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Balancing Investment Protection and Regulatory Chill: How Indonesian Investment Agreements Impact the Regulation and Enforcement of Mining Licenses

Darian Amarta* Prita Amalia Yulinda Adharani
Faculty of Law, Universitas Padjadjaran Jl. Raya Bandung Sumedang KM.21, Hegarmanah, Jatinangor, Sumedang Regency, West Java 45363, Indonesia
* E-mail of the corresponding author: darian19001@mail.unpad.ac.id

Abstract
Investment agreements continues to be welcomed by host states for the investment it attracts, but a growing body of work supports the idea that investment agreements may also restrict host states from enacting specific public regulations for fear of capital flight, reputational damage and costs involved within ISDS proceedings, an effect known as Regulatory Chill. Previous works on Regulatory Chill in Indonesia's mining industry have analyzed the partial rollback of a ban on open pit mining in protected forests as a response to the affected investors' threat for the commencement of the arbitration. Following the change of Indonesia's mining system from contracts of works to licenses, 3 new investor-state disputes involving mining licenses have been raised to ISDS. This article sets out two main objectives: (i) to establish the existence of the Regulatory Chill effect in connection with Indonesia's mining sector and (ii) to examine potential solutions through amendments to Indonesia's investment agreement. This article has found one instance of the Regulatory Chill effect in the form of policy response from the case of Nusa Tenggara v. Indonesia. However, it failed to find enough evidence of an internalization chill. In regards to Indonesia's investment agreements, this article recommends maintaining the host state's regulatory space by amending investment agreements to include exclusions to sensitive regulatory areas, greater elaboration of FET and Expropriation clauses, as well as the elimination of MFN clauses, and to a lesser extent, the use of exception and incorporation of international environmental obligations.
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1. Introduction

Even from as early as 1832, states has recognized the need to balance the benefits of foreign investment and its potential harms.[1] One means of accomplishing this is through an investment agreement, a bilateral or multilateral treaty that provides certain protections to investors from the host country, creates obligations for the investors in order to obtain such protection, and well as a means of dispute settlement between all parties through arbitration known as the Investor-State Dispute Settlement ("**ISDS**").[2] As of the time of writing, more than 2500 investment agreements have been ratified worldwide, with Indonesia party to 43 of them.[3]

Despite the prevalence of investment agreements, foreign investments may still negatively affect the ability of a host state to enact public welfare policies due to the fear of inducing capital flight or even an investment dispute, an effect known as Regulatory Chill. The Regulatory Chill effect is enhanced by investment agreements that provide for ISDS. To note, Although ISDS does not have the power to force change on a state's regulations, the regulatory ability of a host state may still be significantly impacted by such proceedings[4] since such host state risks facing damages from adverse arbitral awards (which may run to billions of USD),[5] legal and procedural costs, and the deterioration of its reputation as an "investor-friendly" state.[6] If Regulatory Chill primarily drives compliance with international regulation, it would be of little concern. However, it has been noticed that this effect equally affects regulations that is substantially compliant with the treaty in question, thus

[1] Ha-Joon Chang, "Regulation of Foreign Investment in Historical Perspective," *The European Journal of Development Research* 16, no. 3 (2004): 690, https://doi.org/doi.org/10.1080/0957881042000266660.
[2] Alex Grabowski, "The Definition of Investment under the ICSID Convention: A Defense of Salini," *Chicago Journal of International Law* 15, no. 1 (2014): 291-293.
[3] United Nations Conference on Trade and Development, "Investment Policy Hub: International Investment Agreements Navigator: Indonesia," accessed February 21, 2023, https://investmentpolicy.unctad.org/international-investment-agreements/countries/97/indonesia.
[4] Kyla Tienhaara, "Regulatory Chill in a Warming World: The Threat to Climate Policy Posed by Investor-State Dispute Settlement," *Transnational Environmental Law* 7, no. 2 (2018): 233, https://doi.org/doi:10.1017/S2047102517000309.
[5] 469 Million USD (Around 6.3 Trillion Rupiah on 2016) in Permanent Court of Arbitration, *Indian Metals & Ferro Alloys Ltd v. Republic of Indonesia*, PCA Case No. 2015-40, Final Award (Permanent Court of Arbitration March 29, 2019); For a case won by the Claimant, 8.3 Billion USD (Around 117 Trillion Rupiah on 2019) International Centre for Settlement of Investment Disputes, *ConocoPhillips Petrozuata B.V. v. Bolivarian Republic of Venezuela*, Decision on Rectification (International Centre for Settlement of Investment Disputes, 2019).
[6] Kyla Tienhaara, "Regulatory Chill and the Threat of Arbitration: A View from Political Science," in *Evolution in Investment Treaty Law and Arbitration* (Cambridge: Cambridge University Press, 2011), 7–10, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2065706.

creating an effect going beyond what the treaties intended.[1]

This particular phenomenon has been observed in Indonesia. Around 2002, when the Indonesian government moved to ban open pit mining in a protected forest, they encountered resistance from the affected investors. When the threat of arbitration emerged from the investors, the Indonesian government swiftly provided exemptions from the ban to the selected investors. Nabiel Makarim, Indonesian Minister of Environment and Forestry from 2001 – 2004, also admitted that the threat to submit the dispute through ISDS had been an essential factor in giving the exemptions at that time.[2] Following the case, Indonesia had amended approached mining concessions, from granting mining companies government contracts to issuing mining licenses. After this switch, several new ISDS claims have emerged from Indonesia's mining sector.[3] These cases will be examined in order to show whether or not there further instances of Regulatory Chill in Indonesia's mining sector.

