain	Japan
4	2017	<i>Nissan v India</i>	<i>Investment:</i> 70 per cent share in Renault Nissan Automotive India Private Limited, a consortium that built an industrial automotive facility in Chennai, the capital of Tamil Nadu. <i>Summary:</i> Claims arising out of non-payment of incentives by the Indian State government of Tamil Nadu, which had been allegedly promised to the claimant	Settled	India	Japan

No	Year of initiation	Short case name	Summary	Outcome of original proceedings	Respondent state	Home state of investor
			under the agreement for building of a car plant, signed with the State government in 2008.			
5	2016	<i>Eurus Energy v Spain</i>	<i>Investment:</i> Investments in a renewable energy generation enterprise. <i>Summary:</i> Claims arising out of a series of energy reforms undertaken by the Government affecting the renewables sector, including a 7 per cent tax on power generators' revenues and a reduction in subsidies for renewable energy producers.	Pending	Spain	Japan Netherlands
6	2015	<i>JGC v Spain</i>	<i>Investment:</i> Shareholding in two solar thermal power plants in Cordoba, Spain. <i>Summary:</i> Claims arising out of a series of energy reforms undertaken by the Government affecting the renewables sector, including a 7 per cent tax on power generators' revenues and a reduction in subsidies for renewable energy producers.	Decided in favour of investor	Spain	Japan

Four outbound claims are against Spain brought by large Japanese companies under the (original) ECT, also involving claims involving the host state's changes to the regulatory regime for renewable energy, and piggybacking on dozens of claims by other countries' investors.⁶⁴ Only two are against states

⁶³ UNCTAD, Investment Dispute Settlement Navigator: Japan (n.d.), at <https://investmentpolicy.unctad.org/investment-dispute-settlement/country/105/japan>.

⁶⁴ See generally e.g., T.-P. LE/H.T.-H. NGUYEN, Balancing Interests in the Renewable Energy Sector through a Radical Change Criterion: Let the Wolf Guard the Hen House?, Kluwer Arbitration Blog (25 July 2022), at <https://arbitrationblog.kluw>

that score more poorly on corruption indices, with the 2017 FTA claim against India being settled (seemingly in May 2020 for around a third of the 660 million USD claimed by a large automobile manufacturer),⁶⁵ and the BIT claim against China being discontinued (either abandoned or settled).

Otherwise, there have only been a few ISDS arbitrations brought indirectly through Japanese affiliates incorporated in other countries (for example through the UK against the Czech Republic and Panama), or settled after filing was expected (such as a dispute under an aluminium processing contract with Indonesia). Japanese companies (especially larger ones), and their legal advisors as well as diplomats, are also much more aware nowadays of the rights given under investment treaties reinforced by ISDS provisions. There has also been a push since 2018 belatedly to raise the profile of international arbitration and even seek to make Japan more of a hub for regional dispute resolution services.⁶⁶

erarbitration.com/2022/07/25/balancing-interests-in-the-renewable-energy-sector-through-a-radical-change-criterion-let-the-wolf-guard-the-hen-house/; H. PANG, Investor-State Dispute Settlement in Renewable Energy: Friend or Foe to Climate Change?, in: Lin/Kysar (eds.), *Climate Change Litigation in the Asia Pacific* (2020) 144–172. The claimant has substantively succeeded in the Eurus claim listed as “pending”, after the tribunal awarded 106 million Euros in damages on 14 November 2022 on the merits. See MCERLAINE, *supra* note 62, and L. BOHMER, Analysis: Unpacking the Reasons That Led the Eurus V. Spain Tribunal to Award 106+ Million Usd to Compensate for the Claw-Back Component of Spain’s New Regulatory Regime, *Investment Arbitration Reporter* (21 November 2022), at <https://www.iareporter.com/articles/analysis-unpacking-the-reasons-that-led-the-eurus-v-spain-tribunal-to-award-106-million-usd-to-compensate-for-the-claw-back-component-of-spains-new-regulatory-regime/>. However, the claimant sought a rectification of the award on 5 January 2023: ICSID, Case Details: *Eurus Energy Holdings Corporation v. Kingdom of Spain* (ICSID Case No. Arb/16/4) (2022), at <https://icsid.worldbank.org/cases/case-database/case-detail?CaseNo=ARB/16/4>.

