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The Relationship of EU Law and Bilateral Investment Treaties of EU Member States: Treaty Conflict, Harmonious Coexistence and the Critique of Investment Arbitration

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ACADEMIC DISSERTATION

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Summary

Investment treaties have come under fire in the past few years in Europe. The critics are arguing that investment treaties constitute a threat to the policy autonomy of 'host' states as they allow foreign investors to challenge domestic regulatory measures adopted in sensitive areas of public policy, such as protection of the environment and public health. Investment treaties provide access to ad hoc arbitration where private arbitrators determine whether legislative, administrative and judicial acts of the host state comply with investment protection standards and whether the claimant investor is entitled to compensation. Thus far, investors have raised more than 800 known claims against more than hundred states, with tribunals awarding hundreds of millions of dollars in compensation to investors in a number of high-profile cases. For the critics, the ability of private arbitrators to determine the appropriateness of a wide range of domestic policy measures (coupled with their ability to award compensation) constitutes an illegitimate intervention in the domestic political process. On the other side of the argument, the proponents of investment treaties argue that the critique is based on misunderstandings and hyperbole, with arbitral tribunals showing a high measure of deference to the public interest of host states when reviewing measures that investors have challenged. More generally, the proponents argue that investment treaties protect the fundamental rights of investors against arbitrary exercises of public power, promote the international rule of law, and increase investor confidence by guaranteeing a more stable regulatory framework for transnational economic activity.

Alongside this heated debate, there is another related debate that concerns the relationship of EU law and bilateral investment treaties (BITs) of EU member states. In this more technical debate, the EU Commission argues that BITs concluded between two member states (intra-EU BITs) are incompatible with EU law and have to be terminated. The Commission argues that arbitration under intra-EU BITs breaches the principle of non-discrimination and the exclusive jurisdiction of the European Court of Justice (ECJ) to provide authoritative interpretations of EU law. These arguments form the basis of the pending infringement proceedings against five member states, and the Commission has raised the same arguments in a number of arbitrations where EU investors have brought claims against member states under intra-EU BITs. Arbitral tribunals have not, however,

concluded with the Commission. In their view, intra-EU BITs protect the fundamental rights of investors and are fully compatible with EU law. As investment treaties provide broader and more effective protection to investors than EU law and national laws of the member states, they form a complementary remedy for investors within the internal market.

The purpose of this thesis is to combine and provide an analysis of these two seemingly distinct debates concerning the future of investment treaties in Europe. Existing scholarship has provided less than in-depth analyses of the Commission's arguments on the relationship of EU law and member state BITs. Hence, as a first matter, I provide a comprehensive analysis of the arguments that intra-EU BITs breach the principle of non-discrimination and the autonomy of the EU legal order. The analysis shows that the case law of the ECJ provides no watertight answers, and that the Court could go either way depending on which of the relevant cases it chooses as its frame of reference. I suggest, however, that the future of intra-EU BITs should not be decided on the basis of the Commission's formal arguments, but on the basis of an analysis of the general arguments for and against investment treaties outlined above. As noted, the proponents are arguing, for example, that investment treaties are akin to human rights treaties and promote the international rule of law, whereas the critics argue that the treaties promote narrow corporate interests at the expense of the public interest and undermine the regulatory autonomy of host states.

To understand the plausibility of these opposing arguments, I analyze both the assumptions that undergird them as well as the materials on which they rely. The analysis shows that the opposing arguments are based on anecdotal evidence and unverified assumptions, rather than on empirically proven hypotheses or on detailed analyses of the case law that arbitral tribunals have hitherto produced. I argue that the critics and proponents entertain simplified assumptions about the purposes and implications of investment treaties, with both sides ignoring countervailing evidence. My discussion also shows that the disagreement between the opposing sides is inherently political, as the opposing arguments rely on contrasting understandings about how state-market relations should be arranged in the global economy. In other words, the disagreement is not about the level of deference that arbitral tribunals should give to domestic policy, but about the allocation of power between domestic and international institutions. This suggests that whichever way the ECJ

goes in its upcoming judgment concerning intra-EU BITs, it will necessarily send a political message to the various stakeholders involved in investment law debates in Europe. If the Court finds that the treaties are compatible with EU law, the critics will see it as a capitulation to transnational economic forces and as reflecting the technocratic nature and ethos of the European project, whereas the proponents will see it as a responsible exercise of judicial discretion which understands the importance of investor confidence for the future prosperity of Europe. Conversely, if the Court finds that intra-EU BITs are incompatible with EU law, the critics will see it as a symbolic victory in the broader battle against further trade and investment liberalization, whereas the proponents will view it as a naïve attempt to placate some of the anti-globalization sentiment that is alive and well in certain segments of the European body politic. The broad argument of the thesis is simple. The relationship of EU law and investment treaties should not be discussed in the current technocratic and legalistic register but in a register that acknowledges the political nature of the relationship and foregrounds the different political visions upon which the opposing arguments are based.

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Prologue

In December 2013, the *Micula* tribunal rendered its final award and ordered Romania to pay around 85 million euros (plus substantial interest) in damages to a group of investors for breach of the fair and equitable treatment standard of the bilateral investment treaty (BIT) between Romania and Sweden.¹ At the heart of the dispute was a set of investment incentives designed to facilitate economic development in Romania's 'disfavored' regions. Romania had adopted the incentives in the late 1990s, and during its EU accession talks it became evident that the incentives constituted illegal state aid under EU law. As a result of the EU Commission's gentle arm-twisting, most of the incentives were revoked in 2005, some two years before Romania acceded to the EU. This led the investors to claim that their rights under the BIT had been violated, and while the award has many interesting features,² the tribunal, in essence, concurred with the argument that the revocation had breached the investors' 'legitimate expectations' and therewith the fair and equitable treatment standard.³ As a response, the Commission issued a suspension injunction,⁴ which debarred Romania from paying the award pending the Commission's decision on the compatibility of such payment with EU state aid rules. In March 2015, the Commission made a formal decision that Romania's compliance with the award constitutes illegal state aid and obligated Romania to collect the amounts which the claimants had succeeded in recovering.⁵ The *Micula* claimants, in turn, challenged both the injunction and the state aid

¹ *Ioan Micula, Viorel Micula, S.C. European Food S.A, S.C. Starmill S.R.L. and S.C. Multipack S.R.L. v. Romania*, ICSID Case No. ARB/05/20, Award, 11 December 2013.

² One of them being that the principal claimants, the Micula brothers, were born and raised in Romania, had migrated to Sweden in the 1980s and then acquired Swedish nationality in mid-1990s (and simultaneously renounced their Romanian nationality), after which they had mostly lived and worked in Romania. The Swedish government argued that the brothers had not demonstrated that they had Swedish nationality or, alternatively, that they had no effective link to Sweden, but the tribunal dismissed these arguments and concluded that the brothers 'are and have been Swedish nationals at all times relevant to the Tribunal's jurisdiction in this dispute.' See *Ioan Micula, Viorel Micula, S.C. European Food S.A, S.C. Starmill S.R.L. and S.C. Multipack S.R.L. v. Romania*, ICSID Case No. ARB/05/20, Decision on Jurisdiction and Admissibility, 24 September 2008, para. 106.

³ More specifically, the tribunal saw that the claimants' investment decision was made in reliance on Romania's promise to hold the incentives in force for a period of ten years. See *Micula* award, supra note 1, pp. 181-195.

⁴ The decision was taken under Art. 11(1) of Council Regulation (EC) No 659/1999, which provides detailed rules for the application of Article 93 of the EC Treaty (now Article 108 of the Treaty on the Functioning of the European Union (hereinafter TFEU)). See Council Regulation (EC) No 659/1999 of 22 March 1999 laying down detailed rules for the application of Article 93 of the EC Treaty, OJ L 83, 27.3.1999, pp. 1-9.

⁵ Commission Decision (EU) 2015/1470 of 30 March 2015 on State aid, OJ L 232, 4.9.2015, pp. 43-70.

decision before the General Court⁶ and continue to seek the award's enforcement in a number of EU and non-EU jurisdictions with the aim of seizing and liquidating Romanian assets located therein.⁷ In parallel with these public proceedings, Romania sought to annul the award under the applicable arbitration rules, but its petition was rejected in February 2016.⁸

Micula embodies the complexities in the relationship of EU law and EU member state BITs. State aid is just one area where BIT provisions or decisions of arbitral tribunals can conflict with EU law, and both extra-EU BITs (i.e. treaties with third states) and 'intra-EU' BITs (treaties between two EU member states) can trigger such conflicts. In the *Micula* proceedings the EU Commission argued that if the tribunal finds in the claimants' favor, the award will be unenforceable under EU law as it conflicts with EU state aid rules, but the tribunal held that it was 'inappropriate' for it 'to base its decisions...on matters of EU law that may come to apply after the Award has been rendered'.⁹ Conversely, in the state aid proceedings one question was whether EU law protects the claimants' right to receive compensation under the BIT, but the Commission held that EU state aid rules applied fully to the *Micula* award.¹⁰ These opposing arguments and outcomes reflect how the EU institutions and arbitral tribunals apply different legal rules to resolve conflict arguments in a way that gives priority to the treaty under which they were created. This suggests that treaty regimes are inclined to have a 'ghetto mentality', with each regime defending its turf from intrusions by rival regimes.¹¹

Situations where a member state's EU law obligations come in the way of complying with its obligations under a BIT are just one aspect of the problematique of member state BITs. The Commission has pressed the member states to terminate their mutual BITs, including

⁶ Case T-646/14, *Micula e.a. v Commission*, ECLI:EU:T:2016:135 (the case, which concerned the request to annul the Commission's suspension injunction decision was discontinued in February 2016 at the request of the applicants); Case T-694/15, *Micula e.a. v Commission*, OJ C 68, 22.2.2016, pp. 30-32 (this latter case is pending and concerns the annulment of the Commission's state aid decision).

⁷ For some information on the status of the enforcement proceedings, see Clovis Trevino, 'As tribunal is finalized for second *Micula v. Romania* ICSID arbitration, new developments come in relation to earlier award', *IAReporter News Service*, 1 May 2015.

⁸ *Ioan Micula, Viorel Micula, S.C. European Food S.A, S.C. Starmill S.R.L. and S.C. Multipack S.R.L. v. Romania*, ICSID Case No. ARB/05/20, Award on Annulment, 26 February 2016. The official title of the ICSID Convention is Convention on the Settlement of Investment Disputes Between States and Nationals of Other States, 575 UNTS 159.

⁹ *Micula* award, supra note 1, para. 340.

¹⁰ *Micula* state aid decision, supra note 5, para. 127.

¹¹ The phrase 'ghetto mentality' is from David Kennedy, 'The Mystery of Global Governance', 34 *Ohio Northern University Law Review* (2008), pp. 827-860, at 828.

the Romania-Sweden BIT, on a number of grounds. In the Commission's view, intra-EU BITs amount to an 'anomaly within the EU internal market'¹² as EU law provides adequate or similar type of protection to EU investors. In legal terms the Commission has raised two main arguments. First, intra-EU BITs breach the principle of non-discrimination as they provide protection only to the nationals of the contracting states (to the exclusion of nationals of other member states), and, second, intra-EU BITs breach the exclusive jurisdiction of the European Court of Justice (ECJ)¹³ to interpret EU law under Article 344 of the Treaty on the Functioning of the European Union (TFEU),¹⁴ as arbitral tribunals may have to interpret EU law without the ECJ's involvement, which threatens the uniform interpretation and autonomy of EU law.¹⁵ However, the bulk of member states disagrees with the Commission and has refused to take any action, which prompted the latter to start infringement proceedings against five member states in June 2015, and similar proceedings are being planned against other member states as well.¹⁶ The Commission's approach has received its share of criticism. One commentator noted that the termination of intra-EU BITs 'as demanded by the EU Commission would...deprive EU citizens of subjective rights...[and] would be an unparalleled occurrence as regards fundamental principles of the European Union'.¹⁷ This view is fueled by the perception that a number of member states suffer from administrative incapacity and corruption and do not necessarily have 'independent courts that decide cases in accordance with pre-established rules of law'.¹⁸ Under such circumstances, the argument proceeds, investment arbitration may provide the

¹² The quote is from the Commission's *amicus curiae* submission to the *Eureko* tribunal. See *Eureko v. Slovak Republic*, PCA Case No. 2008-13, Award on Jurisdiction, Arbitrability and Suspension, 26 October 2010, para. 177.

¹³ Article 19 of the Treaty on European Union (TEU) provides, as amended by the Treaty of Lisbon, that the 'Court of Justice of the European Union shall include the Court of Justice, the General Court and specialised courts'. Hence, it is more appropriate to continue to abbreviate the Court of Justice as ECJ instead of CJEU.

¹⁴ Consolidated version of the Treaty on the Functioning of the European Union, OJ C 326, 26.10.2012, pp. 47-390

¹⁵ See e.g. *ibid.*, paras. 175-196. The question whether arbitral tribunals are 'ordinary courts' in the meaning of Article 267 TFEU (i.e. whether they can submit preliminary questions to the ECJ) is addressed below in Chapter 5.

¹⁶ See European Commission press release, 'Commission asks member states to terminate their intra-EU bilateral investment treaties', IP/15/5198, 18 June 2015.

¹⁷ See Christian Tietje, 'Bilateral Investment Protection Treaties between EU Member States (Intra-EU BITs) as a Challenge in the Multi-Level Legal System', in Christian Tietje, Gerhard Kraft and Mathias Lehmann (eds.), *Beiträge zum Transnationalen Wirtschaftsrecht*, No. 104 (2011, CL-146), p. 19.

¹⁸ See Charles N. Brower and Stephan W. Schill, 'Is Arbitration a Threat or a Boon to the Legitimacy of International Investment Law?', 9 *Chicago Journal of International Law* (2009), pp. 471-498, at 479. Similarly, Tietje notes that intra-EU BITs 'contribute to the elevation and intensification of the legal protection of economic operators in the Internal Market. Similar to international investment law, intra-EU BITs stabilize and strengthen the rule of law in the Internal Market'. See Christian Tietje, 'Bilateral Investment Treaties Between EU Member States (Intra-EU BITs) - Challenges in the Multilevel System of Law', 10 *Transnational Dispute Management* (2013/Issue 2), p. 23.

only (effective) remedy against arbitrary exercises of public power. More generally, the proponents argue that investment treaties and arbitration are akin to human rights treaties and adjudication, with arbitral tribunals 'relying on and developing human rights jurisprudence' when deciding investment disputes.¹⁹

These arguments suggest that conflicts between EU law and member state BITs should be resolved on the basis of the values that underpin the EU constitutional order, rather than on the basis of specific primary law rules, such as the principle of equal treatment. The ECJ has implied that the 'EU constitutional order consists of some core principles which may prevail over provisions of the [founding] Treaties,'²⁰ and among these 'principles' are the foundational values of the EU, which are now listed in Article 2 of the Treaty on European Union, namely, 'respect for human dignity, freedom, democracy, equality, the rule of law and respect for human rights'.²¹ The idea that values should determine how treaty conflicts are resolved foregrounds the final aspect of the problematique of member state BITs.²² Although arbitration clauses have been a standard part of BITs from the 1980s onward, investment arbitration has faced an avalanche of criticism within the EU only in the past few years, in particular in the context of the transatlantic free trade negotiations. Across Europe, the public and political debate on investment treaties has followed a similar script. The critics argue that the inclusion of an investment chapter in the transatlantic trade agreements provides unnecessary special privileges to foreign investors and undermines the ability of governments to regulate in the public interest. In their view, arbitral tribunals focus solely on the economic impact that host state measures have on investments and downplay or ignore the attendant public interest, such as public health and the protection of the environment. Moreover, arbitral tribunals may award sizeable compensation to investors for measures that enjoy widespread legitimacy among domestic constituencies. As a prominent critic put it, 'investment arbitration has become an instrument of protection for foreign investment to the exclusion of other interests such as the environment, health, access to essentials like medicines, electricity and water, positive discrimination to

¹⁹ Charles N. Brower and Sadie Blanchard, 'What's in a Meme? The Truth about Investor-State Arbitration: Why It Need Not, and Must Not, Be Repossessed by States', 52 *Columbia Journal of Transnational Law* (2014), pp. 689-777, at 689-690 and 757.

²⁰ See Allan Rosas and Lorna Armati, *EU Constitutional Law. An Introduction* (Hart, 2012), p. 54.

²¹ Article 2 of the Treaty on the European Union provides that the 'Union is founded on the values of respect for human dignity, freedom, democracy, equality, the rule of law and respect for human rights, including the rights of persons belonging to minorities.'

²² The idea that values should determine how treaty conflicts are resolved is one of the themes in *Jan Klabbers, Treaty Conflict and the European Union* (Cambridge University Press, 2009).

advantage underprivileged groups and human rights'.²³ This view stands in stark contrast to the above narrative according to which investment treaties protect fundamental rights and are in line with the EU's foundational values. But how plausible are these two opposing perceptions to begin with? Is it possible to find common ground over the values and interests that investment treaties seek to promote or is this, unavoidably, a perspectival matter? And how should the question of values and interests affect the resolution of conflicts between EU law and member state BITs?

²³ M. Sornarajah, *Resistance and Change in International in the International Law on Foreign Investment* (Cambridge University Press, 2015), p. 392.

1. Introduction

1.1. The Substantive Context of the Study

The purpose of this thesis is two-fold. The first purpose is to provide an analysis of the formal conflict scenarios that member state BITs and EU law may give rise to.²⁴

Schematically speaking, the relevant conflict scenarios can be divided into two broad categories. The first category is composed of 'primary conflicts', which refers to the argument that arbitration under member state BITs is 'inherently' incompatible with EU law. This understanding is at the heart of the Commission's main arguments on intra-EU BITs, namely, that they breach both the autonomy of the EU legal order and the principle of non-discrimination as established under primary EU law and in the case law of the ECJ.²⁵ The second category is composed of 'regulatory conflicts', which refers to potential conflicts stemming from domestic implementation of EU legal acts and other decisions of national authorities related to the requirements of EU law, which an investor challenges before an arbitral tribunal. Regulatory conflict arguments are not premised on a conflict between BIT arbitration clauses and EU law, but on conflicts between one or more substantive BIT provisions and specific emanations of the *droit communautaire dérivé*. Yet the two conflict categories are in part intertwined; if and when an investor raises a claim against a member state measure that relates to an EU act, the latter may raise that EU act in the arbitral proceedings, which breaches, in the Commission's view at least, the exclusive jurisdiction of the ECJ and threatens the autonomy of the EU legal order.