2. Domestic Regulation, International Law, and Regulatory Chill

From the international law approach, domestic regulations and international law can be seen as a unified legal framework (monism) or independent legal frameworks (dualism).[4] A domestic regulation can breach international obligations and create obligations for remedies in the international setting, but is otherwise unaffected by international law.[5] In investment law, a host state's policy can breach its own investment treaty obligations and create an obligation to compensate the affected investor, but this does not mean that every breach of international law requires the domestic investment policy to be transformed. Further, a distinction must be made between Regulatory Chill and compliance with international law. When a host state's policy has contravened with the obligation in the investment treaty that it is a party of, the transformation of the domestic regulation to be aligned with such treaty is solely considered to be compliance with the treaty.[6] In contrast a Regulatory Chill effect may still transpire even if the policy is compliant with such investment treaty, caused by the deterring effect of the potential damages, legal and procedural costs, and the deterioration of its "investor-friendly" reputation.[7]

A frequent criticism of the Regulatory Chill theory is that it devolvsed into questioning the merit of entering investment agreement.[8] Accordingly, we have limited our discussion to issues and solutions within the framework of investment agreements. A further criticism of the Regulatory Chill theory is that due to its premise of investors undermining a state's regulatory ability, researchers would need to find evidence of regulations that *failed to be* issued.[9] To respond to this criticism, we must look into how Regulatory Chill is studied. Ashley Schram identified the following methodologies in analyzing Regulatory Chill:

Table 1. The policy response, treaties and awards, internalization, and their differences.

	Analysis	**Required data**	**Chilling effect**	**Potential Drawback**
Policy Response	Polices that are amended or revoked in response to the usages of ISDS	News, interviews with parties in charge of policies, regulations and subsequent amendments	Occurs to policies already in effect	Unclear reasonings on why the policies change
Treaties and Awards	Results or potential results of ISDS proceedings	Arbitral awards and memorandums	Occurs to policies already in effect	Chilling effect can occur even if the ISDS claim is discontinued
Internalization	The effect of concerns over ISDS to the making of the policies	Interviews with parties in charge of policies policies and parliamentary discussions	Occures to policies under draft	Requires measuring awareness of parties in charge of policies as well as their considerations of ISDS.

[1] Tienhaara, "Regulatory Chill in a Warming World: The Threat to Climate Policy Posed by Investor-State Dispute Settlement," 237.
[2] Mines and Communities, "Nabiel Makarim Agrees with Mining in Protected Forests," *MAC: Mines and Communities*, June 15, 2002, http://www.minesandcommunities.org/article.php?a=7737; Tempo Interactive, "State Minister for Environment: Issuing Mining Licenses for 13 Companies was a Mistake," *TEMPO.CO*, March 15, 2004, https://en.tempo.co/read/40685/state-minister-for-environment-issuing-mining-licenses-for-13-companies-was-a-mistake.
[3] United Nations Conference on Trade and Development, "Investment Policy Hub: International Investment Dispute Settlement Navigator, Indonesia," accessed January 20, 2023, https://investmentpolicy.unctad.org/investment-dispute-settlement/country/97/indonesia.
[4] Mochtar Kusumaatmadja, *Pengantar Hukum Internasional Buku I - Bagian Umum*, 4th ed. (Jakarta: Bina Cipta, 1982), 53–58.
[5] Malcolm N. Shaw, *International Law*, 6th ed. (Cambridge: Cambridge University Press, 2008), 133.
[6] Tienhaara, "Regulatory Chill in a Warming World: The Threat to Climate Policy Posed by Investor-State Dispute Settlement," 3.
[7] Tienhaara, "Regulatory Chill and the Threat of Arbitration: A View from Political Science," 7–10.
[8] Jessica Ji, "Attacking ISDS Provisions for Causing Regulatory Chill: A Moving Target," *Thomson Reuters: Practical Law Arbitration Blog*, May 25, 2018, http://arbitrationblog.practicallaw.com/attacking-isds-provisions-for-causing-regulatory-chill-a-moving-target/.
[9] Eric Neumayer, "Do Countries Fail to Raise Environmental Standards? An Evaluation of Policy Options Addressing 'Regulatory Chill,'" *International Journal of Sustainable Development* 4, no. 3 (February 2001): 19, https://doi.org/DOI:10.1504/IJSD.2001.004446.