65 A. SHAH/S. VARADHAN, Exclusive: Nissan Settles Dispute with Indian State over Unpaid Dues – Sources, *Reuters* (28 May 2020), at <https://www.reuters.com/article/us-nissan-india-arbitration-exclusive/exclusive-nissan-settles-dispute-with-indian-state-over-unpaid-dues-sources-idUSKBN2342AR>. See also, against the backdrop of claims already against Spain: J. HEPBURN, Revision of Renewable Energy Contracts Raises Spectre of International Arbitration Proceedings against India, *Investment Arbitration Reporter* (29 November 2019), at <https://www.iareporter.com/articles/revision-of-renewable-energy-contracts-raises-spectre-of-international-arbitration-proceedings-against-india/>, noting that Japan’s SoftBank Energy may be among foreign investors impacted by India’s more recent state-level shifts in renewable energy policy.

66 J. CLAXTON *et al.*, Developing Japan as a Regional Hub for International Dispute Resolution: Dream Come True or Daydream?, *Journal of Japanese Law* 47 (2019)

Nonetheless, the relative paucity of outbound ISDS filings by Japanese investors, compared to FDI volumes and other big outbound investor states, arguably reflects a cautious but evolving assessment of costs and other ‘institutional barriers’ compared to the benefits of ISDS arbitration. It makes considerable sense to pursue a negotiated settlement ‘in the shadow of the law’, including a potential direct claim in arbitration but also through indirect pressure from Japan as home state typically able to invoke an inter-state dispute settlement procedure, as can be seen for example in the context of complex trade and investment tensions with Korea since 2019.⁶⁷

If Japanese outbound investors continue not to file many ISDS claims or use them vigorously to secure settlements with host states, or mainly pursue them against developed states with less corruption, the Japanese government may become more amenable to incorporating more consistent and clear legality provisions in their future treaties (Part IV.1. above). This is also likely if counterparties start pushing for them more strongly, and Japan perceives such provisions as helpful to safeguard the ISDS-backed regime generally amidst considerable ongoing concern worldwide – including in parts of Asia.

It should also be easier for Japan to include such more explicit and consistent legality provisions given its preference and considerable success in incorporating anti-corruption obligations on states (Part IV.1. above). Such provisions could also go part of the way towards addressing the concern that host states may deliberately solicit bribes, to assert later corruption in defence of an ISDS arbitration claim thanks especially to an explicit legality provision – yet never investigate and indict the local parties for such corruption.

VI. CONCLUSIONS

Japan is known as one of the largest outbound investors globally, but the country was slow in developing its international investment agreement network until the turn of the 21st century. Nonetheless, many of Japan’s (relatively few, but growing) BITs and Investment Chapters in FTAs contain an express anti-corruption provision. This probably reflects the country’s domestic law that takes a tough stance against corruption and bribery. Such innovation in treaty drafting is in the interests of Japan’s many outbound investors, with operations in countries that adhere less well to the rule of law.

In contrast, Japan’s international investment agreement drafting regarding express legality provisions is complex and disparate, with quite a few

109; J. CLAXTON *et al.*, Disruption as a Catalyst for International Dispute Services in Japan: No Longer Business as Usual?, in: Nottage *et al.*, *supra* note 44, 237–260.

67 J. CLAXTON *et al.*, Litigating, Arbitrating and Mediating Japan-Korea Trade and Investment Tensions, *Journal of World Trade* 54 (2020) 1.

treaties omitting them altogether. This may be due to the country's limited awareness of those provisions' significance. It could also reflect Japan's less vigorous pursuit of including explicit legality provisions in investment treaties, which would give host states stronger defences against Japan's outbound investors bringing ISDS claims against such states (raising objections about corruption or other illegality allegedly tainting the investments).