Put differently, regulatory conflict scenarios are part of the evidence which is relevant for determining whether investment arbitration breaches the autonomy of EU law. Given this, as well as the breadth of potential conflict scenarios between secondary EU law and BIT protection standards, I will subsume my discussion on regulatory conflicts into the discussion on primary conflicts. Providing an extensive discussion on regulatory conflicts

²⁴ I will use the term EU law regardless of the time period to which the discussion relates. Terms such as 'Community law' and 'EC law' will only appear in citations. I have incorporated materials that were available before 15 September 2017, and materials that became available after this date receive only a few incidental remarks.

²⁵ Article 19 of the Treaty on European Union (TEU) provides, as amended by the Treaty of Lisbon, that the 'Court of Justice of the European Union shall include the Court of Justice, the General Court and specialised courts.' Hence, it is more appropriate to continue to abbreviate the Court of Justice as ECJ instead of CJEU. See *Consolidated Version of the Treaty on the European Union*, OJ C 326, 26.10.2012, pp. 13-390

would inflate the length of the thesis well above the faculty guidelines, so my purpose is to point out the main rules and principles that come into play, rather than to elaborate on the substantive areas of secondary law where regulatory conflicts may arise. As a whole, the questions that the analysis seeks to answer include the following: do BIT arbitration clauses breach the EU law principles of non-discrimination and/or the autonomy of the EU legal order? In which ways can BIT protection standards conflict with secondary EU law? If the existence of primary or regulatory conflicts is established, what are the applicable conflict rules under EU law and international law? *Micula* shows that it is necessary to analyze the scenarios from the perspectives of EU law and international (investment) law, and Chapters 3 to 5 will take these two perspectives.

As noted, these are technical questions in the sense that their resolution does not require taking a stand either on the critique of investment treaties and arbitration or on the arguments with which they are defended. One might also argue that the two issues should be addressed separately because the substantive questions are distinct: the conflict arguments are the stuff of legal dogmatics, whereas the pros and cons of investment treaties are predominantly a matter of politics, at least until the relevant issues are settled in law. But, clearly, the critique is both legal and political in the sense that the procedural and substantive rules that apply in investment arbitration (together with the background of many arbitrators in private sector legal practice) are perceived as resulting in a pro-investor bias in the jurisprudence of arbitral tribunals, which constrains the regulatory autonomy of host states. Generally speaking, discussing the treaty conflict scenarios in isolation of broader institutional questions and the interests and values that undergird the critical debate not only lacks ambition but makes it difficult to take sides with respect to the conflicts' resolution. Hence, the second purpose of the thesis is to combine the doctrinal debate on treaty conflicts with the contentious debate on the pros and cons of the investment treaty regime. What the linking of the two debates strives to achieve is to, first, create an understanding of the values and interests that investment treaties are understood as promoting, and, second, to provide a critical analysis of the assumptions and evidence upon which the arguments depend. To give an example, the Commission has argued that intra-EU BITs breach the principle of non-discrimination, which renders them inapplicable as a matter of EU law. Another, more general argument is that intra-EU BITs are unnecessary within the internal market because EU law provides similar type of protections. The first argument focuses on equal treatment, whereas the second asserts that

investors receive adequate protection within the internal market. Neither argument is based on an analysis of the alleged pros and cons of investment treaties, as they either prioritize a third value (equal treatment) or assume that investment treaties protect the fundamental rights of investors and nothing else. By ignoring the critical debate on investment treaties, the Commission's approach looks overly technocratic and problematic from the perspective of the foundational values of the EU. My general goal is to get a grasp of the relative strengths and weaknesses of the opposing arguments raised in the critical debate. This should not only allow situating the answers of the formal legal analysis (the first purpose of the thesis) over the relationship of member state BITs and EU law into a broader context, but also say something about the future of investment treaties in Europe; are they as useful and necessary as the proponents claim, or do they pose a threat to the foundational values of the EU as the critics claim, or is the truth somewhere in between. Answering this large question is no doubt a difficult task, but also critically important for the legitimacy of the EU's future investment policy as it should illustrate to what extent the idea of the EU as a constitutional order, grounded on fundamental values, holds water in this particular context.

To my knowledge, no book-length contributions on the relationship of EU law and member state BITs have been written. Existing scholarship consists of articles and monograph chapters focusing on specific aspects of the relationship, and given the shortness of such texts they can only scratch the surface of this multifaceted and complex topic. Hence, many of the formal questions raised above have not received in-depth analysis, and in many cases the conclusions of commentators turn out to be tentative upon closer scrutiny. For example, the case law of the ECJ is crucial to understanding whether BIT arbitration clauses breach the principle of non-discrimination *as a matter of EU law*. Many commentators rely on that case law when inferring that the clauses are either compatible or incompatible with EU law, but these conclusions are often less than plausible as the cases and their context are presented in a summary fashion, raising the question of whether they are relevant in the BIT context in the first place.²⁶ Put differently,

²⁶ Representative works include Angelos Dimopoulos, 'The Validity and Applicability of International Investment Agreements between EU Member States under EU and International Law', 48 *Common Market Law Review* (2011), pp. 63-93; Thomas Eilmansberger, 'Bilateral Investment Treaties and EU Law', 46 *Common Market Law Review* (2009), pp. 383-429; Steffen Hindelang, 'Circumventing Primacy of EU Law and the CJEU's Judicial Monopoly by Resorting to Dispute Resolution Mechanisms Provided for in Inter-se treaties? The Case of Intra-EU Investment Arbitration', 39 *Legal Issues of Economic Integration* (2012), pp. 179-206; August Reinisch, 'Articles 30 and 59 of the Vienna Convention on the Law of treaties in Action:

existing scholarship does not answer conclusively to what extent the case law of the ECJ is relevant and (if it is relevant) what implications it has for member state BITs as a matter of EU law *and* international law. Another observation is that none of the existing contributions connect the doctrinal debate on the different conflict scenarios with the critical debate on the purposes and implications of investment treaties, which is a central objective of this thesis.

1.2. Structure of the Thesis

With the above in mind, the structure of the work is as follows. Chapter 2 starts with a general introduction to the central elements of treaty conflicts, in particular to the alleged conflicts between EU law and member state BITs. The topics under discussion include: how are treaty conflicts defined in doctrine and what is their relevance in the present context, what are the main conflict rules and principles under EU law and international law, what is the relevance of the distinction between intra-EU and extra-EU BITs, and what role can courts and tribunals play in the resolution of treaty conflicts. As to the last of these, I discuss a number of structural and ad hoc factors that explain why courts and tribunals are more likely to reject conflict arguments than to uphold them. I also provide a few introductory remarks on the (EU law) question of competence, as it highlights how EU law imposes constraints on the treaty-making capacity of the member states. Chapter 3 discusses arbitration cases where the Commission and respondent EU member states have raised primary conflict arguments to challenge the jurisdiction of the arbitral tribunals. Their basic argument is that *intra-EU* BITs breach the principle of non-discrimination and the exclusive jurisdiction of the ECJ to interpret EU law, with the consequence that the clauses have become inapplicable under the *lex posterior* rule enshrined in Articles 30(3) and 59(1) of the Vienna Convention on the Law of Treaties (VCLT). Arbitral tribunals have rejected these conflict arguments on a number of grounds. They have held, for example, that EU law and BITs are 'complementary' legal frameworks which can continue to co-exist as before, and in their view the problem of discrimination is resolved by extending BIT privileges to all EU investors. The final part of Chapter 3 provides an

The Decision on Jurisdiction in the *Eastern Sugar* and *Eureko* Investment Arbitrations', 39 *Legal Issues of Economic Integration* (2012), pp. 157-177; Tietje, 'Bilateral Investment Protection Treaties between EU Member States, supra note 17; Hanno Wehland, 'Schiedsverfahren auf der Grundlage bilateraler Investitionsschutzabkommen zwischen EU-Mitgliedstaaten und die Einwendung des entgegenstehenden Gemeinschaftsrechts', 6 *SchiedsVZ - Zeitschrift für Schiedsverfahren* (2008), pp. 222-234.

introductory analysis of the tribunals' findings and here many of the topics discussed in Chapter 2 will resurface. The final section also provides some preliminary remarks on the type of value and interest claims that undergird the tribunals' conclusions, a topic which will re-emerge in Chapter 7.

The discussion in Chapter 3 is a prelude to Chapters 4 and 5 where I provide a thorough analysis of the argument that BIT arbitration clauses breach the principle of non-discrimination and autonomy of the EU legal order *as a matter of EU law*. The case law of the ECJ is at the heart of the discussion, and the analysis focuses on cases raised in scholarship and in some of the arbitrations discussed in Chapter 3. One conclusion is that commentators and arbitral tribunals have often provide a less than comprehensive analysis of the cases by not paying adequate attention to their specific context, which has led, arguably, to false analogies between the cases and the relevant BITs. As to discrimination, the main conclusion is that BIT arbitration clauses appear to breach the principle of non-discrimination, although the Court's case law provides some support to the opposing conclusion as well. If member state BITs constitute prohibited discrimination, the central question is what implications such finding carries *both* as a matter of EU law and international law. Should, for example, the scope of member state BITs be extended so as to cover all EU investors, or, conversely, should the member states terminate intra-EU BITs? Or should the treaties be allowed to remain in force on the assumption that they protect the fundamental rights of investors? And is discrimination an internal EU law problem, having no impact on the status of member state BITs as a matter of international law?

On autonomy, the central conclusion is that the ECJ could go either way depending on the message it wants to send to the member states. The Court has construed the autonomy doctrine in a piecemeal fashion, and some of its central dicta are expressed in abstract language, which makes it difficult to understand the scope of the findings and their relevance for member state BITs. I start the analysis by looking at a number of arbitrations where the parties have invoked specific EU law instruments. These cases are directly relevant to the analysis as they show how arbitral tribunals have engaged with EU law in their deliberations. Some of these cases are also relevant because they raise the prospect of regulatory conflicts; when an investor has challenged a measure, which was adopted so as to comply with an EU act, there is a potential conflict between the respondent member

state's obligation to implement the EU act as a matter of EU law and its obligation to treat the investment in a certain way under the relevant BIT. I will provide an outline of the main rules and principles in respect of regulatory conflicts and look at the basic approaches that arbitral tribunals and the EU institutions have taken or are likely to take.²⁷ As to my conclusion on autonomy, the analysis shows that a strict reading of the Court's reasoning implies that arbitral tribunals have engaged with EU law (and potentially will continue to do so) in ways that may be problematic from the perspective of the autonomy of the EU legal order. But this potential 'threat' can be resolved in a number of ways and I will look at a number of issues that either support or undermine the argument that investment arbitration breaches the autonomy of EU law. One such issue is WTO jurisprudence which contains a number of cases where the Dispute Settlement Body has held that specific EU law instruments breach WTO law, but this has not given rise to concerns in respect of the autonomy of EU law. Does this mean, by analogy, that arbitral tribunals too can interpret EU law without threatening the autonomy of EU law or are the two contexts different in some crucial respect?

Chapters 6 and 7 change perspective and provide a general account of the arguments for and against investment treaties. The primary focus of existing scholarship is naturally on the technical and legal aspects of the critique, which relate to the way in which arbitrators are appointed,²⁸ or to the problem of 'double hatting',²⁹ or to forum-shopping, or to lack of consistency in the decisions of arbitral tribunals, or to how awards are not subject to normal appellate review, or to lack of transparency in respect of proceedings and case documentation. Each of these questions is undoubtedly important and would merit a separate discussion, and, arguably, the concerns they reflect could for the most part be resolved through treaty reform, with the Commission's proposal for an investment court system representing one authoritative solution. The relevant scholarship is burgeoning, but

²⁷ While the discussion on regulatory conflicts is not directly relevant for the autonomy analysis, its inclusion is warranted by its practical relevance; such conflicts are likely to arise in arbitral practice in the future as well.

²⁸ For a comprehensive discussion of the matter in respect of the ICSID Convention, see Maria Nicole Cleis, *The Independence and Impartiality of ICSID Arbitrators. Current Case Law, Alternative Approaches, and Improvement Suggestions* (Brill, 2017).

²⁹ A recent article provides an interesting empirical analysis of the 'normative concerns over double hatting by determining the extent to which it occurs and whether the practice has eased or worsened over time' on the basis of '1039 investment arbitration cases (including ICSID annulments) and the relationships between the 3910 known individuals that form' the investment arbitration community. See Malcolm Langford, Daniel Behn and Runar Hilleren Lie, 'The Revolving Door in International Investment Arbitration', 20 *Journal of International Economic Law* (2017), pp. 1-28.

my own main interest in respect of the critique lies elsewhere, and starts from the premise that the resolution of the above issues would not placate the most ardent critics or address their central concern and neither would treaty reform promote their political agenda. Put differently, if the critique is understood in the above technical or legalistic sense, and if academic lawyers set the terms of the debate, many critics will think that the fox is guarding the henhouse. The point is not that academic lawyers would not be able to provide impeccable analyses of the technical concerns and propose convincing solutions, but that because the critique is at heart political, no amount of treaty reform can address its core. I will elaborate on this approach (and provide justifications to it) in the next section.

What Chapters 6 and 7 strive to do is to look at the plausibility of the general assumptions that undergird the arguments for and against investment treaties. The analysis will provide a summary of the relevant empirical evidence as well as of the other reference points (such as individual awards) on which the different arguments are grounded. As noted in the previous section, this analysis paves the way for understanding how the critical debate should be taken account of in the context of member state BITs. I should point out already here that the discussion in Chapters 6 and 7 relies on 'impressionistic' materials in addition to academic sources. The most vocal critics of the investment treaty regime come from non-academic quarters, such as NGOs, who tend to argue in a completely different register than academics. I will nonetheless discuss their arguments in Chapter 6 as they are much more open about their political goals than neutrality-driven academic commentators, although I am certain that some of the latter secretly hold similarly passionate views.

The critics rely on a handful of headline-making cases where the conflict between investor interests and the public interest is evident, with the focus being on the 'legitimacy' of the challenged measure and individual case outcomes. These cases are then argued as reflecting a more general trend in arbitral jurisprudence where tribunals protect narrow corporate interests at the expense of the public interest. The next step in the critics' causal chain associates the investment treaty regime with the downsides and symbols of economic globalization, such as environmental degradation, erosion of faith in the domestic political process and greedy multinationals. I suggest that the critics are not naïve in the sense that they would be unaware of how simplified their account of the investment treaty regime is. In my mind, the purpose of the critique is not to provide neutral, scientific evidence that corroborates the above storyline, but to mobilize political opposition so as to compel

policy-makers, government officials and politicians to share the basic view that investment arbitration constitutes an illegitimate intrusion into the domestic political process. However, it is necessary to problematize this basic storyline and to further flesh out its basic premises. I provide an analysis of two arbitrations that the critics have raised to show how arbitral tribunals either ignore or downplay the public interest of host states. In both cases, political opposition against the claimants' investment played a significant role in the decisions that led the investors to bring claims under the relevant investment treaty. I suggest that the cases can be framed in a number of ways and that the critical framing is not necessarily the most compelling one. I also look at two general arguments that academic commentators have raised to criticize the investment treaty regime. The first argument makes an association between the regime and neoliberalist ideas and policies, and the second argument asserts that investment treaties and arbitration compel states to refrain from legitimate public interest measures for fear of costly litigation - a phenomenon commonly referred to as 'regulatory chill'.

Chapter 7 analyzes four general arguments *for* the investment treaty regime. The first of these argues that investment treaties bear similarities to human rights treaties in that they protect foreign investors from the arbitrary exercise of public power. The proponents refer to a number of cases where foreign investors have suffered injustice and hardship at the hands of host states to highlight the ethical underpinnings of international investment law. Contrary to the critics, the proponents argue that there is still too much state sovereignty around, as government interventions in the marketplace are often arbitrary, discriminatory and/or make no economic sense. I look at the empirical evidence on the treatment of foreign investors as well as analyze the other reference points with which the proponents defend the human rights analogy. If the critics share a worldview where the investment treaty regime takes the side of the bad guys, the proponents share a worldview where foreign investors are the underdogs facing arbitrary treatment in host states. The proponents' view of economic globalization is generally positive, with investment treaties providing a benchmark for what is acceptable government conduct in the global economy. By opening their doors to transnational economic activity, host states have made a bargain under which they concede parts of their sovereignty against the benefits of trade and investment liberalization. While host states are free to adopt policy measures according to their preferences, arbitral tribunals ensure that they give adequate consideration to the interests of foreign investors. In such view, that arbitral tribunals review *all* types of

domestic measures is a natural corollary of the underlying bargain and of the perception where arbitrators are akin to human rights judges enforcing international protection standards.

The second general argument is based on the perception that investment treaties and arbitration promote the rule of law. As a number of arbitral tribunals have held that the fair and equitable treatment standard entails basic due process requirements, the assumption is that host states will engage in institutional reform so as to avoid future claims and liability under investment treaties. While it is easy to create the *impression* that the investment treaty regime promotes the rule of law, there is no empirical evidence that would support the argument. On the contrary, some of the evidence suggests that investment treaties may decrease the incentives of domestic institutions to engage in reform if and when investment disputes are taken away from domestic courts. More generally, rule of law rhetoric is easy, although far-reaching institutional reform is hard and slow and requires not only financial but plenty of human and political capital. The last two arguments for the investment treaty regime are intertwined and focus on the economic impact of investment treaties. The broad contention here is that investment treaties increase investment flows, which in turn contributes to economic growth and development. As to the first element, the evidence provides some support to the argument that investment treaties *may* increase investment flows between certain country pairs, but it also shows that other FDI determinants - market size, labor costs and tax breaks - play a more central role in investment decisions. The alleged correlation between FDI and economic development, in turn, is a gross simplification, with the central conclusion being that the impact of FDI depends entirely on country- and investment-specific conditions.

One conclusion that comes from Chapters 6 and 7 is that both sides rely on anecdotal evidence to substantiate their arguments. Another conclusion is that the opposing sides endorse completely different views on the appropriate model of state-market relations. The proponents see that further investment and trade liberalization is not only unavoidable but normatively desirable because of the benefits it brings, with investment treaties ensuring that governments refrain from protectionist and arbitrary regulation. The critics see that investment treaties threaten domestic regulatory autonomy and the protection of public goods. Their proposal is that states should exit the investment treaty regime so as to loosen the stranglehold that transnational economic actors have over the domestic political

process. I suggest that instead of hanging on to their pet arguments, the opposing sides should acknowledge and defend the different political visions they put forward with more analytic rigor, as they will otherwise continue to talk past each other. Chapter 8 provides a short discussion of these competing political visions and draws some general conclusions on the basis of the previous chapters. I discuss what implications my understanding of the critical debate should have for the future of the EU's investment policy, including member state BITs. A useful reference point is provided by the previous debates concerning the legitimacy of the WTO. The essence of the critique of the investment treaty regime is remarkably similar to the critique of the WTO, and the political agenda of the investment treaty critics is strikingly similar to the agenda of the global justice movement that made headlines from the 1999 Seattle protests onward. Relying on Andrew Lang's book, *World Trade Law after Neoliberalism*, I give a short summary of the debates concerning the world trade system around the turn of the millennium and attempt to show how the reactions to the critique of investment arbitration follow a similar type of pattern as the reactions to the critique of the WTO. In both cases, the critique led (or is about to lead) to technical and procedural reforms, which hides from sight the competing political visions that the critics were and are trying to articulate, which in turn obscures the attendant political stakes.