The policy response and internalization methodology are relied in this current study. Here, the policy response analysis will be utilized to explore into publicly available cases which involves Indonesia's mining sector and the policy responses towards each suit. The specific cases that are utilized in this writing are *IMFA v. Indonesia*, *Nusa Tenggara v. Indonesia*, as well as *Churchill Mining and Planet Mining v. Indonesia*. In a policy response analysis, Regulatory Chill effect shall be found in the event the following are met:

1. There exists regulations or implementation which are/is challenged by an investor;
2. There is a threat or a utilization of ISDS to challenge the regulation or its implementation; and
3. In response to the threat or the use of ISDS, the regulations or its implementation are/is changed.[1]

The difficulty of the analysis law in determining whether a peculiar change to a policy is genuinely affected from the use of ISDS. Even according to Tienhaara, "*a considerable amount of decision-making is not made out in the open*" and there may also be certain incentives given to policymakers in order to avoid admitting that such decision is caused by the suit from an investor, or separately blame a foreign investor for a policy they wish to abandon for a separate reason.[2]

Without the outright admission from the policymakers, such as what happened in the "protected forest case", the reason of any policy change may not be very transparent. However, we are also able to analyze further into the "protected forest case": aside from the admission from the policymaker, the timeline of the policy response lines up with the usage of ISDS. In that case, the regulation was issued and challenged 2 (two) years prior to any policy response made. Additionally, the time lapsed between the first threat of ISDS aand the policy response was slightly more than cooling-off period that must be exhausted for the ISDS proceeding to commence.[3] A policy response is therefore able to be attributed to the usage of ISDS in the event the policy has been disputed for a period of time, and the policy change only occurs around a similar timeframe as the usage of the ISDS itself.

On the internalization analysis, this article analyzes the two amendments carried out towards Indonesia's mining law in 2020. Here, we particularly analyze the reasoning of the policymakers for such amendments and whether Regulatory Chill impacted the policymakers' decision.

3. Cases and Findings

3.1. The Overview of Indonesia's disputes relating to mining sector.

This research looked into the case of *IMFA v. Indonesia*, *Nusa Tenggara v. Indonesia*, as well as *Churchill Mining and Planet Mining v. Indonesia*, which involve objections to some part of the Indonesian mining license process. These cases involves regulations overlapping concession, incomplete permits and imposition of tariffs, as well as the use of ISDS to challenged those regulations.[4] In all except the *Nusa Tenggara v. Indonesia* case, the tribunal ruled in favour of Indonesia and there were no government response indicating a regulatory chill effect. As *Nusa Tenggara v. Indonesia* has fulfilled all of the criteria of the Regulatory Chill effect, this particular case is further analysed.

3.2. Nusa Tenggara v. Indonesia

Nusa Tenggara v. Indonesia occurred in the background of a move by the Indonesian government to transition Indonesia's mining industry from exporting raw ore to exporting processed ores to shift big part of the value-chain to Indonesia. This culminates in Law No. 4 of 2009 ("**Mining Law**"), which through Article 103, mandates mining license holders to domestically process and purify ores, and therefore effectively banning raw ore exports. In effect, this required companies to either construct smelters, fund development of other domestic smelters, or funnel their ores to existing domestic smelters. The holders of Contracts of Work which predated the law were also imposed the obigation to conduct domestic purification as a precondition for securing an export license. Since PT Newmont Nusa Tenggara ("**PTNNT**") was holder of Contract of Work, PTNNT had to comply with the new regulation within 5 (five) years. In concert, progressive export tariffs for copper concentrate was implemented, starting from 25% in January 2014 and by July 2016, it gradually became 60%. While PTNNT had complied with the processing requirements, they had not complied with the purification requirements, which required a smelter, and had to face increasing export tariffs.

From what has been stipulated above, we can look further into the dispute and connection or causality

[1] Ashley Schram *et al*., "Internalisation of International Investment Agreements in Public Policymaking: Developing a Conceptual Framework of Regulatory Chill," *Global Policy* 9, no. 2 (May 2018): 3–6, https://doi.org/10.1111/1758-5899.12545; Tienhaara, "Regulatory Chill and the Threat of Arbitration: A View from Political Science," 3–6.

[2] Tienhaara, "Regulatory Chill and the Threat of Arbitration: A View from Political Science," 4.

[3] Stuart G. Gross, "Inordinate Chill: Bits, Non-NAFTA MITs and Host-State Regulatory Freedom- An Indonesian Case Study," *Michigan Journal of International Law* 24, no. 3 (2003): 895.

[4] *Indian Metals & Ferro Alloys Ltd v. Republic of Indonesia*, PCA Case No. 2015-40, Final Award paragraphs 54–64; International Centre for Settlement of Investment Disputes, *Nusa Tenggara Partnership B.V. and PT Newmont Nusa Tenggara V. Republic of Indonesia*, No. ICSID CASE No. ARB/14/15 (International Centre for Settlement of Investment Disputes August 29, 2014); International Centre for Settlement of Investment Disputes, *Churchill Mining and Planet Mining Pty Ltd v. Republic of Indonesia*, No. ICSID Case No. ARB/12/40 and 12/14 (International Centre for Settlement of Investment Disputes December 6, 2016)

between the usage of ISDS and the eventual policy response. This shall be seen from how the timeline of the policy response is concurrent with the usage of ISDS.