This treaty drafting practice may change over time if more foreign inbound investors commence ISDS arbitration claims against Japan, and if more Japan's outbound investors bring ISDS cases against states with a strong rule of law tradition (also less likely to raise defences of corruption and other serious illegal behaviour by investors). However, such a change will take time because there is reportedly only one known inbound ISDS treaty-based claim against Japan and six outbound ISDS filings by Japanese investors. In any event, and perhaps more likely, Japan may adopt more and clearer legality provisions if other counterparty states push more strongly for them. Japan would then agree to these in its future treaties to demonstrate its overall commitment to combatting corruption, and to preserve the legitimacy of the ISDS arbitration system.

SUMMARY

This article, part of an interdisciplinary Asia-focused book project, addresses for Japan the difficult practical and policy question facing arbitration tribunals when a foreign investor claims mistreatment by a host state but the latter alleges that the investment was tainted by corruption or other similar serious illegality. By way of background, Japan emerged from the 1980s as a leading exporter of foreign direct investment (FDI). Yet it has low inbound FDI despite some significant growth since the late 1990s (Part II.). This is despite Japan having comparatively very little corruption, which is often problematic for foreign investors (Part III.).

To protect and promote outbound FDI after a hesitant start, over the last two decades, Japan has accelerated ratifications of standalone bilateral investment treaties (BITs) as well as investment chapters in free trade agreements (FTAs). Almost all allow foreign investors from the home state to directly initiate investor-state dispute settlement (ISDS) arbitration against host states to get relief from violations of substantive treaty commitments, such as non-discrimination or compensation for expropriation (Part IV.1.).

Japan's investment treaty practice on corruption and illegality is comparatively interesting for two reasons (Part IV.2.). First, from around 2007, its treaties have often required host states to take measures against corruption. This should help Japan's outbound investors, but these obligations are general-

ly weakly phrased. Secondly, Japan's treaties have been less consistent in expressly limiting their protections to foreign investments made in accordance with host state laws (including against corruption). This may be due to treaty drafters from Japan and counterparty states being less aware of the significance of such express legality provisions, which will often lead tribunals to decline jurisdiction if corruption is established, thus leaving foreign investors without treaty protections. Such outcomes may also incentivise host states to ensure a bribe is taken, to use as a treaty defence if foreign investors ever launch treaty claims, whereas other outcomes for tribunals are possible if there is no express legality provision. Another possibility is that this drafting is deliberate, again to benefit Japanese outbound investors as claimants because the absence of a legality provision renders more difficult defences from host states, which typically have more corruption than in Japan.

Japan may adopt more and clearer legality provisions if it becomes subject to more inbound ISDS arbitration claims, and/or if claims by Japanese outbound investors are mostly against well-governed host states with little scope for corruption. Yet both types of claims remain few (Part V.). The shift may therefore come more from other counterparty states pushing for such legality provisions and Japan agreeing in its future treaties to demonstrate its overall commitment to combatting corruption, and to preserve the legitimacy of the ISDS arbitration system (Part VI.).

ZUSAMMENFASSUNG

Der Beitrag ist Teil eines interdisziplinären Buchprojekts mit einem Fokus auf Asien. Er befasst sich mit Blick auf Japan mit der schwierigen praktischen wie politischen Frage, die sich Schiedsgerichten stellt, wenn ein ausländischer Investor behauptet, von einem Gaststaat ungerecht behandelt zu werden, letzterer aber einwendet, dass das Investment durch Korruption oder ähnlich ernsthafte Rechtsverstöße kompromittiert sei. Japan ist seit den 1980er Jahren einer der führenden Exporteure von ausländischen Direktinvestitionen. Aber ausländische Direktinvestitionen in Japan bewegen sich trotz einer deutlichen Steigerung in den späten 1990er Jahren nach wie vor auf einem niedrigen Niveau (Teil II.). Hieran ändert auch die Tatsache nichts, dass Japan vergleichsweise wenig Korruption kennt, die für ausländische Investoren oftmals ein Problem darstellt (Teil III.).