1.3. The Argument and Some Words on Methodology

In light of the above, the argument that this thesis strives to put forward is relatively easy to articulate. My general objective is to combine the doctrinal debate on treaty conflicts with the critical debate on the purposes and implications of the investment treaty regime. The doctrinal analysis finds that member state BITs are problematic from the perspectives of non-discrimination and the autonomy of the EU legal order, although the Court's previous case law does not provide entirely conclusive answers. The analysis of the critical debate shows that taking sides in the debate necessarily requires endorsing a particular (albeit abstract) vision of how state-market relations should be arranged in the global economy. In this light, whichever way the ECJ goes in its assessment of member state BITs, it will necessarily send a political signal to various stakeholders involved in the investment law debates. At the end of the thesis, I also provide some comments on the Commission's proposal for an investment court system, which is understood as safeguarding the right to regulate and as addressing the other procedural and substantive

concerns raised in the critical debate. While the investment court system no doubt remedies some of the structural flaws of old-fashioned BITs, the argumentation of the Commission is highly technocratic as it defends the reform proposals through rhetorical one-liners that find no support in existing evidence. This suggests that the idea that the Commission's proposal comes more than halfway to meet the critics' concerns is misplaced, because it assumes that investment protection - as part of the broader investment and trade liberalization agenda - is in the interest of all EU citizens. The inability of the Commission to articulate and defend the investment court system against the backcloth of a political vision based on a notion of collective purpose may signal a broader gap between the mindset of the EU institutions and segments of the European body politic. I will refrain myself from making practical proposals on how the Commission should defend or modify its approach, but hopefully the analysis in the following chapters demonstrates why many critics will fail to understand the wisdom of the proposed investment court system, and why the relevant debates should become much more political and much less legal. That said, it is useful to provide some comments on the nature of the analysis and discussion carried out in the following chapters.

My 'method' - if you can label it as such - reflects the less than novel idea that legal scholars should not isolate their research from the broader political and economic phenomena to which their research relates, but, rather, embrace and accommodate the 'living political matrix'³⁰ so as to increase understanding of the role that law plays in politics and economic governance. The discussion in Chapters 6 and 7 in particular embraces the living political matrix of international investment law by foregrounding the material and normative outcomes that investment treaties and arbitration are understood as producing on a global scale. While the following chapters refer to a number of economic studies and political science literature, this thesis is by no means an interdisciplinary study. I only focus on some of the conclusions of economic literature when they pertain directly to the general arguments on the pros and cons of investment treaties and arbitration, and the political science works I use seek to explain some of the reasons that drove states to conclude investment treaties in the first place. In this, my 'method' reflects the commonsense idea that academic lawyers will benefit from having a basic understanding

³⁰ This phrase is from Joseph Weiler, 'The Transformation of Europe', 100 *Yale Law Journal* (1991), pp. 2403-2483, at 2409.

of neighbouring disciplines, or, more generally, from being 'broad-minded' as Klabbers put it.³¹

The discussion in the following chapters also relate to the debate on the fragmentation of international law, at the center of which is the description and analysis of specialized normative 'regimes', such as the 'trade law regime' and the 'human rights regime'. Regimes promote different type of interests and values, and when two or more regimes come into contact and claim jurisdiction and authority over the same subject-matter, the question is which regime should prevail and on what grounds. In other words, how should such 'regime collisions' be dealt with.³² Given that there is no established hierarchy of norms under international law, no regime can 'normatively trump the other', which may 'lead to irreconcilably different outcomes in judicial or arbitral procedures',³³ as each regime is bound to apply its own rules and principles to an issue over which other regimes have a direct interest as well.³⁴ Some of the arguments discussed below suggest that EU law and the investment treaty regime are on a collision course. For example, the Commission's arguments on intra-EU BITs seek to exclude the investment treaty regime from having jurisdiction over a range of disputes that also fall under the jurisdiction of member state courts and the two EU courts, whereas the arguments for investment treaties claim that the two regimes have distinct spheres of application and can continue to co-exist as before.

³¹ Jan Klabbers, 'The Relative Autonomy of International Law or the Forgotten Politics of Interdisciplinarity', 1 *Journal of International Law and International Relations* (2004-2005), pp. 35-48, at 35.

³² The pioneering work in this regard is Andreas Fischer-Lescano and Gunther Teubner, 'Regime-Collisions: The Vain Search for Legal Unity in the Fragmentation of Global Law', 25 *Michigan Journal of International Law* (2004), pp. 999-1046, which was expanded to monograph length two years later. See Andreas Fischer-Lescano and Gunther Teubner, *Regime-Kollisionen: Zur Fragmentierung des Globalen Rechts* (Suhrkamp, 2006).

³³ Kerstin Blome et al., 'Contested Collisions. An Introduction', in Kerstin Blome et al. (eds.), *Contested Regime Collisions. Norm Fragmentation in World Society* (Cambridge University Press, 2016), pp. 1-17, at 3.

³⁴ Initially, the proliferation of specialized normative regimes gave rise to formal concerns about the unity and coherence of the international legal order, particularly among practitioners and scholars with an interest in the traditional institutions of general international law, namely, the International Court of Justice and the 'diplomatic law' that governs the activities of the United Nations and its specialized agencies. Their fear was not only that specialized courts and tribunals provide inconsistent interpretations of general international law, but that fragmentation undermines the (presumed) authority of the institutions they represent and hold dear. See Martti Koskenniemi and Päivi Leino, 'Fragmentation of International Law? Postmodern Anxieties', 15 *Leiden Journal of International Law* (2002), pp. 553-579. This formal concern had little chance of containing fragmentation, and as many commentators have noted, it is much more important to understand and highlight the 'conflicting societal goals and interest[s]' that undergird regime collisions, rather than to propose formal solutions to them. This last quote is from Blome et al., 'Contested Collisions', supra note 34, at 3-4. For an extensive proposal on how to approach fragmentation as a formal legal problem, see International Law Commission, *Fragmentation of International Law: Difficulties Arising from the Diversification and Expansion of International Law*, Report of the Study Group of the International Law Commission (finalized by Martti Koskenniemi), UN Doc. A/CN.4/L.682, 13 April 2006 (hereinafter 'Fragmentation report').

These arguments also reflect idea that regimes have an *Eigenrationalität* which they seek to universalize at the expense of other regimes.³⁵ Distinguishing between regime rationalities is relatively easy if the underlying goals of two regimes are clearly opposite, but identifying the 'rationality' of EU law or the investment treaty regime is much more difficult for a number of reasons. Both regimes relate to broader economic, legal and political arrangements that shape the general orientation of normative and distributive outcomes in the global economy. It seems commonsensical that both EU law and investment treaties promote, for example, welfare in the sense that they relate to broader economic governance structures that produce stability, resources and prosperity to (segments of) *certain* populations. At the same time, however, being part of such structures automatically implicates both in the social and economic inequality that prevails in large swaths of the planet. Put differently, and in more abstract and critical terms, the functional orientation of regimes toward a specific objective 'does not at all signify that they would work in view of a globally defined common good'. Rather, such functional labels may only refer 'to their quality as mechanized producers of outcomes that are internally validated by their embedded hierarchies of preference - their structural biases'.³⁶ In yet other words, regimes are 'functional for themselves',³⁷ rather than for the normative goals they profess to. However, this is not to say that regimes would not promote and protect certain values, but that it is important to understand that regime labels are no substitute for critical analysis.

To return to the question of method, the following chapters do not rely on a specific theoretical approach, apart from endorsing the 'living political matrix' of the investment treaty regime. On the one hand, the analysis of the conflict arguments in Chapters 3 and 4 is largely doctrinal or dogmatic as the chapters examine formal legal arguments presented before arbitral tribunals and the ECJ, and their attendant reasoning, as well as the legal texts from which the arguments stem. However, I do not aim to systematize the materials or propose doctrinal solutions to specific interpretive questions beyond the context of member state BITs, although some such proposals may emerge as a byproduct of the discussion. The main purpose is to explain and understand the background of the conflict arguments as well as the reasoning of arbitral tribunals and the ECJ to the extent they

³⁵ Blome et al., 'Contested Collisions', supra note 33, p. 3.

³⁶ Martti Koskeniemi, 'Hegemonic Regimes', in Margaret Young, *Regime Interaction in International Law* (Cambridge University Press, 2012), pp. 305-324, at 317.

³⁷ *Idem*.

pertain to the relationship of EU law and member state BITs. On the other hand, parts of the discussion in Chapters 3 to 5, and in particular the discussion in Chapters 6 and 7 is clearly 'non-dogmatic', as the analyses go beyond the relevant legal materials and strive to understand the type of value claims that undergird not only those materials but the arguments for and against the investment treaty regime. For example, the proponents argue that investment treaties and arbitration stabilize domestic institutional conditions by protecting cross-border economic activity from arbitrary exercises of public power. Social constructivists would say that this argument is based on a subjective construction of social reality, as the human and institutional activities to which it refers have no objective and identifiable essence. Rather, the 'nature' of those activities depends on the subjective meanings we assign to them.³⁸ While in some respect I agree with this basic idea, I resist its categorical tone. Clearly, the purposes and implications of the investment treaty regime are socially construed through the medium of language, but it is still possible to identify, describe and analyze the regime's imprint on the real world in a way that captures at least some aspects of its 'essence' (or 'essences' to be more precise). In this, I strive to employ the method of what the classical scholar Richard Bentley called *ratio et res ipsa* - reason confronting the thing itself.

In the previous section I noted that in my view the critique of the investment treaty regime is essentially political, and that the reform proposals of the Commission are bound to leave many unimpressed. This view requires some explanation. In an article where they claim to tell the 'truth' about investment arbitration, two proponents of the investment treaty regime argue that the 'current discourse on international investment law is replete with inaccuracies and hypothetical fears'.³⁹ The argument that the critics do not really understand what they are talking about is a familiar one, and I will address the proponents' more detailed arguments in the following chapters, but what I again suggest is that the proponents and the critics are talking past (or misunderstanding) each other precisely because they fail to foreground the political nature of their disagreement. The proponents look at the world and point to the benefits of investment and trade liberalization, with investment treaties and arbitration guaranteeing a stable regulatory framework for transnational economic activity, which continues to produce positive spillover effects on a

³⁸ See e.g. Peter L. Berger and Thomas Luckmann, *The Social Construction of Reality: a Treatise in the Sociology of Knowledge* (Penguin, 1971).

³⁹ Brower and Blanchard, 'The Truth about Investor-State Arbitration', *supra* note 19, at 689.

global scale - a rising tide lifting all boats. The critics, in turn, look at the world and see an unsustainable global economy that promotes inequality, environmental degradation, and narrow corporate interests at the expense of the global commons and other public values. Both sides make sweeping associations between individual investment disputes and the investment treaty regime as a whole, and between the regime and the costs and benefits of economic globalization. Both also endorse a particular (though highly general) model of state-market relations, with the critics aiming to rein in transnational economic forces by removing investment treaties and arbitration from the domestic policy equation. The proponents, in turn, preach the gospel of economic liberalism, with the investment treaty regime ensuring that protectionist and arbitrary exercises of public power are kept in check.

Between the somewhat schematic groups of 'critics' and 'proponents' stand a large, dispassionate majority, which holds more moderate views on the pros and cons of the regime. The majority of academic lawyers interested in the critique, for example, would probably acknowledge that the regime needs some type of reform, and most would acknowledge that the broader political concerns that animate the critique are urgent and important and require immediate attention domestically and internationally. At the same time, however, they understand that addressing these concerns falls outside their job description, as their resolution is understood to depend on and as requiring the input of openly political actors and other legal regimes and institutions - including economists, human rights lawyers and domestic political parties. To give an example of this logic, reforming the investment treaty regime may be perceived as broadening the regulatory autonomy of host states, but whether or not the reforms actually promote the normative goals of the critics (such as sustainable and more inclusive development and protection of the environment) is not the concern of academic lawyers who focus on debating the 'merits' of the critique and proposing treaty reforms. The complexity of the broader political concerns that fuels the critique is of course evident - how does one promote sustainable development, for example - and the role of investment law scholarship may seem entirely marginal in the bigger scheme of things. I suggest that this helps explain, at least partly, why legal scholarship tends to focus on doctrinal work even when the relevant doctrines pertain to a hotly politicized topic such as international investment law. Studying the content of legal rules and principles, and placing those rules and principles in a systematic order, is usually the only conceptual universe that academic lawyers are familiar with.

Going outside this 'comfort zone 'will create feelings of ambiguity and incompetence, as the broader political and economic questions that, for example, the critics of investment treaties invoke are not amenable to doctrinal analysis.

There is also sense that it is naïve (or overly ambitious) to think that the global problems that animate the critique are amenable to political resolution in the first place. If one wishes to do something about, say, environmental degradation, it is much wiser to exit academia or to donate money or to change one's diet to a more carbon-neutral direction, rather than to focus on the more systemic concerns that, say, NGOs raise when criticizing investment treaties and arbitration. However, the purpose of the discussion in Chapters 6 and 7 is not to propose solutions to the broader political concerns of the critics, nor to lay a guilt trip on academic investment lawyers who focus on case law analysis and doctrinal evolution. Rather, the purpose is to understand better the assumptions of both the critics and the proponents, and to assess whether those assumptions hold water. Another purpose is to foreground the broad political visions of the opposing sides, and to demonstrate that taking sides in the debate will necessarily entail a choice between the two competing visions, even if those visions are expressed in very abstract terms. These questions are driven by my own interest in understanding better the critical debate and the underlying political stakes, rather than by an ambition to change the world. I am not naïve about the motives of the opposing sides in the sense that the critics do not necessarily represent progressive forces, and the proponents are not just privileged and reactionary conservatives seeking to entrench the unjust status quo. I share the broad political concerns of the critics, but I simultaneously recognize that those concerns escape my conceptual capabilities, and as Chapters 6 and 7 have been written in a 'research chamber', armchair scholarship is perhaps the term that best describes the discussion therein; the point being that although I am fully aware that the worlds of politics and business have their share of bad faith actors who utilize and promote investment treaties for personal gain, I cannot base my analysis on what I do not know.

As a final matter, it is useful to say a few words on the basic approach I take with respect to EU law. There is an ongoing debate on the relationship of EU law and international law. One central question in this debate is whether EU law is part of international law or

whether it has a 'non-international legal nature',⁴⁰ given that the founding treaties and the jurisprudence of the ECJ have created a 'specified interstate governmental structure defined by a constitutional charter and constitutional principles'.⁴¹ Whether the EU is a constitutional order or not and what its relationship to international law is are interesting questions, but they will appear only incidentally in the following chapters. For example, the relationship of EU law and international law is discussed in the context of EU law rules which relate to treaties that member states have concluded between themselves and with third states. As to the constitutional idea, Weiler has noted that 'in critical aspects the Community has evolved and behaves as if its founding instrument were not a treaty governed by international law but, to use the language of the European Court, a constitutional charter governed by a form of constitutional law'.⁴² Again, I am not interested in pondering whether the EU is a constitutional order, but in understanding what type of interests and values its rules and principles, and the actions of its institutions, are argued as promoting in the present context. The discussion will touch on some aspects of the constitutionalism debate, but I will not foreground it at any point. I also have to confess that my knowledge of EU law is very limited. While the analysis of EU law rules and principles that are directly relevant aims to be rigorous, I have very little knowledge about the scope and content of secondary law in most policy areas, as I do about the precise division of competences between the EU and its member states. The central purpose is to understand how the relationship of EU law and member state BITs should be resolved in light of the case law of the ECJ on the one hand, and in light of the critical debate on the other.

⁴⁰ Bruno de Witte, 'European Union Law: How Autonomous is its Legal Order?', 65 *Zeitschrift für öffentliches Recht* (2010), pp. 141-155, at 147.

⁴¹ Weiler, 'The Transformation of Europe', supra note 30, p. 2407.

⁴² Joseph Weiler, 'The Reformation of European Constitutionalism', 35 *Journal of Common Market Studies* (1997), pp. 97-131, at 97.

2. Treaty Conflicts, Intra-EU and Extra-EU BITs, and the Limits of Formal Dispute Settlement

2.1. Introduction

An 'extremely difficult problem'⁴³, these words of an eminent international lawyer, expressed during the final stages of the drafting process of the VCLT, reflect the complexity of the topic of treaty conflict. Reading the reports of the Special Rapporteurs and the transcripts of the ILC meetings, or later academic contributions, testify that entire careers could be spent analyzing treaty conflicts in their varied dimensions. The ILC, faced with the Herculean task of drafting a general convention on the law of treaties, struggled to establish some basic rules in respect of treaty conflicts between identical (AB:AB) and non-identical parties (AB:AC).⁴⁴ The more difficult issues, such as providing a typology of treaty conflicts and taking account of the variables that undergird different scenarios, never entered the analytical process. For present purposes, it is necessary to address those aspects of this 'extremely difficult problem' which pertain to the conflict scenarios under discussion. Section 2.2. provides a 'technical' account of treaty conflicts by discussing how doctrine has defined treaty conflicts as well as the relevance that these definitions have to the conflict arguments discussed in Chapters 3 and 4. Section 2.3. focuses on the distinction between extra-EU and intra-EU BITs and on the basic rules and principles that govern treaty conflicts under EU law and international law. The discussion highlights how, on the one hand, EU law requires member states to eliminate conflicting treaty obligations, and the many obstacles that the application of this 'requirement' faces in an international law context. Section 2.4. focuses on a number of issues. First, I provide some observations on the role that courts and tribunals can have in the resolution of treaty conflicts. Treaties are created by states and, as many commentators have noted, courts and tribunals are reluctant to become treaty 'destroyers' when conflict arguments are raised before them. I discuss the general reasons that lead courts and tribunals either to circumvent or reject conflict arguments, and one of these reasons is related to the values and interests that typically undergird treaty conflict arguments. After this, I focus on party intent, which is a

⁴³ Statement by Paul Reuter, representative of France, at the 857th meeting. See *Yearbook of the International Law Commission* (1966/Vol. I, part 2), p. 97 (para. 28).