On September 16 2013, PTNNT made its objection to the processing requirement, in which PTTNT threatened to close the mine entirely due to the policy.[1] On December 10 2013, PTNNT and the Indonesian government succeeded to conduct negotiations, which resulted in PTNNT agreeing to funnel their concentrate to local companies planning to build smelters, although PTNNT was still resistant to building its own smelter.[2] Later on January 2014, as there was the newest amendment to the relevant regulations issued, PTNNT further renewed its objections of what it called "potentially restrictive conditions to obtain an export permit" and the new export tariffs,[3] although PTNNT has stopped the copper concentrate export activities at that point. The negotiations continued throughout May 2014 and meanwhile, PTNNT ramped down its operations, citing that the measure "*will disrupt the lives* […] *of 8,000 employees and contractors and impact thousands of more people*." Eventually, PTNNT suspended the entire processing operations in June 2014.[4]

The ISDS claim was filed on June 30 2014. In accordance with the relevant bilateral investment treaty ("**BIT**"), the a claim would be admissible after 3 months from the first request for amicable settlement.[5] Generally, such cooling off period is seen as a jurisdictional requirement, with the parties being barred from proceeding to arbitration unless it attemps amicable settlement in that time period, except for cases of futillity.[6] However, a "bare" amicable settlement clauses, such as the one present in this case, do not give firm obligations on potential claimants to actively attempt amicable settlement, with some noting that exhausting this period was enough for a claim to be deemed admissible.[7] Since initial negotiations started on December 2013, by June 30 2014 the dispute was admissible to be settled in arbitration. The filing of the ISDS claim evoked condemnation from some Indonesian ministers, some threatening to revoke PTTNT's license entirely. Meanwhile, others remained optimistic in securing a solution through negotiations.[8] Nevertheless, Indonesian government's general stance was clear that it would remain open to more negotiations until a special meeting on the subjected was convened.[9] On 24 July 2014, the president of Indonesia issued a presidential decision to seek legal counsel in preparation the upcoming legal dispute.[10]

On August 25, PTNNT was eventually willing to withdraw its ISDS claim, citing an "encouraging recent development".[11] This decision came as senior government officials finally showed willingness to open formal negotiations to conclude a Memorandum of Understanding ("**MoU**") with PTNNT.[12] The MoU was signed between Indonesian government and PTNNT within the week of the claim being withdrawn from ICSID.[13] Due

[1] Azis Husaini, "Newmont Mengancam Menutup Tambang Batu Hijau," *Kontan.co.id*, September 20, 2013, https://industri.kontan.co.id/news/newmont-mengancam-menutup-tambang-batu-hijau.

[2] PT Newmont Nusa Tenggara, "Press Release: PTNNT Supports Government Goals on In-Country Processing: PTNNT Does Not Export Unprocessed Ore," *Newmont.com*, December 10, 2013, https://s24.q4cdn.com/382246808/files/doc_news/archive/Siaran-Pers-10-Desember-2013-PTNNT-Supports-Government-Goals-on-In-Country-Processing.pdf.

[3] Newmont Mining Corporation, "Newmont Provides Update on Export Ban in Indonesia," *Newmont.com*, January 22, 2014, https://www.newmont.com/investors/news-release/news-details/2014/Newmont-Provides-Update-on-Export-Ban-in-Indonesia/default.aspx.

[4] The Jakarta Post, "Newmont Stops Production Pending Export Clarity," *The Jakarta Post*, June 4, 2014, https://www.thejakartapost.com/news/2014/06/04/newmont-stops-production-pending-export-clarity.html; PT Newmont Nusa Tenggara, "Press Release: PTNNT Expects to Ramp Down Production as Process to Secure Export Permit Not Yet Complete," *Newmont.com*, May 7, 2014, https://s24.q4cdn.com/382246808/files/doc_news/archive/PTNNT-Final-release_v001_h6d514.pdf.

[5] Kingdom of the Netherlands and Republic of Indonesia, "Agreement between the Government of the Kingdom of the Netherlands and the Government of the Republic of Indonesia on Promotion and Protection of Investment" (n.d.), art. 12, https://www.italaw.com/sites/default/files/laws/italaw6150.pdf.

[6] Addyana Belaputri et al., "the Exhaustion of the Cooling-off Period: A Non-Mandatoy Pre-Condition in Investment Arbitration,"*Transnational Business Law Journal* 2, no. 2 (August 2021): 14, https://doi.org/10.23920/transbuslj.v2i2.788

[7] ICSID, "Overview of Investment Treaty Clauses on Mediation," *icsid.worldbank.org*, July 2021, 2–3, https://icsid.worldbank.org/sites/default/files/publications/Overview_Mediation_in_Treaties.pdf; Anna Holloway, "Approaches to Providing for Mediation in Investment Treaties and Model Clauses," *Kluwer Arbitration Blog*, February 26, 2022, https://arbitrationblog.kluwerarbitration.com/2022/02/26/approaches-to-providing-for-mediation-in-investment-treaties-and-model-clauses/.

[8] Rachma Tri Widuri, "Pemerintah Siap Ladeni Gugatan Newmont," *TEMPO.CO*, July 3, 2014, https://bisnis.tempo.co/read/590098/pemerintah-siap-ladeni-gugatan-newmont.

[9] detikFinance, "CT: Kita Berharap Newmont Cabut Gugatan Arbitrase," *finance.detik.com*, July 11, 2014, https://finance.detik.com/berita-ekonomi-bisnis/d-2634718/ct-kita-berharap-newmont-cabut-gugatan-arbitrase; Liputan6.com, "RI Siapkan Strategi Buat Perang Lawan Newmont di Arbitrase," *djkn.kemenkeu.go.id*, July 14, 2014, https://www.djkn.kemenkeu.go.id/berita_media/baca/5810/RI-Siapkan-Strategi-Buat-Perang-Lawan-Newmont-di-Arbitrase.html.