Im Verlauf der vergangenen beiden Jahrzehnte hat Japan, nach einem zögerlichen Beginn, den Abschluss von eigenständigen bilateralen Investitionsabkommen wie auch die Ratifizierung von Investitionsregelungen in Freihandelsübereinkommen beschleunigt, um ausländische Direktinvestitionen zu fördern und zu sichern. Fast alle dieser Abkommen erlauben ausländischen Investoren, unmittelbar von ihren Heimatstaaten aus ein Investor-Staat-Schiedsverfahren gegen den jeweiligen Gaststaat einzuleiten, um Hilfe gegenüber wesentlichen

Verletzungen der Regelungen der Abkommen wie etwa durch Diskriminierung oder fehlende Entschädigung für Enteignungen zu erhalten (Teil IV.1.).

Die japanische Handhabung der Investitionsabkommen mit Blick auf Korruption und andere Gesetzesverstöße ist aus zwei Gründen von Interesse (Teil IV.2.). Zum einen, weil die Abkommen seit etwa 2007 oftmals von den Gaststaaten verlangen, Maßnahmen gegen Korruption zu ergreifen, um japanischen Unternehmen bei ihren ausländischen Direktinvestitionen zu helfen. Diese Verpflichtungen sind jedoch im Allgemeinen nur vage formuliert. Zum zweiten sind Japans Investitionsabkommen nicht durchgängig konsistent in der Beschränkung ihrer Schutzwirkung auf solche ausländischen Direktinvestitionen ausgestaltet, die unter Beachtung des Rechts des Gaststaates einschließlich dessen Regelungen gegen Korruption getätigt wurden. Einer der Gründe dafür könnte sein, dass die Verfasser der Abkommen aus Japan und den jeweiligen Vertragsstaaten sich der Bedeutung eines klar formulierten Legalitätserfordernisses nicht hinreichend bewusst waren. Die Folge ist, dass Schiedsgerichte oftmals ihre Zuständigkeit in Fällen verneinen, in denen nachweislich Korruption stattgefunden hat, womit der Schutz der Abkommen für die Investoren entfällt. Ein solches Ergebnis könnte Gaststaaten veranlassen, dafür zu sorgen, dass tatsächlich Korruptionszahlungen erfolgen, um dies als Verteidigungsmaßnahme vorbringen zu können, sollte ein ausländischer Investor ein Verfahren wegen einer Verletzung des Abkommens einleiten wollen, da die Schiedsgerichte im Falle des Fehlens eines eindeutigen Legalitätserfordernisses eine größere Entscheidungsfreiheit bezüglich ihrer Zuständigkeit haben. Eine andere Möglichkeit ist, dass die Abkommen absichtlich vage abgefasst werden, um wiederum japanischen Investoren als Kläger zu begünstigen, denn das Fehlen eines eindeutigen Legalitätserfordernisses macht die Verteidigung für die Gaststaaten schwieriger, da diese typischer Weise mehr Korruption als Japan haben.

Japan könnte möglicherweise mehr und klarer formulierte Legalitätserfordernisse verwenden, falls es verstärkt mit Schiedsklagen aufgrund von ausländischen Direktinvestitionen im eigenen Land überzogen werden sollte und/oder falls künftige Schiedsklagen japanischer Investoren sich überwiegend gegen solche Gaststaaten richten sollten, in denen es aufgrund von strikter Regulierung kaum Korruption gibt. Allerdings sind beide Arten von Schiedsklagen bislang selten (Teil V.). Ein Wandel dürfte deshalb wohl eher von Staaten ausgehen, mit denen Japan Investitionsabkommen geschlossen hat, wenn und soweit diese verstärkt eindeutig formulierte Legalitätserfordernisse verlangen und Japan dem für künftige Abkommen zustimmt, um sein generelles Eintreten für die Bekämpfung der Korruption unter Beweis zu stellen und die Legitimität des Systems der Investor-Staat-Schiedsverfahren zu sichern (Teil VI.).

(Die Redaktion)