⁴⁴ AB:AB conflicts refers to a situation where states A and B conclude two successive treaties containing incompatible provisions, whereas AB:AC conflicts refers to situations where one of the parties to the earlier treaty (A) concludes a later conflicting treaty with state C (and possibly with states D, E and F as well).

central element of treaty interpretation, but its actual role in the resolution of treaty conflicts remains in part a mystery. I will also sketch some preliminary remarks on the role of party intent in the application of specific conflict rules. As a final matter, I provide an introductory comment on the issue of competence and how it affects the dynamics of treaty conflict in the EU context. With the entry into force of the Lisbon Treaty, the EU now has exclusive competence over foreign direct investment. The question is at what point in time did member state BITs, extra-EU BITs in particular, come within the scope of EU law and what implications this should have had on the member states' ability to maintain the treaties in force. While this may seem a moot point in light of the transitional regime established for extra-EU BITs, it nonetheless highlights how EU law limits member states' general treaty-making capabilities even in areas where the EU has no (exclusive) competences. Such general 'pre-emption' reduces the likelihood of treaty conflict, but simultaneously creates uncertainty for third states which have concluded treaties with member states.

Generally speaking, the following discussion shows that conflict rules are empty vessels in terms of values and interests, although their application in individual cases can signal an implicit preference for one value or interest over another. The primacy of EU law, for example, means that EU law trumps, without exception, conflicting national laws and treaty obligations in intra-EU relations. In this sense, primacy of EU law applies 'automatically' and prevents a contextual analysis of the prudence of its application. As a related matter, and as noted, I discuss why international courts and tribunals are not necessarily receptive of the primacy of EU law or of the obligation of member states to eliminate conflicting treaty obligations under the principle of sincere cooperation and Article 351 TFEU.⁴⁵ This discussion acts as a lead-in to the more general analysis of the cases where the arbitral tribunals rejected a number of conflict arguments raised by the respondent member states and the EU Commission (which is carried out in Chapter 3).

⁴⁵ The principle of sincere cooperation is found in Article 4(3) TEU, which reads as follows: 'Pursuant to the principle of sincere cooperation, the Union and the Member States shall, in full mutual respect, assist each other in carrying out tasks which flow from the Treaties. The Member States shall take any appropriate measure, general or particular, to ensure fulfilment of the obligations arising out of the Treaties or resulting from the acts of the institutions of the Union. The Member States shall facilitate the achievement of the Union's tasks and refrain from any measure which could jeopardise the attainment of the Union's objectives.' As Advocate General Maduro put it, Article 351 TFEU, to which I referred already, is a specific expression of the principle of sincere cooperation. See Case C-05/06, *Commission v Austria*, Opinion of Advocate General Maduro, ECLI:EU:C:2008:391, para. 33.

2.2. Defining Treaty Conflicts

To schematize matters, treaty conflicts are defined in two basic ways in scholarship. Jenks speaks of conflicts arising 'only where a party to the two treaties cannot simultaneously comply with its obligations under both treaties', which he calls a conflict 'in the strict sense of direct incompatibility'.⁴⁶ A number of later writers have endorsed this approach, for example, Karl noted that in technical terms 'there is a conflict between treaties when two (or more) treaty instruments contain obligations which cannot be complied with simultaneously'.⁴⁷ The second group of definitions are much broader and their length can range from single sentences to highly analytical expositions. For example, Metz provides an elaborate classification where conflicts are arranged by gradation and she speaks of (e.g.) 'Pflichtenkollisionen', 'Zielkollisionen' and 'politische Konflikte',⁴⁸ whereas Aufrecht is content with noting that conflict arises between successive treaties when 'both deal with the same subject matter in a different manner'.⁴⁹ A sub-group within this second group focuses more on the undergirding purposes of treaties and less on the content of individual treaty provisions. For example, the 2006 report of the Study Group on the Fragmentation of International Law (the ILC Report) argues that a 'treaty may sometimes frustrate the goals of another treaty without there being any strict incompatibility between their provisions', and this is referred to as a 'looser' understanding of treaty conflict.⁵⁰ In a similar vein, Borgen argues that conflict can arise 'when one treaty... frustrate[s] the purpose of another treaty',⁵¹ whereas Ranganathan asks whether a state's conduct that breaches the object and purpose of a treaty may breach 'a more general obligation of good faith', as 'spelt out in VCLT Articles 18, 26 and 31'?⁵²

⁴⁶ Wilfred Jenks, 'Conflict of Law-Making Treaties', 30 *British Yearbook of International Law* (1953), pp. 401-453, at 426.

⁴⁷ Wolfram Karl, 'Conflicts Between Treaties', in Rudolf Bernhardt (ed.), *Encyclopedia of Public International Law. Volume 7* (North-Holland, 1984), pp. 467-472, at 468. For additional references, see Joost Pauwelyn, *Conflict of Norms in Public International Law. How WTO Law Relates to Other Rules of International Law* (Cambridge University Press, 2003), p. 167

⁴⁸ Nele Matz, *Wege zur Koordinierung völkerrechtlicher Verträge. Völkervertragsrechtliche und institutionelle Ansätze* (Berlin: Springer, 2005) pp. 8-18.

⁴⁹ Hans Aufrecht, 'Supersession of Treaties in International Law', 37 *Cornell Law Quarterly* (1952), pp. 655-700, at 655-656. For additional references, see Pauwelyn, *Conflict of Norms*, supra note 47, pp. 167-169.

⁵⁰ See 'Fragmentation report, supra note 34, para. 24.

⁵¹ For similar descriptions see e.g. Christopher J. Borgen, 'Treaty Conflicts and Normative Fragmentation', in Duncan B. Hollis (ed.), *The Oxford Guide to Treaties* (Oxford University Press, 2012), pp. 448-471, at 455-456. See also Surabhi Ranganathan, *Strategically Created Treaty Conflicts and the Politics of International Law* (Cambridge University Press, 2014), p. 53 (pondering the question whether Article 30 of the Vienna Convention on the Law of Treaties, which contains the lex posterior conflict rule, covers situations 'where one treaty impairs the object and purpose of another without breaching any specific obligation').

⁵² Ranganathan, *Strategically Created Treaty Conflicts*, supra note 51, p. 54.

Generally speaking, the following discussion will relate to and contain elements from both types of definitions. For example, the argument that BIT arbitration clauses breach the autonomy of the EU legal order is premised on a direct incompatibility between the clauses and Article 344 TFEU (discussed below), but the principle of autonomy is also built on the back of a number of other primary law provisions and their underlying purposes, and the CJEU's relevant dicta strive to safeguard its exclusive jurisdiction and guarantee the uniform interpretation of EU law. Such objectives have a connection to specific primary law provisions, but they also stem from the Court's own perception of the EU legal order and of its role within that order. In this way, an alleged conflict between BIT arbitration clauses and the autonomy of the EU legal order stems in part from the purposes of the EU founding treaties, as interpreted by the ECJ, and not only from a direct conflict with specific primary law provisions. Regulatory conflicts, in turn, are 'simpler' in this respect as they stem from alleged conflicts between one or more BIT protection standards (such as fair and equitable treatment) and particular acts of the EU institutions, which member states then implement, and in this way they are conflicts in the 'strict sense of direct incompatibility', as Jenks put it. In other words, in regulatory conflict scenarios a member state has an obligation to implement or comply with an EU act (regulation, directive, decision), which allegedly breaches its obligation to provide certain kind of treatment under a BIT.

The relevant case law of arbitral tribunals and the ECJ contain only a few general remarks on the nature of the alleged treaty conflicts, which suggests that the matter was considered as requiring no elaboration or as being clear on the basis of the parties' arguments. But the above remarks leave many questions open about the nature of primary and regulatory conflicts. For example, are primary conflict arguments based, similarly to regulatory conflicts, on 'mutually exclusive obligations'?⁵³ Assuming that BIT arbitration clauses breach the autonomy of the EU legal order or the principle of non-discrimination, to whom are the obligations to safeguard the autonomy of EU law and to provide equal treatment owed? It seems plausible to argue that such obligations could be owed to any of the following three candidates: other member states, nationals of other member states, or even the EU, given its much-emphasized *sui generis* nature. And, related, what is the nature of

⁵³ The quote is from Pauwelyn, *Conflict of Norms*, supra note 47, p. 167.

the rights that BITs create and who are the bearers of those rights? That is to say, are investors enforcing their own rights or the rights of their home state (as party to the BIT) when raising a claim under a BIT? If investors are viewed as direct bearers of BIT rights, this can strengthen the perception that investment treaties are akin to human rights treaties, which in turn can affect the way in which conflict arguments are perceived, as will be discussed below. In other words, if investment treaties are not merely inter-state exchanges of mutual rights and obligations, but endow individuals with rights, then clearly any argument that seeks to invalidate such rights must be critically analyzed. As noted in the introduction, however, the alleged conflicts between EU law and BITs are not necessarily based on opposing values per se, but on different levels of protection that the two regimes provide to investors.

Once a treaty conflict is established, the next logical question is which conflict rule should apply. General international law includes a number of conflict rules - including *lex priori*, *lex specialis* and *lex superior* - and the VCLT gives much authority to the *lex posterior* rule, which is the only conflict rule included in its provisions. Primary EU law, on the other hand, has a single provision dealing with the status of member states' treaties, but the relevance of Article 351 TFEU is limited. It only covers treaties concluded between member states and *third* states *before* the former acceded to the EU. Hence, Article 351 TFEU is irrelevant in respect of treaties concluded after EU accession, as it is with respect to treaties concluded between two or more member states. As to the contents of Article 351 TFEU, it allows member states to honor their pre-accession treaty obligations owed to third states, but simultaneously requires that they take 'appropriate steps' to eliminate incompatibilities from such treaties so as to ensure compliance with EU law.⁵⁴ When it comes to member state treaties that fall outside the scope of Article 351 TFEU, the case law of the ECJ sends a similar and clear enough message: here too member states are to ensure that EU law ultimately prevails over conflicting treaty obligations, regardless of the time of the conclusion of the conflicting treaty and regardless of whether the relevant

⁵⁴ As the Commission once put it, 'Article 234 of the Treaty [i.e. Article 351 TFEU] does not establish that public international law obligations prevail over Community law, but rather the reverse. It points out that the second paragraph of that article provides that the Member States concerned are to take all appropriate steps to eliminate the incompatibilities established, which may include repudiating the public international law obligation at issue.' See Case T-3/99, *Banatrading*, ECLI:EU:T:2001:187, para. 63.

obligation is owed to another member state or a third state.⁵⁵ The following sections will put more flesh on the bones of these basic principles.

2.3. The Distinction between Intra-EU and Extra-EU BITs

2.3.1. Extra-EU BITs

This brings us to the distinction between intra-EU and extra-EU BITs. The latter are concluded between a member state and a third state. The basic rule here is that conflicts between EU law and extra-EU BITs have no impact on the legal status of the latter as a matter of international law. Under international law, two basic principles govern the position of third states in situations where a treaty party has or assumes conflicting obligations under another treaty to which the former is not party: the *res inter alios acta* principle provides that treaties only bind their parties and remain valid as between them, and the *pacta tertiis nec nocent nec prosunt* principle provides that 'no treaty may create obligations' for a third state 'without its consent'.⁵⁶ As will be shown, and schematically speaking, EU law recognizes these principles, in particular in the form of Article 351 TFEU, but simultaneously requires that member states take action so as to eliminate their conflicting treaty obligations. Put differently, if a conflict exists between EU law and an extra-EU BIT, member states are obligated to eliminate the conflict in favor of EU law, but only as a matter of EU law, as the *res inter alios acta* maxim applies fully under international law.⁵⁷ In yet other words, if an extra-EU BIT is in conflict with EU law, the third state (and its investors) can continue to demand that the member state party complies with its obligations under the BIT.

However, the EU's newly acquired competences over FDI have also affected the EU law status of extra-EU BITs. The so called Grandfathering regulation⁵⁸ has created a

⁵⁵ The best discussion on this admittedly large and complex issue (and on the relevant case law of the ECJ) is in Klabbers, *Treaty Conflict and the European Union*, supra note 22 (chapters 6, 8 and 9).

⁵⁶ The quote is from Ranganathan, *Strategically Created Treaty Conflicts*, supra note 51, p. 56.

⁵⁷ This maxim is also found in Article 30(4) of the Vienna Convention on the Law of Treaties (VCLT), and its application is without prejudice to the responsibility of the state that concludes conflicting treaties with non-identical parties. This is recognized in Article 30(5) VCLT, which provides that Article 30(4) is without prejudice 'to any question of responsibility which may arise for a State from the conclusion or application of a treaty the provisions of which are incompatible with its obligations towards another State under another treaty.' See Vienna Convention on the Law of Treaties, 1155 UNTS 331.

⁵⁸ Regulation (EU) No 1219/2012 of the European Parliament and of the Council of 12 December 2012 establishing transitional arrangements for bilateral investment agreements between Member States and Third Countries (hereinafter Grandfathering Regulation), OJ L 351, 20.12.2012, pp. 40-46.

transitional regime for extra-EU BITs, which allows their continued existence on a number of conditions until the EU has concluded equivalent investment protection treaties with the respective third states.⁵⁹ The regulation expressly states that extra-EU BITs 'remain binding on the Member States under public international law',⁶⁰ but simultaneously requires that member states 'take the necessary measures to eliminate incompatibilities, where they exist, with Union law, contained in bilateral investment agreements concluded between them and third countries'.⁶¹ Member states have to notify the extra-EU BITs they wish to maintain in force and the Commission is to screen the notified treaties for their compatibility with EU law.⁶² Technically speaking, a regulation cannot trump primary law provisions, which implies that if extra-EU BITs breach the principle of non-discrimination, for example, member states are under an obligation to eliminate that incompatibility, and this is of course what the regulation requires as well. Generally speaking, the discrimination and autonomy concerns are equally relevant in respect of extra-EU and intra-EU BITs, but it seems unlikely that the Commission will raise the matter through infringement proceedings or before arbitral tribunals established under extra-EU BITs for a number of reasons.

A 2014 study found that 1160 extra-EU BITs were in force⁶³ and the capital-exporting member states continue to place a high premium on the treaties. Not only are the treaties perceived as important for generating (and protecting) inward and outward investment flows, but a number of governments actively sought to retain their capacity to conclude new BITs pending the conclusion of investment treaties by the Union, which capacity is now explicitly recognized in the Grandfathering regulation (under certain conditions).⁶⁴ It is noteworthy that the Grandfathering regulation sets a deadline for the Commission to report on its application by January 10th 2020,⁶⁵ which reflects the complexity and time-consuming nature of the assessment process, and the high number of extra-EU BITs suggests that many of them will continue to remain in force even after 2020. What is more,

⁵⁹ Already in 1976, the ECJ had held that even in areas of exclusive competence member states can be authorized to maintain in force their existing treaties until they are replaced by EU-level treaties. See Case 41/76, *Suzanne Criel v Procureur de la République*, ECLI:EU:C:1976:182, para. 32.

⁶⁰ Grandfathering Regulation, supra note 58, recital, para. 5.

⁶¹ Ibid., recital, para. 11.

⁶² The applicable 'screening' rules vary in accordance with the time of conclusion of the notified extra-EU BITs. See *ibid.*, Articles 2 to 9.

⁶³ UNCTAD, 'Investor-State Dispute Settlement: An Information Note on the United States and the European Union', *IIA Issues Note*, 2/2014, p. 3.

⁶⁴ Grandfathering Regulation, supra note 58, Articles 7 to 11.

⁶⁵ Ibid., Article 15(1).

in May 2017, the ECJ published Opinion 2/15 where it held that matters related to FDI fall within the exclusive competence of the EU, apart from investment protection (to the extent it relates to non-direct investments) and investment arbitration, which fall within a competence shared between the EU and the member states.⁶⁶ This effectively gives a veto right to member state parliaments over any EU trade agreement containing an investment protection chapter, which creates uncertainty over the EU's investment protection policy as well as over the future of extra-EU BITs. In September 2017, the Belgian federal government submitted a request for an opinion from the ECJ on the compatibility of the Investment Court System (ICS) established in Chapter Eight of CETA with the founding treaties. The Court's opinion will not only determine the future of the ICS but also have an impact on the future of extra-EU BITs. In sum, while much of the discussion in Chapters 3 to 5 will focus on intra-EU BITs, I will provide some remarks on extra-EU BITs as well.

2.3.2. Intra-EU BITs and the 'Limits' of Primacy of EU Law

Intra-EU BITs are concluded between two EU member states and, as noted, the ECJ has held that EU law prevails over member states' mutual treaty obligations in case of conflict,⁶⁷ but the application of primacy of EU law outside the EU legal order is not evident. International courts and tribunals may, for a number of reasons, either apply a different conflict rule or conclude that the other treaty and EU law are fully compatible, whatever the EU institutions think of the matter.⁶⁸ This is particularly the case if the ECJ has not ruled on the relationship of EU law and a given intra-EU treaty. More generally, the blindness with which primacy applies as a matter of EU law does not fit well to an international law context. As a first matter, primacy of EU law provides a technical, value-neutral solution to treaty conflicts, and its mechanical application overlooks the interests and values that the conflicting (non-EU) treaty promotes. In other words, primacy is blind to the context. Second, and from the opposite perspective, there are many practical reasons

⁶⁶ There were some additional FDI issues that remain an area of shared competence, but it is not necessary to discuss these in the present context. See *Opinion 2/15*, ECLI:EU:C:2017:376, para. 305.

⁶⁷ See e.g. Case C-3/91, *Exportur*, ECLI:EU:C:1992:420, para. 8 (where the Court held that 'it should be observed that the national court rightly considered that the provisions of a convention concluded after 1 January 1958 by a Member State with another State could not, from the accession of the latter State to the Community, apply in the relations between those States if they were found to be contrary to the rules of the Treaty.').

⁶⁸ Binder makes the point that when the same parties conclude a later treaty, which conflicts with an earlier treaty they have concluded, no treaty conflict can exist because the parties in question have given their 'consent to the termination or modification...of the earlier treaty'. However, in many cases states conclude treaties without any awareness over their potential implications for obligations assumed under earlier treaties, and this holds true in the present context as well. See Guyora Binder, *Treaty Conflict and Political Contradiction. The Dialectic of Duplicity* (Praeger, 1988), pp. 7-8.

that support and justify the application of primacy of EU law. If the member states were free to contract out of their EU law obligations, in however limited fashion, the uniform interpretation of EU law would become impossible to achieve, gradually derailing the entire European project. In this light, primacy of EU law makes much practical sense, as does the more general obligation of member states to eliminate conflicting treaty obligations.