[10] RED, "Presiden Instruksikan Sikap Tegas dan Keras Hadapi Newmont," *hukumonline.com*, July 25, 2014, https://www.hukumonline.com/berita/a/presiden-instruksikan-sikap-tegas-dan-keras-hadapi-newmont-lt53d20ee4bfe5b/.

[11] PT Newmont Nusa Tenggara, "Press Release: PTNNT Discontinues and Withdraws Arbitration Claim in Anticipation of Formal MoU Negotiations with Indonesian Government," *Newmont.com*, August 26, 2014, https://s24.q4cdn.com/382246808/files/doc_news/archive/Final-NNT-News-Release-26-August-2014-PTNNT-Discontinues-and-Withdraws-Arb_v001_w0g1d7.pdf.

[12] Michael Taylor and Yayat Supriatna, "UPDATE 2-Newmont Withdraws Mining Arbitration Case against Indonesia," *Reuters*, August 26, 2014, https://www.reuters.com/article/indonesia-newmont-arbitration-idAFL3N0QW3EG20140826.

[13] PT Newmont Nusa Tenggara, "Press Release: PTNNT to Resume Operations and Copper Concentrate Exports," *Newmont.com*, September 4, 2014, https://s24.q4cdn.com/382246808/files/doc_news/archive/PR-4-Sep-2014-PTNNT-to-Resume-Operations-and-Copper-Concentrate-

to this decision, PTNNT received its export permit on September 22 2014, granting it the authorization to export reduced quantities of copper concentrate, despite not having gone through a purification process.[1] In the meantime PTNNT agreed to comply with the export tariffs, their export was allowed on the basis of a deposit of a Smelter Surety Bond, rather than compliance with the obligation to purify as what has been stated in the Mining Law as well and its implementing regulations.[2] Therefore, this a rollback of the government's previous implementation of the Mining Law.

PTNNT's dispute heavily mirrors the "protected forest case" since there was a long-contested policy being waived in response to the threat of investment arbitration. The effectiveness of the usage of ISDS was also acknowledged by PTNNT, which announced that the government was willing to negotiate an MoU if the claim had been withdrawn.[3] Therefore following the shift from Contract of Work to mining licenses, there is an observable Regulatory Chill effect in Indonesia's mining sector in the form of a policy response.

4. The Existence of Mining Law and Internalization Chill

Regulatory Chill can also manifest in the form of internalization chill, where policymakers avoid the potential ISDS claims by staying away from creating regulations that they deem as risky. Internalization chill may be analysed from interviews with relevant policy makers or by going through the available discussions during the formulation. Here, the focus of the analysis is on the two amendments made to the Mining Law through Law No. 3 of 2020 and Law No. 11 of 2020. These laws came under constitutional review for procedural defects, with the latter being criticized for lacking public consultation.[4] Some insights may be obtained from the respective constitutional reviews of both laws, specifically from the rationale given by Indonesian government as well as parliament in defense of the substantive need for the laws.

For the first amendment, the rationale of parliament was "*the inability of the existing law to address actual issues and conditions in the mining sector, including cross sectoral issues*".[5] Further concerns exist, which particularly stance that unless a license extension for coal mining, as facilitated by the amended law, was granted, there would arise a critical shortage of coal for Indonesia's coal power plants. Moreover, the rationale given by Indonesian government was: the amendment was essential to optimize the implementation of the smelter construction requirements. For the second amendment, the parliament explained that the law was important in order to increase the Ease of Doing Business in Indonesia, trim away the complicated bureaucracy, as well as establish a suitable investment climate.[6]

The adjustment to the mining law's smelter construction requirement might seem to be an effort to avoid disputes such as *Nusa Tenggara v. Indonesia*. However, the difficulty in applying the smelter regulation was an issue that went beyond only PTNNT.[7] As such, the available data cannot support the conclusion that such change was conducted mainly due to the case of *Nusa Tenggara v. Indonesia*. Hence, in accordance with the methodology of Regulatory Chill analysis, which is limited to ISDS usage, there has yet to be any observable instance of internalization chill in regards to Indonesia's mining sector.

5. Adapting Investment Agreements

The approach which has been implemented in investment agreements is the requirement that investment conform with local regulations. That was the case for the contract of work in the "protected forest case"[8] as well as the BIT in *Nusa Tenggara v. Indonesia*.[9] As can be gleamed from these cases, this requirement is not effective at

Exports_v001_q410i2.pdf.

[1] PT Newmont Nusa Tenggara, "Press Release: PTNNT Receives Export Permit, Shipments Expected to Resume This Week," *Newmont.com*, September 22, 2014, https://s24.q4cdn.com/382246808/files/doc_news/archive/Export-Permit-Press-Release-22-September-2014-PTNNT-Receives-Export-Permit_v001_t1p2r7.pdf; The Jakarta Post, "Newmont Gets Export Permit despite Pending Smelter Fund," *The Jakarta Post*, September 20, 2014, http://www.thejakartapost.com/news/2014/09/20/newmont-gets-export-permit-despite-pending-smelter-fund.html.