Third, and related, primacy of EU law could also be defended with reference to the foundational values of the EU and the provisions of the Fundamental Rights Charter (Charter).⁶⁹ If EU acts are presumed to reflect values such as the rule of law and respect for human rights, and if they have to comply with the provisions of the Charter, then clearly none of the affected parties need to worry when EU law occupies a given field and requires the member states to eliminate conflicting treaty obligations. However, many investment disputes raised under member state BITs have no connection to EU law as they concern purely domestic measures. While such measures have to comply with the internal market freedoms and the principle of non-discrimination, their contents may constitute a breach of investment protection standards even if they comply with EU law. As will be shown, many of the cases discussed in Chapter 3 related to policy measures that could not be challenged under EU law. As to the fundamental values of the EU, which should guide its actions and shape the imprint it has on the real world, they are a perspectival matter, and the protections of the Charter are modest in comparison to typical investment protection standards. Likewise, what the EU stands for depends also on what exactly is considered to constitute the EU.

Is the EU responsible for the social costs of the austerity measures imposed on Greece, regardless of the Eurozone's more limited membership and the involvement of non-EU financial institutions in the conclusion of the successive austerity packages? As the editors of the *Common Market Law Review* noted, 'there is a widespread resentment against austerity measures forced upon citizens with barely any meaningful consent by their own countries' legislatures'.⁷⁰ Similarly, does the EU bear responsibility for the situation in Western Sahara? The Polisario Front has argued that because the EU-Morocco association

⁶⁹ Charter of Fundamental Rights of the European Union, OJ C 326, 26.10.2012, pp. 391-407.

⁷⁰ Editorial Comments, 'Debt and Democracy: "United States then, Europe now"', 49 *Common Market Law Review* (2012), pp. 1833-1840, at 1833. See also Paul Kirchhof, 'Verfassungsnot!', *Frankfurter Allgemeine Zeitung*, 12 July 2012.

agreement applies in the area of Western Sahara, the EU is actively supporting Morocco's illegal occupation.⁷¹ And is the EU's mandatory policy for the relocation of asylum seekers a breach of the principle of representative democracy, as argued by the Slovak Republic, because that policy was adopted without the input of national parliaments?⁷² Certainly, millions of people across Europe think that the EU is to be blamed for an endless list of 'ills faring their lands',⁷³ although such perceptions may often be based on misguided, disorganized and even delusional assumptions. The point of these disparate examples is that the application of EU law over member states' conflicting treaty obligations is not necessarily a sign of progress in the eyes of those whose treaty rights are affected as a result. Similarly, from the perspective of an international court or tribunal, the primacy of EU law is not necessarily equated with the foundational values of the EU, and the practical reasons supporting the primacy (or general superiority) of EU law remain extraneous to an international law context.

Generally speaking, BIT protections are broader and more effective than remedies available under EU law and national laws of the member states,⁷⁴ although any comparison of the respective remedies will reveal that the comparison is not necessarily a simple task.⁷⁵ One reason that explains the 'generosity' of BIT remedies is that the bulk of member state BITs follow the 'European template'. Although the treaties contain no liberalization commitments, most of them are 'old-fashioned' in that the protection standards are written in vague and highly general language, with no reference made to the contracting states' right to regulate. The treaties allow investors to challenge any domestic regulatory measure adopted by the three branches of government, with liability depending on two factors - attribution and breach of a BIT obligation - whereas under domestic laws and EU law the criteria of liability are stricter (I discuss this issue further in Chapter 4). The Commission

⁷¹ See Case T-512/12, *Front Polisario v Council*, ECLI:EU:T:2015:953 and Case C-104/16 P, *Council v Front Polisario*, ECLI:EU:C:2016:973. The General Court held not only that the Front Polisario had legal standing to bring a claim against the EU Council's decision regarding the conclusion of the trade agreement, but also annulled the decision. The ECJ, in turn, quashed the General Court's decision on the ground that the Front Polisario had no locus standi.

⁷² See Case C-643/15, *Slovak Republic v. Council of the European Union*, Opinion of Advocate General Bot, ECLI:EU:C:2017:618, paras. 49-50.

⁷³ This is taken from Tony Judt, *Ill Fares the Land* (Penguin Books, 2010).

⁷⁴ For a discussion of this issue, see e.g. *Eureka B.V. v. The Slovak Republic*, PCA Case No. 2008-13, Award on Jurisdiction, Arbitrability and Suspension (hereinafter *Eureka* award), 26 October 2010, paras. 250-262; Mavluda Sattorova, 'Investor Rights under EU Law and International Investment Law', 17 *Journal of World Investment & Trade* (2016), pp. 895-918.

⁷⁵ For a useful discussion in this respect, see Martins Paporinskis, 'Investors' Remedies under EU Law and International Investment Law', 17 *Journal of World Investment & Trade* (2016), pp. 919-941.

has also argued that arbitration under intra-EU BITs breaches the principle of mutual trust, because investment arbitration in intra-EU relations signals a mistrust in the ability of member state courts to act in accordance with the foundational values of the EU when they implement EU law.⁷⁶ Again, this argument is based on contested assumptions. While the idea that member state courts and other domestic institutions respect the foundational values of the EU is understandable from the perspective of EU integration, its realization is a different matter. For example, Hungary's recent law, which sanctions mandatory detention of all asylum seekers, breaches the Reception Conditions Directive, and the Dublin Regulation expressly recognizes the possibility that some member states may have 'systemic flaws' in their 'asylum procedure and in the reception conditions' for asylum seekers.⁷⁷ Likewise, the Commission's 2017 reports on the steps that Romania and Bulgaria have taken in the past ten years in the fields of judicial reform and the fight against corruption and organized crime note, inter alia, that the 'overall institutional set-up to fight corruption in Bulgaria remains fragmented and...largely ineffective',⁷⁸ and 'implementation of court decisions by state institutions and public administration' in Romania remain a concern, which the European Court of Human Rights has characterized as a 'structural deficiency'.⁷⁹ Poland's recent legislation on its judiciary has been described as a 'systemic threat to the rule of law', and the EU's subsequent response is based in part on Article 7 TEU, which provides a mechanism to protect the EU's foundational values.⁸⁰

⁷⁶ This argument was raised in a letter to the Swedish government concerning the termination of the Romania-Sweden BIT. See Europeiska Kommissionen, *Formell underrättelse - Överträdelse nummer 2013/2207* (hereinafter Commission letter), C(2015) 4215 final, Brussels, 19.6.2015, p. 14. The letter is not public but I manage to get a copy of it. See also *Opinion 2/13* (Accession of the European Union to the European Convention for the Protection of Human Rights and Fundamental Freedoms), ECLI:EU:C:2014:2454, paras. 168, 191 and 194 (where the Court argued, inter alia, that the EU 'legal structure is based on the fundamental premise that each Member State shares with all the other Member States, and recognizes that they share with it, a set of common values on which the EU is founded, as stated in Article 2 TEU. That premise implies and justifies the existence of mutual trust between the Member States that those values will be recognized and, therefore, that the law of the EU that implements them will be respected', see para. 168).

⁷⁷ See Lizzie Dearden, 'Hungarian parliament approves law allowing all asylum seekers to be detained', *Independent*, 7 March 2017. See also Article 3(2) of Directive 2013/32/EU of the European Parliament and of the Council of 26 June 2013 on common procedures for granting and withdrawing international protection (recast), OJ, 29.6.2013, L180, pp. 60-95; Regulation (EU) No 604/2013 of the European Parliament and of the Council of 26 June 2013 establishing the criteria and mechanisms for determining the Member State responsible for examining an application for international protection lodged in one of the Member States by a third-country national or a stateless person (recast), OJ, 29.6.2013, L180, pp. 31-59.

⁷⁸ Report from the Commission to the European Parliament and the Council, On Progress in Bulgaria under the Cooperation and Verification Mechanism, Brussels, 25 January 2017, COM(2017) 24 final, p. 6.

⁷⁹ Report from the Commission to the European Parliament and the Council, On Progress in Romania under the Cooperation and Verification Mechanism, Brussels, 25 January 2017, COM(2017) 44 final, p. 6.

⁸⁰ See EU Commission, 'European Commission launches infringement against Poland over measures affecting the judiciary', Brussels, 29 July 2017; EU Commission, 'Communication from the Commission to

While these examples do not constitute proof that foreign investments are treated arbitrarily, they fuel perceptions that investment treaties are necessary to protect the fundamental rights of investors in certain member states. As a member of the European Parliament put it when trying to convince her constituency about the virtues of CETA:

'[i]nvestment protection is needed to guarantee the terms of the agreement, especially with countries where the rule of law is not a given. With Canada, that is not the chief concern, although international treaties are not automatically transposed into Canadian law and therefore cannot always be used in a Canadian courtroom. On the other hand, the Canadians are not so much worried about the Netherlands or Germany, *but they are worried about the rule of law and legal systems in some other member states*. That cannot be very surprising, since companies in those member states are often also worried about the legal systems in their country, speed of legal processes and impartiality of judges. In fact, European companies often use investment protection clauses of investment treaties between EU member states, for example in cases of expropriation.'⁸¹

This statement cuts corners in many respects, but the point about the need of investment protection due to 'some other member states' reflects how the EU membership remains at different levels of economic, legal and political development, which then creates more general assumptions about how this should be taken into account in the policy-making of the EU institutions. In this way, the Commission's conflict arguments on intra-EU BITs disregard its own concerns about the quality of domestic governance in certain member states, which provides a basis for the argument that the termination of intra-EU BITs would 'deprive EU citizens of subjective rights...[which] would be an unparalleled occurrence as regards fundamental principles of the European Union'.⁸² Chapter 3 will show arbitral tribunals have used similar type of logic in their reasoning on the relationship of the relevant BITs and EU law, and this logic relies in part on the general perception that intra-EU BITs continue to serve a useful purpose within the internal market. Similarly, and as noted, many of the arbitrations discussed in Chapter 3 were unrelated to EU law as they

the European Parliament and the Council: A New EU Framework to strengthen the Rule of Law', Brussels, 19 March 2014, COM(2014) 158 final/2.

⁸¹ Marietje Schaake, 'Ten questions on CETA', 8 February 2017, available at <https://marietjeschaake.eu/en/ten-questions-on-ceta>.

⁸² Tietje, 'Bilateral Investment Protection Treaties between EU Member States, supra note 17, p. 19.

were based on domestic measures that could not be challenged under EU law. The mutual trust argument, for example, ignores this aspect of intra-EU BITs as it assumes that all intra-EU investment disputes come within the scope of EU law in a broader sense.

In sum, the application of primacy of EU law faces many obstacles outside the EU legal order, and the Commission's approach to intra-EU BITs is problematic in light of the rule of law concerns outlined above. Since many investment disputes are outside the scope of EU law in that the challenged measures raise no concerns as a matter of EU law, the question is why the member states should not be free to provide additional remedies to EU investors. Whether these rule of law concerns are plausible is addressed in Chapter 7, and the question whether intra-EU BITs constitute discrimination and threaten the autonomy of EU law is addressed in Chapters 4 and 5.

2.4. The Roles of Party Intent and of Courts and Tribunals in the Resolution of Treaty Conflicts, and Some Remarks on the Question of Competence

The previous sections have provided an outline of the basic rules and principles that govern conflicts between EU law and member state BITs. One central question is what role party intent should play in their application? Party intent is central to treaty interpretation, but in respect of treaty conflict arguments it cannot be the only interpretive criterion, as the parties typically disagree about the content of their (past and present) intent over the relevant treaties. To elaborate, and schematically speaking, treaty conflict presumes that the parties' present intent points in different directions, and the same is necessarily true with respect to their past intention: if the parties' intentions on the relationship of the relevant treaties converge, no treaty conflict arises. In yet other words, if the relevant treaties contain no conflict clauses (expressing the parties' intention), and if the parties were not aware of potential conflicts upon the conclusion of the second treaty, the question becomes what the treaty texts and other relevant legal and factual materials say about party intent. Relying on party intent alone would mean that a court would have to uphold one party's intention and overrule the other's, and no court will resolve a treaty conflict with such simplistic method, if only because choosing one intent over another will always have to be justified with reference to some other ground than the intent itself. Put differently, the construction of party intent is necessarily premised on other relevant factual and legal

considerations, such as the object and purpose of the treaties, subsequent practice, previous case law dealing with conflict arguments, and the circumstances surrounding the treaties' conclusion. The same applies the other way around. Treaty texts and case law are often drafted in vague language, which brings party intent back to the equation: when legal texts can be interpreted in a number of ways, the parties' intentions become central in construing a specific meaning to a legal text, but the presiding body cannot rely only on the intent of the parties as expressed during the proceedings, because these will point in different directions.

But one might object and argue that some treaty conflicts should be resolved independently of the parties' intentions on the basis of the relevant treaty texts and case law. One might argue, for example, that the question of whether intra-EU BITs breach the principle of non-discrimination in no way depends on the intention of the BIT parties. It is up to the ECJ to determine whether a given arrangement constitutes prohibited discrimination, and whatever the parties thought about the arrangement's compatibility with EU law remains irrelevant to the Court's analysis. To rebut this argument, one could refer to the member states' consent to be bound by the ECJ's case law, which they expressed by signing and ratifying the treaties that govern EU accession. The point is that party intent will always play a role in an analysis of treaty conflict arguments, but its role varies to a considerable degree depending on the institutional context, the content of the applicable law and other case specific circumstances.

A final matter relates to the relationship of party intent and the application of specific conflict rules. In one of the arbitrations to be discussed in Chapter 3, the tribunal held that Article 30(3) VCLT 'requires no proof of the States Parties' intention to terminate a particular provision', as its application depends solely on the existence of incompatibility between the relevant treaties.⁸³ In light of the above, this statement is less correct than incorrect. Firstly, the tribunal should have footnoted the dictum so as to remind the reader that states have consented to the application of the *lex posterior* rule by signing and ratifying the VCLT and/or by acquiescing to its application as a matter of customary international law. Secondly, the intent to become bound by the VCLT indicates that states cannot argue that the *lex posterior* rule is not relevant, but they can argue that its

⁸³ *European American Investment Bank AG (Austria) v. The Slovak Republic* (hereinafter *EURAM* award), PCA Case No. 2010-17, Award on Jurisdiction, 22 October 2012, para. 240.

application is not warranted in the circumstances of the case. Thirdly, in the arbitration where the tribunal rejected the relevance of intent, it nonetheless repeatedly referred to party intent when rejecting the conflict arguments (for example, by noting that it was not the intention of the drafters of Article 344 TFEU, or the member states, to grant to the ECJ an exclusive jurisdiction that is unexceptional or absolute). Again, the relevant point is that courts and tribunals cannot resolve treaty conflicts by relying solely on the VCLT's *lex posterior* rule or party intent. Both are part and parcel of the analysis alongside other legal and factual considerations relevant in the circumstances of a case. This holds true in respect of other conflict rules as well. In this sense, Jenks' prediction in 1953 that conflict rules would eventually 'reach a more developed stage of maturity',⁸⁴ allowing a more precise delineation of their respective scopes of application remains a distant pipedream, and not only for dearth of relevant practice.

But what role do (or can) courts and tribunals have in the resolution of treaty conflicts in the first place?⁸⁵ In principle, they have two options when a conflict of treaties is established. The court can either 'disapply' one of the treaties or declare it invalid. In practice, however, courts and tribunals are disinclined to do either. Declaring a treaty null and void on the basis of a conflict with another treaty has never happened (to my knowledge) in practice, and it is difficult to come up with a scenario where this might happen, if we set aside the hypothetical situation where an international court of unlimited jurisdiction faces a conflict argument concerning the relationship of the Genocide Convention and a treaty in which the parties pledge to commit genocide.⁸⁶ Put differently, when conflict arguments relate to treaties regulating 'standard' inter-state affairs, there is little room for invalidity arguments, also because the alleged conflicts usually stem not from malevolent intent but from events unforeseen at the time of the conclusion of the relevant treaties. In yet other words, treaty conflict arguments typically relate to situations where one of the treaties contravenes with the other party's present political or economic interests, rather than to situations where one of the parties entertains Machiavellian sentiments upon the conclusion of the later treaty or at a later time. As will be shown below, this was exactly the case with member state BITs. The member states and the

⁸⁴ Jenks, 'The Conflict of Law-Making Treaties', *supra* note 46, p. 453.

⁸⁵ My discussion on this topic owes a debt to Klabbbers, *Treaty Conflict and the European Union*, *supra* note 22, and Binder, *Treaty Conflict and Political Contradiction*, *supra* note 68.

⁸⁶ The point here is that treaty conflict arguments do not usually relate to alleged conflicts between treaties containing *jus cogens* norms and treaties regulating less fundamental matters.

Commission either assumed that the treaties were not a problem from the perspective of EU law or then failed to register the matter altogether both when the BITs were concluded and during the accession negotiations preceding the 2004 and 2007 enlargement rounds.

As noted, it is possible, hypothetically speaking, for a court to declare a treaty invalid or inapplicable, but this is an unlikely event for a number of additional reasons. First, in a typical case, the presiding body only has jurisdiction over one of the relevant treaties, which denotes that it is not competent to make declarations on the treaty falling outside its jurisdiction.⁸⁷ This applies with respect to the ECJ as well; it cannot declare a conflicting member state treaty invalid or inapplicable as a matter of international law, but only hold that the primacy of EU law applies and that the member state has to comply with the relevant EU law provisions. Second, when treaty conflict arguments are raised before a court, this suggests that the parties have failed to find a political solution to the matter, but it also means that the parties are (in principle at least) obligated to accept the subsequent judgment as final and binding. Given that courts and tribunals are not in the position to take account of and balance the divergent interests of the disputing parties (because the applicable law tends to disallow this), a finding of conflict could aggravate the political situation, with the winning party becoming uncompromising and demanding compliance with the court's decision. As to the values and interests that undergird conflict arguments, their transformation into legal arguments is not easy, and a court's ability to review measures for their compatibility with the fundamental values and principles of the body of law over which it presides usually require that its mandate is of the 'constitutional' type. The mandates of arbitral tribunals and the ECJ are clearly different, but their ability to tackle 'constitutional' questions depends in large part on the cause of action and the arguments of the parties. The ECJ, for example, cannot base its analysis directly on the foundational values of the EU in the pending *Achmea* case,⁸⁸ which deals with the compatibility of intra-EU BITs with EU law, but arbitral tribunals have relied on the underlying (and value-laden) purposes of investment treaties in their reasoning on the conflict arguments. The following chapters will discuss this issue from a number of perspectives.

⁸⁷ These remarks apply with similar force in respect of treaties containing identical and non-identical parties. Although, if one of the relevant treaties has third states as parties, and those states are not taking part in the proceedings, the presiding court will be even more inclined to keep its distance from the treaty over which it has no jurisdiction.

⁸⁸ Case C-284/16, *Achmea* (pending). This case relates to an arbitration between a Dutch investor and the Slovak Republic and will be discussed in Chapter 3.

Case specific circumstances may also weaken the force of conflict arguments, and, again, member state BITs provide a good example of this. In the arbitrations discussed in Chapter 3, the respondent member states had not raised the issue of treaty conflict prior to drafting their statements of defense for submission to the tribunals. That is to say, the respondent states had not contacted the other BIT party or taken any other steps to achieve the disapplication or termination of the relevant BITs before raising the matter at the start of the arbitral proceedings.⁸⁹ Under such circumstances conflict arguments come out of the blue, so to speak, and are unlikely to convince the presiding body unless supported by other factual and legal evidence pointing to the existence of conflict. Moreover, a central canon of treaty interpretation is that states enter into treaties in good faith without intending to defeat the object and purpose of previous treaties to which they are parties. If the parties have concluded the relevant treaties without addressing their mutual relationship, and if their validity has not been challenged at any point, the presumption can only be that they continue to apply normally in their respective spheres of application. These points indicate that in most cases it is not only politically wiser but also more plausible in legal terms for a court to make a finding of compatibility and to allow the *Herren der Verträge* to settle the matter as they please. As Klabbers put it with respect to what he calls 'classical' treaty conflict cases, international courts and tribunals 'generally have accepted the co-existence of conflicting treaties as valid instruments within their own sphere. No treaty has ever been declared invalid due to conflict with either an earlier or later treaty.'⁹⁰

It is noteworthy that the treaty conflict arguments raised in the arbitrations discussed in Chapter 3 have taken the form of jurisdictional challenges. The respondent states have argued that the tribunals lacked jurisdiction over the cases because the relevant BIT had been superseded by EU law as of the respondent state's EU accession. Such arguments differ from conflict arguments related to the merits of a case in that the presiding body *is* competent to address jurisdictional challenges even though it has no jurisdiction over the other relevant treaty (here, the EU founding treaties). Such power stems from the

⁸⁹ Apart from an e-mail that the Slovak Republic sent in 2004 to the diplomatic missions of a number of EU member states in Bratislava. That e-mail asked for the recipient states' 'unofficial opinion' on the status of BITs concluded between the Slovak Republic and those other member states. Although some of the diplomatic missions replied to the e-mail, no formal action was taken at any time on the basis of the correspondence, nor did the Slovak Republic seek to terminate its intra-EU BITs by other means. The e-mail was discussed in the *Eureka* arbitration. See *Eureka* award, *supra* note 74, paras. 90-91.

⁹⁰ Klabbers, *Treaty Conflict and the European Union*, *supra* note 22, p. 61.

competence-competence doctrine, under which a court or an arbitral tribunal has the competence to decide its own jurisdiction. While arbitral tribunals have no competence to declare on the validity or alleged breaches of (primary or secondary) EU law, they are competent to rule on whether the BIT is still valid and/or applicable due to the 'influence' of EU law, and this influence could mean, for example, that the BIT parties implicitly consented to the disapplication of the BIT after both of them had acceded to the EU.⁹¹ In sum, while international courts and tribunals could make a finding of non-jurisdiction on the basis of EU law, the above suggests that such finding is highly unlikely.

There is one more issue that requires some preliminary remarks. That issue is the division of competences between the EU and its member states over foreign investment related matters. The question of competence has import with respect to extra-EU BITs in particular, whereas it is less relevant in the context of intra-EU BITs, as the discussion in Chapters 4 and 5 will show. The general principles governing competence are unambiguous, but these principles are relatively unhelpful in determining the precise division of competences between the EU and its member states in a number of policy areas. EU law provides that when a matter remains within the competence of the member states, they are free to legislate in that area, both domestically and with third states, but they nonetheless have to comply with EU law when doing so. In areas of shared competence, both the EU and the member states are free to legislate, but if the EU takes action, member states may use their competence only to the extent that the EU has not used its own competence.⁹² In areas of exclusive EU competence, 'only the Union may legislate and adopt legally binding acts', and member state action is limited to situations where the EU empowers them to act 'or for the implementation of Union acts.'⁹³

Extra-EU BITs were concluded between the 1950s and the 2010s, during which time the EU's competences over foreign investment have changed radically, with foreign direct investment becoming an exclusive EU competence with the entry into force of the Lisbon Treaty. The basic question is what impact the evolution of EU competences has had for the

⁹¹ Another related question is whether a court is competent to interpret a treaty over which it has no jurisdiction. In our case, the question is whether the EU courts can interpret BITs and whether arbitral tribunals can interpret EU law either in the context of conflict arguments or when deciding a case on the merits. Generally speaking, both institutions have such competence, but there are important distinctions and variations in this regard, which will be discussed in Chapter 5.

⁹² See Article 2(2) TFEU.

⁹³ See Article 2(1) TFEU.

status of extra-EU BITs as a matter of EU law? Prior to the Lisbon Treaty, the EU had adopted some sector-specific legislation related to third country companies (i.e. foreign investors) and also had some relevant competences (e.g. over trade in services), but the EU had no express competences over FDI or investment protection.⁹⁴ Hence, it is somewhat unclear whether extra-EU BITs came within the scope of EU law already before the Lisbon Treaty in the sense that the treaties were subject to, for example, the EU non-discrimination rules. While this question is largely academic, given the Grandfathering regulation and the uncertainties over investment protection in the context EU trade agreements, I will speculate a bit on this issue in Chapter 4, if only because much of the debate on competences is shrouded in ambiguity. It should be remembered, however, that the question of competence has no direct impact on the status of extra-EU and intra-EU BITs as a matter of international law. Member states may be obligated to amend or terminate treaties due to a transfer of competences to the EU, but outside the EU legal order the treaties remain fully valid.

2.5. Conclusion

The above discussion showed how treaty conflicts have been defined in doctrine, and how those definitions related to the conflict scenarios between EU law and member state BITs. As to specific conflict rules, it is relatively easy to identify the relevant rules and principles, but the discussion showed why the internal requirements of EU law (primacy of EU law, Article 351 TFEU and the principle of sincere cooperation) may receive a hostile reception in an international law context. Since those requirements are blind to the context, international courts and tribunals may apply a rule that prioritizes the non-EU treaty or make a finding of compatibility against, say, the arguments of the Commission. Related to this, and more generally, section 2.4. strived to show why courts and tribunals are unlikely to establish the existence of treaty conflicts. This reluctance stems from a number of factors. First, the competence of courts and tribunals is typically limited to one of the relevant treaties; second, treaty conflicts are typically undergirded by economic and political interests, which the presiding body is unable to take into account; and third, case specific circumstances may undermine conflict arguments, particularly if the treaty parties had not raised the prospect of conflict prior to the relevant proceedings. I also made some

⁹⁴ See Frank Hoffmeister and Günes Ünüvar, 'From BITS and Pieces towards European Investment Agreements', in Marc Bungenberg, August Reinisch and Christian Tietje (eds.), *EU and Investment Agreements: Open Questions and Remaining Challenges* (Nomos, 2013), pp. 57-85.

comments on the role of party intent. A central observation was that party intent is always important for an analysis of conflict arguments, but that it cannot be the only criterion against which conflict arguments are settled. Since the intent of the disputing parties points in different directions, the presiding body has to rely on other factual and legal materials to establish the intent of the parties and to resolve the conflict arguments.

All of these issues have an impact on the resolution of conflicts between EU law and member state BITs, and they will be discussed in the following chapters through and through. Chapter 3 discusses arbitral cases where the Commission and member states have argued that arbitration clauses in *intra-EU* BITs breach EU law. Their argument has been that the clauses have become inapplicable as of the EU accession of the 'new' member states in 2004 and 2007 under the *lex posterior* rule enshrined in Articles 30(3) and 59 VCLT. Arbitral tribunals have rejected these arguments on a number of grounds, and it is in this context that many of the issues discussed in this chapter will resurface and help explain the tribunals' approaches.

3. Harmonious Co-existence: Primary Conflict Arguments in Arbitral Practice

3.1. The Political Context of Primary Conflict Arguments

Since the relevant arbitral cases were raised under intra-EU BITs, it is important to say a few words on the background of these treaties. Apart from the Germany-Greece and Germany-Portugal BITs, intra-EU BITs were 'born' with the accession of the formerly socialist states to the EU in 2004 and 2007, which changed the status of around two hundred investment treaties from extra-EU to intra-EU BITs.⁹⁵ Most of the treaties were concluded in the 1990s in the wake of the dissolution of the Soviet Union, and they played a small part in the political transition from state-planned to market-based economies, signaling to western investors that new markets were open and safe for business. The formerly socialist states had also signed EU association agreements in the 1990s, each of which included a 'referential' provision on investment protection. For example, Article 64 of the EU-Romania association agreement provided that one of the aims of cooperation on investment promotion should be the 'conclusion by the Member States and Romania of Agreements for the promotion and protection of investment'.⁹⁶ In other words, the association agreements explicitly encouraged the candidate states to conclude BITs with existing member states. Against this backdrop, one might assume that the Commission, as the principal author of the association agreements, was aware of the potential problems that the parallel application of EU law and what later became intra-EU BITs might bring about after the formerly socialist states had acceded to the EU. Yet it appears that this was not the case. While the Commission expressed some concerns with respect to BITs that the candidate states had concluded with the United States,⁹⁷ there is some evidence that the

⁹⁵ The Germany-Greece and Germany-Portugal BITs were concluded in 1961 and 1980 respectively (i.e. prior to the EU accession of the latter parties). The Energy Charter Treaty (ECT), to which both the EU and its member states are parties, also provides for arbitration between EU investors and member states, but as the ECT is a so called mixed agreement I will not discuss in what follows, apart from few incidental remarks. See Energy Charter Treaty, 2080 UNTS 95.

⁹⁶ See Article 64 of the Europe Agreement establishing an association between the European Economic Communities and their Member States, of the one part, and Romania, of the other part, OJ L 357, 31.12.1994, pp. 2-173.

⁹⁷ These concerns related, above all, to the privileged treatment that EU investors were entitled to within the internal market, and the Commission sought to ensure that US investors could not invoke the BITs' national treatment and most-favored nation treatment obligations so as to demand similar treatment as EU investors in the post-2004 member states with which the US had concluded BITs. See *Understanding Concerning Certain U.S. Bilateral Investment Treaties*, signed by the U.S., the European Commission, and acceding and

problem of intra-EU BITs remained under the radar until investors from the old member states started to bring claims against the newly acceded states.

A letter sent by the Commission to the Czech Republic in connection with the *Eastern Sugar* arbitration supports this perception. The Commission letter, dated 13 January 2006, was a reply to a letter of the Czech Ministry of Finance concerning the possible effects of EU law on intra-EU BITs, and the Commission noted that 'the complexity of the questions raised has required the input and analysis by various Commission services'.⁹⁸ This suggests that the questions posed in the Czech letter took the Commission by surprise, which also explains that it took some seven months for the Commission to send the reply.⁹⁹ For now, it is unnecessary to go into the details of the letter, suffices it to note that the Commission saw, first, that EU law prevails over intra-EU BITs in case of conflict and, second, that the termination of intra-EU BITs 'would take effect according to the respective provisions of each such BIT'. Hence, the Commission recognized that intra-EU BITs remained valid and in force as a matter of international law, with investors being able to 'continue to rely on' the BITs' arbitration clauses. The Commission also noted that arbitral tribunals should give primacy to EU law in case of conflict with an intra-EU BIT, but simultaneously acknowledged that the tribunals might arrive 'at a different conclusion'. What also provides a backdrop to the letter is the Czech Republic's track record of intra-EU BITs before 2006. In 2003, for example, the *CME* tribunal had awarded the claimant investor around \$270 million (plus ten percent in interest to be paid retroactively for a period of three years) in damages for a string of the Czech Republic's regulatory decisions, which had caused the claimant to divest itself of the relevant investment.¹⁰⁰ It is noteworthy that the compensation equaled roughly the Czech Republic's health-care budget,¹⁰¹ which suggests that what prompted the letter was not simply the formal legal concerns about the compatibility of intra-EU BITs with EU law, but the fear that investment arbitration might impose an unbearable burden on the Czech Republic's finances.

candidate countries for accession to the European Union (September 22, 2003). Available at <https://www.state.gov/s/l/2003/44366.htm> (accessed 12 July 2016).

⁹⁸ Letter by Mr. Schaub of EC Internal Market and Services, 13 January 2006, sent to Mr. Zelinka, the Czech Deputy Minister of Finance. The letter is quoted in *Eastern Sugar B.V.(Netherlands) v. The Czech Republic*, SCC Case No. 088/2004, Partial Award (hereinafter *Eastern Sugar* award), 27 March 2007, para. 119.

⁹⁹ The author of the letter expressly 'apologize[d] for the delayed reply' after which the letter referred to the complexity of the Slovak Republic's questions. See *idem*.

¹⁰⁰ *CME Czech Republic B.V. v. The Czech Republic*, UNCITRAL, Final Award, 14 March 2003.

¹⁰¹ See Gus Van Harten, *Investment Treaty Arbitration and Public Law* (Oxford University Press, 2008), p. 7.

Another relevant matter was discussed in the *EURAM* arbitration. The tribunal noted that the Slovak Republic had sent letters to the member states with which it had concluded a BIT, asking whether they were willing to 'terminate [the BITs] mutually'.¹⁰² The letters were sent, apparently, around the time of the Slovak Republic's EU accession,¹⁰³ but it appears that they had not led to any formal bilateral or unilateral action. Whether the letters were the product of legal analysis or a political reaction to the threat of BIT claims is unknown,¹⁰⁴ but in legal terms inquiring about mutual termination is clearly different from raising treaty conflict arguments, and the *EURAM* tribunal noted that both the Slovak Republic and Austria (the claimant's home state) still listed the BIT 'as one of the international treaties to which they are' parties.¹⁰⁵ A third relevant fact for assessing the politics surrounding primary conflict arguments in the context of intra-EU BITs was raised in a 2008 report of the Economic and Financial Committee for the EU Council, which observed that most member states 'did not share the Commission's concern in respect of arbitration risks and discriminatory treatment of investors and a clear majority of Member States preferred to maintain the existing agreements [i.e. intra-EU BITs]'.¹⁰⁶ In other words, most member states consider that intra-EU BITs were compatible with EU law and that investors could continue to rely on their protections as before.

In sum, and apart from the two letters referred to, member states had not taken any action to terminate their mutual BITs before primary conflict arguments were raised before arbitral tribunals.¹⁰⁷ The particulars of the arbitral cases where primary conflicts have been

¹⁰² *EURAM* award, supra note 83, para. 201.

¹⁰³ The date of the letter is uncertain. On the one hand, the tribunal noted (*idem.*) that 'upon accession to the EU, the Slovak Republic had sent a note requesting its BIT partners that were EU Member States to accept a mutual termination.' On the other hand, a footnote (at para. 201, footnote 220) gives the appearance that the letter was sent only in 2011.

¹⁰⁴ Prior to its EU accession, the Slovak Republic had faced only one BIT claim, and the second claim against it was raised only in 2006, which suggests that the letters were not sent because of an increasing number of BIT claims (assuming that the letters were sent around the time of its EU accession). Assuming that the letter was sent only in 2011, the Slovak Republic had faced 6 BIT claims by then, and the Commission was also aware of the potential conflicts between EU law and member state BITs by then. This case information was derived from an UNCTAD database, see at <http://investmentpolicyhub.unctad.org/ISDS> (accessed 12 June 2016).

¹⁰⁵ *EURAM* award, supra note 83, para. 202.

¹⁰⁶ Economic and Financial Committee, *Annual EFC Report to the Commission and the Council on the Movement of Capital and the Freedom of Payments* (ECFIN/CEFCPE(2008)REP/55806), 21 November 2008, para. 17. Available at <http://register.consilium.europa.eu/pdf/en/08/st17/st17363.en08.pdf> (accessed 6 June, 2015).

¹⁰⁷ As the *Binder* tribunal put it with respect to the Czech-German BIT, 'the...BIT has not been terminated pursuant to the provision in Article 13(2) of the BIT. Nor would it seem that the Czech Republic and Germany have agreed in any other way that the BIT should be terminated or cease to be operative.' See *Binder v. Czech Republic*, Award on Jurisdiction (hereinafter *Binder* award), 6 June 2007, para. 60.

raised vary considerably and the available documentation is limited to the final awards, which means that the following discussion relies on the tribunals' expositions of the parties' conflict arguments.¹⁰⁸ The number of relevant cases where documents are available count around ten and the cases involve just three new EU member states, though in few cases a number of old member states took part in the proceedings (as claimant investors' home states) on the invitation of the tribunals.

3.2. Primary Conflict Arguments under Articles 30(3) and 59 VCLT

In each of the arbitrations, the relevant BIT had entered into force *before* the relevant EU accession treaty. This meant that the accession treaty was the later treaty in temporal terms, and this timeline had direct relevance for the application of Articles 30(3) and 59(1) VCLT. These two articles deal with successive treaties 'relating to the same subject-matter', and outline a number of rules regarding the validity, primacy and parallel application of treaties falling under their scope. Both articles endorse the *lex posterior* rule by giving priority to the later treaty. In essence, the Commission and the respondent member states argued that the arbitral tribunals lacked jurisdiction, because intra-EU BITs were superseded by EU law as of the EU accession of the new member states, which had led to the automatic termination of intra-EU BITs. An alternative argument was that arbitration clauses in intra-EU BITs were superseded by EU law and had become inapplicable upon the EU accession of the new member states. In other words, since the intra-EU BIT parties were also parties to the later accession treaties, the latter took priority under the VCLT's *lex posterior* rule if and when the BITs were in conflict with EU law.

Primary conflict arguments raised under Articles 30(3) and 59(1) VCLT have been very similar, although the criteria and implications of the two articles are quite different. Under Article 59(1) the earlier treaty is *terminated* if the conditions for its application are met, whereas under Article 30(3) the conflicting provisions of the earlier treaty become *inapplicable*. Article 59 VCLT is titled 'Termination or Suspension of the Operation of a Treaty Implied by Conclusion of a Later Treaty', and its first paragraph reads as follows:

¹⁰⁸ A short note on quotation in this regard. Sometimes the quotes are from the respondent's own submissions and sometimes they are tribunal's own phrasings of the respondent's original submissions, but I refer similarly to both.