[2] "Memorandum Of Understanding Between Directorate General Of Mineral And Coal, The Ministry Of Energy And Mineral Resources And Pt Newmont Nusa Tenggara On Adjustment Of The Contract Of Work," Government of Indonesia and PT Newmont Nusa Tenggara, uploaded 2014, https://www.sec.gov/Archives/edgar/data/1164727/000119312514332104/d784425dex101.htm.

[2] "Press Release: PTNNT Discontinues and Withdraws Arbitration Claim in Anticipation of Formal MoU Negotiations with Indonesian Government."

[3] "Press Release: PTNNT Discontinues and Withdraws Arbitration Claim in Anticipation of Formal MoU Negotiations with Indonesian Government."

[4] Ananda Teresia and Gayatri Suroyo, "Indonesia Issues Emergency Regulation to Replace Jobs Law," *Reuters*, December 30, 2022, https://www.reuters.com/world/asia-pacific/indonesia-issues-emergency-regulation-replace-controversial-job-creation-law-2022-12-30/.

[5] Mahkamah Konstitusi, *Putusan Mahkamah Konstitusi Nomor 60/PUU-XVIII/2020*, No. 60/PUU-XVIII/2020 (Mahkamah Konstitusi October 27, 2021).

[6] Mahkamah Konstitusi, *Putusan Mahkamah Konstitusi Nomor 91/PUU-XVIII/2020*, No. 91/PUU-XVIII/2020 (Mahkamah Konstitusi November 25, 2021).

[7] Julia Tijaja and Mohammad Faisal, "Industrial Policy in Indonesia: A Global Value Chain Perspective," (working paper, Asian Development Bank, October 2014), 33–38, https://www.adb.org/sites/default/files/publication/110982/ewp-411.pdf.

[8] Gross, "Inordinate Chill: Bits, Non-NAFTA MITs and Host-State Regulatory Freedom- An Indonesian Case Study," 896.

[9] Agreement between the Government of the Kingdom of the Netherlands and the Government of the Republic of Indonesia on Promotion and Protection of Investment, art. 1.

restraining Regulatory Chill effects. An explanation for Regulatory Chill effect is that public welfare policies is able and has been challenged multiple times in investment arbitration.[1] As a result to the lack of consistency in investment arbitration awards, it can be arduous for states to comprehend whether any given regulation will be considered in breach of its obligations according to the investment agreements.

The uncertainty runs counter to the need for any state to maintain regulatory space for public welfare. In the case of Indonesia's mining sector, this is intrinsically tied to the right to regulate its natural resources. The state's sovereignty over its own natural resources has already been conceived through the doctrine of the state's right of control (*Hak Menguasai Negara*), which is stipulated under Article 33 (3) of Indonesia's Constitution. Essentially, this law requires the state to have "control" over its natural resources, for the purpose of the greater public welfare. A state's right of control would be respected if it preserves the authority to manage its natural sources for the improvement of, *inter alia*, public welfare.[2] With this understanding, the mining concessions to domestic and foreign investment firms do not breach the doctrine of the state's right of control, as long as the state itself remain able to assert regulations on the environmental, social, or other public welfare purposed sectors.

The need to reconcile between this domestic need for regulatory space and its international obligations is already evident in the practice of treaty negotations. This typically involves negotations of substantive provisions of the treaty while keeping existing domestic regulations in mind.[3] While this guarantees that any given international obligation does not conflict with the domestic regulations which are still in effect, it may not be sufficient in order to anticipate future regulatory needs. Following *Churchill Mining and Planet Mining v. Indonesia* and *Nusa Tenggara v. Indonesia* cases, Indonesian government has also acknowledged this the need to update its investment agreements to meet this regulatory needs.[4]

5.1. The Recent Developments in Investment Agreements

5.1.1. Exceptions

Exceptions is an affirmative defense which removes the liability of a host state for the regulations that would be a breach of its obligations under the treaty.[5] Usually, it is formulated as reiterations of the host state's right to regulate. Recent treaties even specifically mentions environmental concerns in such exceptions. The 2023 EU-New Zealand FTA recognize the right of each party to: (a) decide its sustainable development priorities and policies; (b) set up the levels of domestic labor and environmental protection; as well as (c) modify or adopt the applicable law and policies.[6] Meanwhile, the 2016 Morocco-Nigeria BIT recognizes each party's rights with regards to compliance, regulatory, investigatory, as well as prosecutorial powers. Further, it also allows for measures consistent with the BIT to ensure investment takes social and environmental issues into account.[7]

On a positive note, these exceptions, which are environmental-oriented, allow host states more regulatory space for the concerns covered in the exceptions. Nevertheless, when it comes to the practice, exceptions may be hard to be relied on by states since the threshold for what regulatory measures are "necessary" are not set in stone. Such threshold might require the measure to be the only means to attain the policy objective or, contrarily, that the measure was simply proportional.[8] Therefore, the introduction of the exceptions does not automatically solve the uncertainty issue in international arbitration

5.1.2. Exclusions

Exclusions or carve-outs expressly exclude particular sectors in whole or in part from protections provided by the treaty. Traditionally, exclusions have been used in order to exclude regulations on taxation.[9] Through the recent development, this can be seen from an example coming from Article 29.5 of the Trans-Pacific Partnership Agreement ("**TPP**"), which is a partial exclusion. Article 29.5 of the TPP stipulates that:

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[1] Vera Korzun, "The Right to Regulate in Investor-State Arbitration: Slicing and Dicing Regulatory Carve-Outs," *Vanderbilt Journal of Transnational Law* 50, no. 2 (2017): 375, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2950939.

[2] Majelis Permusyawaratan Rakyat, "Ketetapan Majelis Permusyawaratan Rakyat Nomor IX/MPR/2001 tentang Pembaruan Agraria Dan Pengelolaan Sumber Daya Alam," Pub. L. No. IX/MPR/2001 (2001), https://onedrive.live.com/download?cid=61919CCED358D3B8&resid=61919CCED358D3B8%217513&authkey=AO06_WwrP0ivXXI&em=2.

[3] Amrih Jinangkung, interview through Joint Coffee Session: Transfer of knowledge through a cup of coffee with L. Amrih Jinangkung, S.H., LL.M. (Director General for Legal Affairs and International Treaties), February 16, 2023.

[4] Indonesia for Global Justice, "Indonesia Terminated 18 BITs," *Indonesia for Global Justice*, March 24, 2015, https://igj.or.id/indonesia-terminated-18-bits/.

[5] Korzun, "The Right to Regulate in Investor-State Arbitration: Slicing and Dicing Regulatory Carve-Outs," 389.

[6] New Zealand and European Union, "Free Trade Agreement Between the European Union and New Zealand" (n.d.), art. 19.2 1, https://policy.trade.ec.europa.eu/eu-trade-relationships-country-and-region/countries-and-regions/new-zealand/eu-new-zealand-agreement/text-agreement_en.

[7] The Government of the Kingdom of Morocco and the Government of the Federal Republic of Nigeria, "Reciprocal Investment Promotion and Protection Agreement Between the Government of the Kingdom of Morocco and the Government of the Federal Republic of Nigeria" (2016), art. 13 (12), https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/5409/download.

[8] Korzun, "The Right to Regulate in Investor-State Arbitration: Slicing and Dicing Regulatory Carve-Outs," 391–92.

[9] Korzun, "The Right to Regulate in Investor-State Arbitration: Slicing and Dicing Regulatory Carve-Outs," 394.

A Party may elect to deny the benefits of Section B of Chapter 9 (Investment) with respect to claims challenging a tobacco control measure of the Party. Such a claim shall not be submitted to arbitration under Section B of Chapter 9 (Investment) if a Party has made such an election.[1]

Here, the formation of the TPP is aimed to carve-out ISDS challenges to tobacco control measures from the extent of the treaty's protection. This is considered to be a partial carve-out since it does not repudiate the entire protection benefits. Rather, it exists to ensure that such challenges are addressed by domestic courts, and not international arbitration. These kinds of partial carve-outs may be a better option than full carve-outs since they strip the risk of Regulatory Chills associated with ISDS, without having to remove the protection for the investors completely. Consequently, there is a higher chance for them to be agreed upon by states.[2] Further, based on their nature, carve-outs represent the stronger end of the preservation of regulatory interest since they deny the application of the treaty. Carve-outs, in consequence of its strong nature, have been specifically urged with regards to climate regulations.[3] The carve-outs may furnish a good balance between the regulatory space and investment protection for the whole Indonesia's mining sector and environmental regulations. In light of that, it is advisable for Indonesia to make sure that it has a clear standard for the application of its exceptions, or opt for exclusions whenever possible in its investment agreements.

5.1.3. The Incorporation of International Obligations

Recent investment agreements have also been focusing on ensuring the existence of regulatory space in the environmental sector by "reaffirming" their international obligations according to other environmental treaties. Article 19.6 of the EU-New Zealand FTA and Article 6 (6) of the Netherlands Model BIT (2019) are the proper examples for this case. Both of these provisions have explicitly incorporated the Paris Agreement as well as all obligations set out within. The incorporation of the regarding international obligations would operate in a similar fashion to exceptions and exclusions, but with regards to international agreements. However, doubts may arise on whether the arbitral tribunals are equipped enough to interpret such necessity of the climate-based policies, which are being challenged. The fact that different tribunals may interpret the various international agreements differently may give birth to further inconsistency.

5.1.4. The Elucidations of the Existing Formulations

Formulations of older investment agreements may also add uncertainty to ISDS proceedings. For instance, the Indonesia-Netherlands BITs, which has been discussed above, regulates the treatment of investment through this provision:

Each Contracting Party shall ensure fair and equitable treatment of the investments of nationals of the other Contracting Party and shall not impair, by unreasonable or discriminatory measures, the operation, management, maintenance, use, enjoyment or disposal thereof by those nationals…[4]

Such general formulation of a Fair and Equitable Treatment ("**FET**") clause does not elaborate on how we can interpret "discriminatory" or "unreasonable". As a consequence, different arbitral tribunals may give birth to different interpretations for which public policy is deemed as "discriminatory" and "unreasonable", noting that there has been little in the way of consistent jurisprudence. In the event that the arbitral tribunals were to draw from the existing bodies of jurisprudence, the thresholds adopted may vary greatly.[5] Previous works on the subject has highlighted the crucial nature of setting a clear limitation on the FET standard, in the risk to state's regulatory space should such limitation fails to be clearly set. In fact, the case of *IMFA v. Indonesia* was decided on a determination of the FET standard.[6]

In recognition of this, FET and Expropriation clauses, that are generally invoked for the purpose of challenging public welfare policies, may be drafted in more particular details. This will ensure consistency in its application. A practical example can be seen in the EU-Canada CETA, which stipulates specific measures which may breach this treatment standard.[7] The list of measures is an exhaustive one, with the possibility of additional measures to be added should the parties agree to it. While the formulation would need to take the specified needs of the parties into consideration, this type of clear-cut formulation would help in reducing the uncertainty which comes with investment arbitration.