'A treaty shall be considered as terminated if all the parties to it conclude a later treaty relating to the same subject-matter and: (a) it appears from the later treaty or is otherwise established that the *parties intended* that the matter should be governed by that treaty; or (b) the provisions of the later treaty *are so far incompatible* with those of the earlier one that the two treaties are not capable of being applied at the same time.'

Article 30 VCLT is titled 'Application of successive treaties relating to the same subject-matter'. Only paragraph 3 is relevant and it reads as follows:

'When all the parties to the earlier treaty are parties also to the later treaty but the earlier treaty is not terminated or suspended in operation under article 59, the earlier treaty applies only to the extent that its provisions are compatible with those of the later treaty.'

The question over the meaning of the phrase 'relating to the same subject-matter', which is found in both articles, received much attention in the argumentation of the disputing parties and the tribunals. Their shared premise was that the phrase is an independent precondition of application that has to be met before the other criteria are considered. In other words, if two successive treaties between identical parties do not relate to the 'same subject-matter', Articles 30(3) and 59 VCLT are inapplicable even if the other conditions for their application are met. As the *Oostergetel & Laurentius* tribunal put it, since 'the EC Treaty and the BIT do not cover the same subject matter, they cannot be considered successive treaties pursuant to Article 30 [VCLT]. Therefore, Article 30... bears no relevance to the present case'.¹⁰⁹ Both the EU Commission and respondent member states have argued that EU law and intra-EU BITs relate to the same subject-matter in the meaning of the two VCLT articles,¹¹⁰ whereas arbitral tribunals have come to an opposite conclusion.¹¹¹

¹⁰⁹ See *Jan Oostergetel & Theodora Laurentius v. The Slovak Republic, Decision on Jurisdiction* (hereinafter *Oostergetel & Laurentius award*), 30 April 2010, para. 104.

¹¹⁰ For these views, see *Eureko award*, supra note 74, paras. 65-77 and 191; *Eastern Sugar award*, supra note 98, para. 101; *Binder award*, supra note 107, paras. 13-15; *Oostergetel & Laurentius award*, supra note 109, para. 66; *EURAM award*, supra note 83, paras. 85-92; *WNC Factoring LTD v. The Czech Republic, PCA Case No 2014-34, Award* (hereinafter *WNC award*), 22 February 2017, para. 295.

¹¹¹ See *Eastern Sugar award*, supra note 98, paras. 159-165; *Oostergetel & Laurentius award*, supra note 109, paras. 74-79; *Eureko award*, supra note 74, paras. 239-267; *EURAM award*, supra note 83, paras. 165-185;

For now, it is unnecessary to discuss which of these two interpretations is more plausible, or whether both sides have misunderstood the meaning of the phrase. Clearly, determining whether BITs and EU law relate to the subject-matter does not answer whether the two treaties are in conflict. Lex posterior is but one conflict rule among many, and it is more useful to first examine whether the alleged conflicts exist before discussing which conflict rules different institutions should or are likely to apply. Logically speaking, the conclusion that BITs and EU law do not 'relate to the same subject-matter' implies that Articles 30(3) and 59 VCLT (and the lex posterior rule) are inapplicable, with other conflict rules becoming relevant. However, most tribunals have not recognized this, as they have proceeded to analyze primary conflict arguments against the other criteria of the two VCLT articles. This approach is understandable in light of the fact that the tribunals concluded that EU law and intra-EU BITs are compatible, and on the ground that their jurisdiction was challenged on the basis of the two VCLT articles alone. Likewise, excluding an analysis of the conflict arguments on the basis of the 'same subject-matter' phrase alone would have seemed overly formalistic and as reflecting a reluctance on the tribunals' part to address the conflict arguments head on.

3.3. Article 59(1) VCLT and the 'Intention and 'Incompatibility' Tests in Arbitral Practice

3.3.1. The 'Intention' Test

The first of the two alternate conditions under Article 59(1) VCLT provides that an earlier treaty 'shall be considered as terminated if all the parties to it conclude a later treaty relating to the same subject-matter' *and* if it 'appears from the later treaty or is otherwise established that the parties *intended* that the matter should be governed by that treaty' (emphasis added). The application of this clause does not require that a conflict exists between two treaties, but it may be applied in such situations as well. Leaving the issue of same subject-matter aside, the only relevant question is whether the parties intended that the earlier treaty is terminated upon the conclusion of the later treaty. There is some variation in the legal sources that the respondent member states have invoked to prove the existence of such intention, but usually the accession treaties, the overall legal framework

I.P. Busta & J.P. Busta v. The Czech Republic, SCC Case V 2015/014, Final Award (hereinafter *Busta* award), 10 March 2017, paras. 115-116; *WNC* award, *supra* note 110, paras. 296-308.

and purpose of the internal market, and the primacy and direct effect of EU law have been argued as entailing or implying that there is a mutual understanding between EU member states that their bilateral treaty arrangements relating to the internal market are superseded by the *acquis* as of EU accession.¹¹² In some cases, primacy and direct effect of EU law were invoked to emphasize that the termination of the BIT had taken place *ex lege*, requiring no formal communication between the contracting states.¹¹³

These arguments on intention failed to convince the tribunals, and quite rightly so. None of the treaties governing EU accession said anything explicit about the status of what were to become intra-EU BITs, and the provisions invoked by the respondent member states were far too vague to constitute the intention of the parties in the meaning of Article 59(1) VCLT.¹¹⁴ For example, in *Eastern Sugar*, the Czech Republic relied on Article 118 of the Czech-EU Association Agreement, according to which rights under pre-accession agreements (such as BITs) are not affected 'until equivalent rights' have been achieved through the EU integration process. The argument was that with EU accession investors had 'achieved' BIT equivalent rights, but the tribunal held that the text of the article contained no intention to terminate the relevant BIT.¹¹⁵ Similarly, the *Eureko* tribunal concluded that 'no clear intention that the BIT should be terminated' was found in the text

¹¹² See *Binder* award, supra note 107, para. 19; *Eastern Sugar* award, supra note 98, para. 102; *EURAM* award, supra note 83, paras., 94-96; *Eureko* award, supra note 74, paras. 86-93; *Anglia Auto Accessories Limited v. The Czech Republic*, SCC Case V 2014/181, Final Award (hereinafter *Anglia Auto* award, 10 March 2017, para. 102; *Busta* award, supra note 111, para. 102. The Czech government raised the 'intra-EU BIT jurisdictional objection' also in two other arbitrations argument also in the *Nepolsky v. Czech Republic* arbitration, but these proceedings were discontinued at an early stage before the tribunal had made a decision on its jurisdiction. The *Nepolsky* case materials are not publicly available. See Luke Eric Peterson, 'Water extraction claim dries up in absence of funds; claimant ordered to cover half of state's expenses in UNCITRAL arbitration', *IAR Reporter News*, 16 June 2010. Likewise, the Czech Republic raised the 'intra-EU BIT jurisdictional objection' also in the *AIYY Ltd v. Czech Republic* arbitration, which the tribunal rejected. The tribunal's decision is not publicly available, but some information on its contents is found in Luke Eric Peterson, 'Narrow investor-state clause bars investor from pursuing FET claim vs Czech Republic, but intra-EU BIT objection is rejected and expro claim will go forward', *IAR Reporter News*, 14 February 2017.

¹¹³ See e.g. *Eureko* award, supra note 74, paras. 92-93. A related question is whether the treaty termination procedure under Article 65 VCLT would have to be resorted to in order to effectuate termination under Article 59. Only the *Eureko* tribunal explicitly dealt with this matter and held that since the Slovak Republic had not followed the procedure laid out in Article 65 VCLT, it could not invoke Article 59 even if the substantive requirements for its application had been met. See *Eureko* award, supra note 74, paras. 234-238.

¹¹⁴ See e.g. *EURAM* award, supra note 83, paras. 186-210.

¹¹⁵ See Article 118 of the Europe Agreement establishing an association between the European Communities and their Member States, of the one part, and the Czech Republic, of the other part, OJ L 360, 31.12.1994, pp. 2-210; *Eastern Sugar* award, supra note 98, paras. 102, 143 and 147. It is noteworthy that the Czech Republic had adopted domestic investment law which included identical substantive protection standards as those found in BITs. The only difference was that the domestic law did not contain a provision on investor-state arbitration. This matter appears from a letter of the Czech Ministry for Finance, quoted in *Eastern Sugar* award, supra note 98, para. 127 (at p. 29).

of the 'Association Agreement, the Accession Treaty or the Lisbon Treaty'.¹¹⁶ Moreover, in two arbitrations the home states of the claimant investors were invited to express their views on the validity of the relevant BITs. In *EURAM*, for example, the Netherlands argued that the Dutch-Slovak BIT 'continues to be fully in force', with EU law having no impact on the tribunal's jurisdiction either.¹¹⁷ In a similar vein, the *Eastern Sugar* tribunal quoted a Commission letter which expressly recognized that intra-EU BITs could only be terminated by following 'the relevant procedure provided' in the BITs,¹¹⁸ and in *Eureko* the Commission recognized that the 2003 Act of Accession contained no 'intention of the parties to abrogate earlier intra-EU BITs' and neither was the Dutch-Slovak BIT 'implicitly terminated or suspended by virtue' of Article 59(1).¹¹⁹ Hence, even if Article 59(1) would provide for *ex lege* termination, such effect could only be achieved when the contracting states agree over its applicability, which implies that the party that relies on the article would at least have had to consult the other party so as to ensure that a mutual intention to terminate exists. In some cases (e.g. in *Binder*) the argument about implied termination also failed to recognize that the claimant's cause of action related to events that preceded the respondent state's EU accession. BITs typically contain so called 'sunset clauses', which stipulate that the treaties' provisions continue to be effective in respect of investments made before the date of termination for a further specified period (usually ten or fifteen years).¹²⁰ Assuming that EU accession had miraculously terminated intra-EU BITs, such termination could not extend to sunset clauses without explicit agreement of the contracting states. To terminate sunset clauses with immediate effect, the contracting states would need to expressly agree on this; the 'general' application of Article 59 (1) cannot, surely, create such effect.

¹¹⁶ *Eureko* award, supra note 74, para. 244. In *Binder*, the tribunal noted that 'the status of the Czech-German BIT was not regulated in connection with that [Accession] Treaty, and there is no indication that it was discussed during the negotiations on the Czech Republic's accession to the EU.' See *Binder* award, supra note 107, para. 59. See also *Eastern Sugar* award, supra note 98, paras. 143-147.

¹¹⁷ See *EURAM* award, supra note 83, para. 125 (submissions of the Austrian government); *Eureko* award, supra note 74, paras. 155-166 (submissions of the government of the Netherlands), the quote is from para. 161. Similarly, in *Binder*, the tribunal referred to a letter of the German Ministry for Economics and Technology, which provided that the accession of both Contracting States to the EU does not, in our opinion, bring about an automatic termination of the [Czech-German] BIT, since these agreements provide to the favoured parties other rights than those of the EC Treaty'. See *Binder* award, supra note 107, para. 61.

¹¹⁸ *Eastern Sugar* award, supra note 98, para. 119.

¹¹⁹ *Eureko* award, supra note 74, para. 187.

¹²⁰ See e.g. Article 13.3 of the Agreement on encouragement and reciprocal protection of investments between the Kingdom of the Netherlands and the Czech and Slovak Federal Republic, which reads as follows: 'In respect of investments made before the date of termination of the present Agreement the foregoing Articles there of shall continue to be effective for a further period of fifteen years from that date'.

3.3.2. The 'Incompatibility' Test

The second alternate criterion under Article 59(1) VCLT, existence of incompatibilities between member state BITs and EU law is a more complex issue. On the assumption that two successive treaties relate to the same subject matter, the incompatibility test requires that provisions of the later treaty 'are so far incompatible' with the earlier treaty that the two 'are not capable of being applied at the same time'. The respondent member states have argued that the entry into force of the accession treaties (at which point the *acquis* became binding on them) necessarily triggered such 'large' incompatibility, and the list of relevant provisions include the following: the respondent member states have argued that BIT provisions on free transfer of payments conflict with EU law provisions, which allow the imposition of restrictions on free movement of capital on public policy grounds;¹²¹ BIT expropriation clauses conflict with EU law, because EU law imposes certain requirements on member states' expropriation laws, and the criteria of lawful expropriations are different under BITs, on the one hand, and under EU law and national laws, on the other hand;¹²² BIT arbitration clauses breach Article 344 TFEU, which grants the ECJ exclusive jurisdiction over EU law related disputes involving member states;¹²³ and, finally, BIT arbitration clauses create a situation of 'direct discrimination on the basis of nationality between investors' from different member states, because only the nationals of the contracting states may resort to arbitration.¹²⁴ In sum, the extent of incompatibility between intra-EU BITs and EU law meets the threshold set in Article 59(1)(b) VCLT.

Arbitral tribunals have rejected this basic argument, but their analyses have varied greatly in terms of length and depth, in part because the arguments of the respondent member states appear to have varied to a similar extent. Some of the tribunals have also addressed some components of the incompatibility argument in relation to Article 30(3) VCLT, which will be discussed in the following section. What is interesting is that the analyses have been heavily influenced by the tribunals' understanding of the subject-matter of EU

¹²¹ See e.g. *Eureko* award, supra note 74, para. 110.

¹²² *Ibid.*, para. 111 (the Slovak Republic argued that 'the expropriation clause in Article 5 of the BIT is incompatible with the regulation of expropriation and damages under EU law, which is derived largely from the ECHR. This is because EU law enables possible restrictions on proprietary rights "necessary for the general interest" which could cause a breach of Article 5 of the BIT', footnote omitted).

¹²³ *EURAM* award, supra note, 83, paras. 98 and 101.

¹²⁴ The quote is from the EU Commission's *amicus curiae* brief in *US Steel Global Holdings I B.V. (The Netherlands) v. The Slovak Republic*, PCA Case No. 2013-6, Brussels, 15 May 2014, para. 31. See also *Eureko* award, supra note 74, para. 113 and *EURAM* award, supra note 83, para. 101; *WNC* award, supra note 110, para. 295. In *Eastern Sugar*, the Czech Republic argued more generally that the 'application of the BIT would breach the principle of non-discrimination' (see *Eastern Sugar* award, supra note 98, at para. 106).

law, on the one hand, and the subject-matter of BITs, on the other hand. As noted, the two VCLT articles speak of successive treaties that 'relate to the same subject-matter', and both the disputing parties and the arbitral tribunals have understood that the phrase constitutes an independent precondition of application. I will first outline the way in which the tribunals discussed the conflict arguments in the context of Articles 59(1)(b) and 30(3) VCLT, and will address the subject-matter issue in the last section of Chapter 3, also because it already touches on the underlying values and interests with which investment treaties are associated.

The *Binder* tribunal's reasoning on the Czech Republic's conflict arguments was impressively short; it simply concluded that no incompatibility exists between the relevant provisions of the two treaties without providing any analysis.¹²⁵ The *Eastern Sugar* tribunal, in turn, held that the Dutch-Czech BIT and EU law are not incompatible, but 'complementary things', and if the BIT gives more rights to Dutch investors than other EU investors, 'it will be for those other... investors to claim their *equal rights*....[but] the fact that these rights are unequal does not make them incompatible'.¹²⁶ In other words, the tribunal saw that the 'source' of discrimination is not the BIT but the non-discrimination rules of EU law, and that procedures exist through which EU investors can claim those rights. The *Oostergetel & Laurentius* tribunal simply quoted this reasoning of the *Eastern Sugar* tribunal when reaching the conclusion that the applicable BIT and EU law were compatible.¹²⁷

The *Eureko* tribunal's analysis was more elaborate. In essence, the tribunal held that the relevant BIT and EU law were not in conflict in the meaning of Article 59(1)(b) VCLT, because the BIT provided broader protections than EU law. For the tribunal, the fair and equitable treatment standard, the expropriation provision, and the full security and protection provision enabled bringing claims that could not be raised under EU law.¹²⁸ Equally, the possibility to resort to arbitration was a more effective remedy than remedies available under EU law or Slovak law.¹²⁹ In other words, the BIT provided broader rights

¹²⁵ *Binder* award, supra note 107, paras. 63-66.

¹²⁶ *Eastern Sugar* award, supra note 98, paras. 169-170 (emphasis in original). The tribunal did not take issue with other potential incompatibilities, and as the publicly available case documentation is limited to the final award it is unknown whether the Czech Republic raised other primary conflict arguments.

¹²⁷ *Oostergetel & Laurentius* award, supra note 109, paras. 86-87.

¹²⁸ *Eureko* award, supra note 74, para. 263.

¹²⁹ *Ibid.*, para. 264.

to investors and there was 'no reason why those rights should not be fulfilled and upheld in addition to the rights protected by EU law'.¹³⁰ The *Eureko* tribunal acknowledged that broader BIT rights 'may violate EU law prohibitions on discrimination' but this was 'not a reason for cancelling' them.¹³¹ Rather, and similarly to the *Eastern Sugar* award, member states were encouraged to extend BIT protections to all EU investors.¹³² In one way, the argument that the obligation of EU member states to provide equal treatment could have an impact on the jurisdiction of an arbitral tribunal is less than plausible. For one thing, the argument is not premised on a material conflict between EU law and BITs, but on the idea that certain treaty rights are reserved only for some actors to the exclusion of others. I will discuss this matter further in Chapter 4. The *Eureko* also discussed the relationship of Article 344 TFEU and investment arbitration, but did so only in respect of Article 30(3) VCLT, so I will discuss the tribunal's relevant reasoning in the following section.

The *EURAM* tribunal noted that its analysis with respect to Article 59(1)(b) VCLT is hypothetical as the BIT and EU law did not relate to the same subject matter in the meaning of the two VCLT articles. The tribunal first addressed the 'theoretical' question of 'what does it mean to say that two treaties are incompatible?'¹³³ The Slovak Republic's argument that conflict arises when one treaty frustrates the goals of another treaty was referred to, but the tribunal provided no analysis of the argument. Rather, the tribunal provided its own construction of incompatibility, which was based on the ordinary meaning of Article 59(1)(b) VCLT. The tribunal interpreted the phrase, 'two treaties cannot be applied at the same time', to mean that conflict occurs when 'one treaty requires what the other treaty prohibits' or 'when compliance with one treaty necessarily causes a breach of the other treaty'.¹³⁴ However, these definitions were not put into use as the tribunal next

¹³⁰ *Ibid.*, para. 263.