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[1] "Trans-Pacific Partnership Agreement" (2016), art. 29.5, https://ustr.gov/sites/default/files/TPP-Final-Text-Exceptions-and-General-Provisions.pdf.

[2] Joshua Paine and Elizabeth Sheargold, "A Climate Change Carve-Out for Investment Treaties," *Journal of International Economic Law* 26, no. 2 (2023): 296, https://doi.org/10.1093/jiel/jgad011.

[3] Tienhaara, "Regulatory Chill in a Warming World: The Threat to Climate Policy Posed by Investor-State Dispute Settlement," 249–50; Paine and Sheargold, "A Climate Change Carve-Out for Investment Treaties," 303–4.

[4] Agreement between the Government of the Kingdom of the Netherlands and the Government of the Republic of Indonesia on Promotion and Protection of Investment, art. 3.

[5] Tienhaara, "Regulatory Chill in a Warming World: The Threat to Climate Policy Posed by Investor-State Dispute Settlement," 244–45.

[6] Bayu Fadhlurrahman, Huala Adolf, Prita Amalia "Limiting Investor Legitimate Expectations In Foreign Investment To Ensure State Economic Sovereignty: Implementations Of The Principle In Indian Metals & Ferro Alloys (IMFA) V Republic Of Indonesia.", *International Jounral of Business, Economics and Law,* 23, no. 1 (2020): 59-60.

[7] European Union and Canada, "EU-Canada Comprehensive Economic and Trade Agreement" (2017), art. 8.10, https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:22017A0114(01)#d1e3692-23-1.

5.1.5. The Elimination and the Limitations of MFN Clauses

Most Favored Nation ("**MFN**") and how the arbitral tribunals have applied them are the important factors which contribute to the general uncertainty in the investment arbitration. The existence of MFN clauses makes certain on how the investors from either state party is able to obtain treatment as favorable as afforded to investors from third states that are in investment agreements with either state party. These clauses have been interpreted to permit an investor to "import" a more favorable clause from another treaty, even when it comes to dispute resolution clauses.[1] The broad interpretation of the MFN clauses entails to unpredictable disputes since the parties would not be able to precisely predict the extent of their own liabilities.[2]

Taking into consideration the aforesaid elucidation, there is a sound argument for the removal or strict limitation of the MFN clause. As a matter of fact, the Indian Model BIT (2015) has removed MFN entirely.[3] Further, the MFN clause scope was severely limited the Comprehensive Economic and Trade Agreement ("**CETA**") to exclude procedures of investment dispute and obligaation in other treaties not enforced by the parties.[4] Regardless, due to the way arbitral tribunals tend to interpret them, newer MFN clauses remains able to pose the risk of generating uncertainty. Arbitral tribunals have the tendency to see MFN clauses as a monolith that allows claimants to import substantive provisions from other treaties, even when the clauses themselves have been more cautiously formulated.[5] Hence, Indonesia should strive to remove MFN clauses from its BITs.

6. Conclusion

During policy making, states needs to balance investors' interest and regulatory needs. In accordance with the ISDS cases which has involved Indonesia, this writing has shown through the case of *Nusa Tenggara v. Indonesia* that in the event the investment agreements have failed strike this balance, the host state's ability to implement its regulations can be significantly reduced. As a consequence, during the negotiations of the new investment agreements, Indonesia would need to take into consideration on its current and future regulatory needs. The effort of preserving the regulatory space can be achieved through the incorporation of the exclusions as necessary, exceptions that reiterate the host state's right to regulate, incorporating international obligations, greater elaboration of the existing formulation of FET and Expropriation clauses, as well as limiting or eliminating MFN provisions in order to bring forth better clarity. The incorprations of these elements may ensure that investment agreements provide an impetus of growth while minimizing Regulatory Chill.

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[1] M. Sornarajah, *The International Law on Foreign Investment*, 3rd ed. (Cambridge: Cambridge University Press, 2010), 204–5.
[2] United Nations Conference on Trade and Development, "Most-Favoured-Nation Treatment," UNCTAD Series on Issues in International Investment Agreements II (New York and Geneva: United Nations, 2010), 105–6, https://unctad.org/system/files/official-document/diaeia20101_en.pdf.
[3] Tienhaara, "Regulatory Chill in a Warming World: The Threat to Climate Policy Posed by Investor-State Dispute Settlement," 244.
[4] EU-Canada Comprehensive Economic and Trade Agreement, art. 8.7 (4).
[5] Simon Batifort and J. Benton Heath, "The New Debate on the Interpretation of MFN Clauses in Investment Treaties: Putting the Brakes on Multilateralization," *American Journal of International Law* 111, no. 4 (2017): 907–8, https://doi.org/doi:10.1017/ajil.2017.77.

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