¹³¹ *Ibid.*, para. 266.

¹³² *Ibid.*, para. 267.

¹³³ *EURAM* award, *supra* note 83, para. 213.

¹³⁴ *Ibid.*, para. 216. The tribunal also made a somewhat confusing statement that it 'does not consider that incompatibility extends to a situation where something that is forbidden under the BIT is merely permitted by EU law, or vice versa', which was followed by the dictum that the tribunal 'does not consider that two treaties are incompatible when they point in the same direction or when the rules they adopt are similar' (see para. 217). This was also what the *Eureko* tribunal was implying, although in equally vague terms (see *Eureko* award, *supra* note 74, paras. 253-254). It appears that the *EURAM* tribunal referred to a situation where member states are free to adopt certain measures as a matter of EU law, typically in an area over which they have exclusive competence, but which measures may still breach e.g. the fair and equitable treatment standard. But this seems to be premised on a logical error: while in the implied situation there is no conflict between the BIT and EU law to the extent that the latter sanctions the measure, the argument that BIT arbitration clauses breach EU law are premised precisely on the idea that EU law 'forbids' something that the BIT 'permits'.

held that 'far from being necessarily incompatible', the BIT and EU law 'can be cumulatively applied'.¹³⁵ To support this conclusion, the tribunal relied on the distinction between pre- and post-establishment treatment of investments, and saw that EU law is focused on the pre-establishment phase whereas BITs protect investments once they are made.¹³⁶ I will return to this distinction below in section 3.5. The tribunal also relied on a number of cases from different contexts to make the point that nothing prevents the 'cumulative' application of two treaties even if they deal with the same subject-matter. The referred cases included an ICSID case where the tribunal held that two tribunals could exercise concurrent jurisdiction 'with respect to the same parties, the same facts and the same cause of action', because 'there is no rule of international law which prevents either tribunal from exercising its jurisdiction'.¹³⁷ By analogy, that investors can obtain remedies under both EU law and the BIT 'does not render them incompatible', but in fact does the reverse, as those remedies 'must be considered as parallel since they enhance the protection of the investor'.¹³⁸ Another case referred to was a case brought before the International Tribunal for the Law of the Sea, in which the tribunal first held that two treaties applied to the dispute and then argued that such 'parallelism of treaties, both in their substantive content and in their provisions for settlement of disputes' is not an infrequent phenomenon.¹³⁹ The point of these separate sources was to substantiate the conclusion that the BIT and EU law 'are not so incompatible that...[they] cannot be applied at the same time'.¹⁴⁰

In sum, the *EURAM* tribunal held that the relevant BIT and EU law are complementary legal frameworks whose parallel application does not create a treaty conflict in the meaning of Article 59(1)(b) VCLT. The discussion traveled at a fairly abstract level and excluded an analysis of the alleged conflicts between specific provisions of the BIT and EU law. However, the tribunal did analyze a number of more specific conflict arguments,

¹³⁵ *Ibid.*, para. 228. For the Slovak Republic's conflict arguments related to Article 59(1)(b) VCLT, see paras. 98-104.

¹³⁶ *Ibid.*, para. 180.

¹³⁷ The tribunal was quoting *Southern Pacific Properties (Middle East) Limited v. Arab Republic of Egypt*, ICSID Case No. ARB/84/3, First Decision on Jurisdiction, 27 November 1985, paras. 28 and 30.

¹³⁸ *EURAM* award, *supra* note 83, paras. 229-230. The tribunal referred to one academic source as well, and the author in question had argued, *inter alia*, that 'bilateral investment protection treaties are "added" legal guarantees for investors', which 'help to increase and enhance the overall level of legal protection of economic subjects in the internal market'. *Ibid.*, para. 232. This quote is from Tietje, 'Bilateral Investment Protection Treaties between EU Member States', *supra* note 17, p. 19.

¹³⁹ *Ibid.*, para. 231. The quote is from *Southern Bluefin Tuna case (Australia and New Zealand v. Japan)*, Award on Jurisdiction and Admissibility, 4 August 2000, UNRIAA vol. XXIII (2004), p. 23, para. 52.

¹⁴⁰ *Ibid.*, para. 234.

but this analysis was carried out only in relation to Article 30(3) VCLT, to which I now turn.

3.4. Article 30(3) VCLT in Arbitral Practice

The conflict arguments in the context of Article 30(3) VCLT have been identical to the arguments raised under Article 59(1)(b) VCLT, so there is little point in repeating them in detail.¹⁴¹ The most common argument is that intra-EU BIT arbitration clauses breach, first, the exclusive jurisdiction of the ECJ to preside over disputes involving questions of EU law, and, second, that the clauses breach the principle of non-discrimination as the nationals of the contracting states alone are able to bring claims under BITs. Another central component of these two arguments was that the EU accession of the new member states triggered the conflicts and that it was the tribunals' obligation to decline jurisdiction under the *lex posterior* rule. Given the tribunals' previous dismissal of similar arguments in relation to Article 59 VCLT, it was predictable that most tribunals quickly rejected arguments based on Article 30(3) VCLT.¹⁴² The *Eureko* and *EURAM* awards contain lengthier analyses of the conflict arguments on Article 30(3) VCLT, and it is useful to discuss them in more detail, as this will pave the way for the discussion in Chapter 4 which adopts the perspective of EU law. The *Eureko* arbitration is also interesting because the Slovak Republic appealed the tribunal's decisions before German courts, and in March 2016 the *Bundesgerichtshof* (BGH) decided to submit preliminary questions to the ECJ on the Dutch-Slovak BIT's compatibility with EU law.

As already noted, in respect of discrimination, the *Eureko* tribunal repeated the advice that the solution is to extend the applicability of the arbitration clause (and presumably the

¹⁴¹ For references, see above footnotes 121-124.

¹⁴² Article 30(3) was not discussed in the *Binder* award and since the award is the only available document it is unknown whether the respondent invoked it in the first place. In *Eastern Sugar*, the tribunal noted that the Slovak Republic had made an argument under Article 30(3) VCLT, but no substantial analysis of the argument followed (see *Eastern Sugar* award, supra note 98, paras. 178-180). The *Oostergetel & Laurentius* tribunal held that Article 30(3) VCLT was irrelevant because the general requirement that two successive treaties must relate to the subject matter was not satisfied (see *Oostergetel & Laurentius* award, supra note 109, para. 104). The *WNC Factoring* tribunal followed and endorsed the *Eastern Sugar* tribunal's approach by noting that the 'fact that the BIT affords certain rights not available to other EU investors does not make the BIT discriminatory; there is nothing in the BIT that prevents investors of other states claiming equal rights under the BIT.' See *WNC* award, supra note 110, para. 309. Finally, the *Anglia Auto* and *Busta* tribunals held that the exclusive jurisdiction of the ECJ is not threatened when the tribunals decide the disputes brought before them, because the latter interpret and apply the relevant BITs and not the articles of the TFEU. See *Anglia Auto* award, supra note 112, para. 127 and *Busta* award, supra note 111, para. 127.

protection standards) to cover all EU investors.¹⁴³ The tribunal also referred to the exclusive jurisdiction of the ECJ (under Article 344 TFEU) over disputes between member states concerning the interpretation and application of EU law, but held that this article has no relevance for disputes between private parties and member states.¹⁴⁴ More generally, the tribunal held that 'no rule of EU law prohibits' arbitration under member state BITs; on the contrary, investor-state arbitration and other types of arbitration are prevalent across the EU, with the ECJ having rendered judgments on how arbitral tribunals should take account of EU law.¹⁴⁵ As a conclusion, there was no incompatibility in the meaning of Article 30(3) VCLT. The Slovak Republic challenged the tribunal's decision on jurisdiction before German courts.¹⁴⁶ After an unsuccessful appeal before Frankfurt's *Oberlandesgericht*,¹⁴⁷ the Slovak Republic seized the *Bundesgerichtshof* (BGH), but as the *Eureko* tribunal had rendered its final award prior to the BGH proceedings, the latter held that Slovakia's request for relief had become inadmissible.¹⁴⁸ The Slovak Republic challenged the final award on similar grounds before the Court of Appeal, but the *Oberlandesgericht* rejected Slovakia's arguments on broadly similar grounds as in the previous decision.¹⁴⁹ Again, the Slovak Republic appealed and in March 2016 the BGH decided to submit preliminary questions to the ECJ on the compatibility of the Dutch-Slovak BIT's arbitration clause with EU law.¹⁵⁰

¹⁴³ *Eureko* award, supra note 74, paras. 266-267.

¹⁴⁴ *Ibid.*, paras. 276 and 282. The *Electrabel* tribunal made a similar point (see *Electrabel S.A. v. The Republic of Hungary*, ICSID Case No. ARB/07/19, Decision on Jurisdiction, Applicable Law and Liability (hereinafter *Electrabel* award, 30 November 2012, paras. 4.150-4.151).

¹⁴⁵ *Eureko* award, supra note 74, para. 274. The tribunal referred to Case C-126/97, *Eco Swiss China Time Ltd v. Benetton International NV*, ECLI:EU:C:1999:269, which will be discussed in Chapter 5.

¹⁴⁶ Frankfurt was the seat of the *Eureko* arbitration and German law constituted the *lex loci arbitri*.

¹⁴⁷ See decision of the *Oberlandesgericht Frankfurt am Main*, 26 SchH 11/10, 10 May 2012. Available (in German) at <http://www.italaw.com/sites/default/files/case-documents/ita0931.pdf> (accessed 14 January 2017). In a nutshell, the Court of Appeal found that investor-state arbitration did not come within the scope of Article 344 TFEU; that national courts can review the EU law compatibility of the decisions of arbitral tribunals and, when necessary, submit preliminary questions to the CJEU under Article 267 TFEU (in other words, the court held that decisions of arbitral tribunals do not escape the preliminary ruling procedure, at least in *Eureko* like circumstances); that the arbitration clause may violate Article 18 TFEU (i.e. the principle of non-discrimination), but such finding does not invalidate the BIT's arbitration provision, but obliges the contracting states to extend BIT protections to all EU investors; Article 30(3) VCLT was also irrelevant because EU law does not prohibit investor-state arbitration and thus no incompatibility in the meaning of Article 30(3) exists (see pp. 15-25 of the judgment).

¹⁴⁸ See decision of the *Bundesgerichtshof*, III ZB 37/12, 19 September 2013, para. 8. The decision is available (in German) at <http://www.italaw.com/sites/default/files/case-documents/italaw1606.pdf> (accessed 14 January 2017).

¹⁴⁹ See decision of the *Oberlandesgericht Frankfurt am Main*, 26 SchH 3/13, 18 December 2014. The decision is available (in German) at <http://www.lareda.hessenrecht.hessen.de> (accessed 14 January 2017).

¹⁵⁰ *Bundesgerichtshof*, Beschluss I ZB 2/15 vom 3. März 2016 in dem Verfahren auf Aufhebung eines inländischen Schiedsspruchs (hereinafter *Eureko* referral).

More specifically, the BGH asked whether '*eine Schiedsklausel in einem unionsinternen BIT mit dem Unionsrecht und insbesondere mit Art. 344, 267 und 18 AEUV vereinbar ist.*'¹⁵¹ The BGH noted that the ECJ's existing case law does not provide sufficient certainty on the matter, but in the decision concerning the submission of the preliminary questions, the BGH came to endorse the approach of the arbitral tribunals. I will discuss the BGH's decision in detail in Chapter 4, so at this point it suffices to summarize some of its main arguments. As to the exclusive jurisdiction of the ECJ under Article 344 TFEU, the BGH argued that it does not affect arbitration under intra-EU BITs, in particular because investors have no similar right to demand compensation from member states under EU law.¹⁵² This implies that the BGH views the arbitration clause as complementing EU remedies, which is analogous to the reasoning of (e.g.) the *Eastern Sugar* tribunal. As to the preliminary ruling mechanism under Article 267 TFEU, the BGH rejected the argument that the inability of arbitral tribunals to submit preliminary questions to the ECJ threatens the uniform interpretation of EU law (which is the object and purpose of Article 267 TFEU). The BGH reasoned that member state courts can ensure that arbitral awards are compatible with EU law at the enforcement stage by reviewing the award by themselves or by using the preliminary ruling mechanism. The BGH drew an analogy between commercial and investor-state arbitration. The ECJ has held that the effectiveness of commercial arbitration requires that arbitral awards are assessed only to a limited extent to ensure their compatibility with EU law and that arbitral awards should be annulled only in exceptional circumstances. For the BGH, the same basic principles should apply in respect of investor-state arbitration as well.¹⁵³ On Article 18 TFEU, the BGH noted that

¹⁵¹ This and the following quotes are from the press release which summarizes the preliminary questions and the BGH's stance on them. See Bundesgerichtshof, Mitteilung der Pressestelle, 'Bundesgerichtshof legt Europäischem Gerichtshof Fragen zur Wirksamkeit von Schiedsvereinbarungen in Investitionsschutzabkommen vor', Nr. 81/2016 (10.5.2016), Beschluss vom 3. März 2016 - I ZB 2/15. The press release is available at <http://www.bundesgerichtshof.de> (accessed 14 January 2017).

¹⁵² The BGH reasoned: 'Das an die Mitgliedstaaten gerichtete Gebot des Art. 344 AEUV, Streitigkeiten über die Auslegung und Anwendung der Unionsverträge allein durch die dort vorgesehenen Verfahren zu regeln, schließt nach Auffassung des Bundesgerichtshofs nicht aus, eine Streitigkeit zwischen einem Unternehmen und einem Mitgliedstaat vor einem Schiedsgericht auszutragen. Insbesondere sehen die Unionsverträge kein gerichtliches Verfahren vor, in dem ein Investor Schadensersatzansprüche geltend machen kann, die ihm aus einem unionsinternen BIT gegen einen Mitgliedstaat erwachsen.'

¹⁵³ According to the BGH: 'Die einheitliche Auslegung des Unionsrechts, die Art. 267 AEUV gewährleisten soll, kann im Schiedsverfahren dadurch sichergestellt werden, dass vor einer Vollstreckung das staatliche Gericht die Vereinbarkeit des Schiedsspruchs mit dem Unionsrecht überprüft und bei Zweifeln über die Auslegung einer unionsrechtlichen Vorschrift die Sache dem Gerichtshof der Europäischen Union vorlegt. Diese Prüfungsbefugnis besteht zwar nur bei grundlegenden Bestimmungen des Unionsrechts, die für die Erfüllung der Aufgaben der Union und insbesondere für das Funktionieren des Binnenmarkts unerlässlich sind, und deshalb zur öffentlichen Ordnung (ordre public) zählen. Der Gerichtshof der Europäischen Union hat dies jedoch bei Schiedssprüchen in Streitigkeiten zwischen Privaten als zulässig angesehen, weil die Erfordernisse der Effizienz des Schiedsverfahrens es rechtfertigten, Schiedssprüche nur in beschränktem

arbitration clauses may constitute prohibited discrimination, but the solution is not necessarily their inapplicability, but the extension of their scope of application to cover all EU investors; again, this is very much in line with the arbitral tribunals' view on the matter.¹⁵⁴ In sum, the BGH did imply that in case of conflict EU law would prevail over the BIT, but it also saw that the two treaties did not relate to the same subject-matter (without, of course, referring to the VCLT), and that there is no reason to treat investor-state arbitration differently from commercial arbitration, with the ECJ having ruled that the latter is clearly compatible with its own jurisdiction. Chapter 4 will address the analogy between commercial and investment arbitration, and will also analyze the other central arguments of the BGH.

In *EURAM*, the tribunal first analyzed whether BIT arbitration clauses breach the exclusive jurisdiction of the ECJ as provided for in Article 344 TFEU. Perhaps it is useful to quote the full text of the article at this point, and it reads as follows:

'Member States undertake not to submit a dispute concerning the interpretation or application of the Treaties to any method of settlement other than those provided for therein.'

The tribunal maintained that Article 344 TFEU 'does not provide for an absolute monopoly of the ECJ over the interpretation and application of EU law'.¹⁵⁵ Given its plain wording, the tribunal reasoned, investment arbitration does not come within its scope and neither does EU law contain any other provisions that would either prohibit or conflict with BIT arbitration clauses.¹⁵⁶ The argument that the ECJ's interpretive monopoly is not absolute was propped by a number of factual and legal considerations. First, the tribunal noted that

Umfang auf die Vereinbarkeit mit Unionsrecht zu überprüfen und die Aufhebung eines Schiedsspruchs oder die Versagung seiner Anerkennung nur in außergewöhnlichen Fällen vorzusehen. Der Bundesgerichtshof möchte bei Schiedsverfahren zwischen einem privaten Unternehmen und einem Mitgliedstaat keine anderen Maßstäbe anwenden.'

¹⁵⁴ In the words of the BGH: 'Allerdings könnte die Schiedsklausel des BIT gegenüber Investoren anderer Mitgliedstaaten, die kein Schiedsgericht anrufen können, eine Diskriminierung im Sinne von Art. 18 Abs. 1 AEUV darstellen. Das hätte aber nicht zwangsläufig zur Folge, dass sich die Antragsgegnerin nicht auf die Schiedsklausel berufen könnte. Nach der Rechtsprechung des Gerichtshofs der Europäischen Union wird eine Dritte diskriminierende Vorteilsgewährung regelmäßig dadurch beseitigt, dass die benachteiligten Personen Anspruch auf die gleiche Behandlung wie die begünstigten Personen haben. Diesen Dritten müsste also gegebenenfalls bei Streitigkeiten mit der Antragstellerin in gleicher Weise Zugang zu einem Schiedsgericht gewährt werden.'

¹⁵⁵ *EURAM* award, supra note 83, para. 248.

¹⁵⁶ *Ibid.*, paras. 255-259

courts and tribunals operating outside the Union regularly interpret and apply EU law, for example in commercial disputes, and the ECJ has no means to ensure that these interpretations conform with its case law.¹⁵⁷ Second, although member state courts are either authorized or obliged to submit questions to the ECJ under Article 267 TFEU, they retain some element of discretion as to whether to resort to the preliminary ruling mechanism, which creates the possibility of misinterpretation and misapplication of EU law.¹⁵⁸ Third, commercial arbitration is a commonplace within the EU, and the ECJ is excluded from reviewing arbitral awards when the parties comply with an award or when the competent national court considers it unnecessary to submit preliminary questions.¹⁵⁹ Fourth, when arbitral proceedings take place within the EU, the ECJ has repeatedly held that commercial arbitral tribunals have an obligation to apply 'fundamental' EU law (therewith sanctioning their existence), and the central case to which the tribunal referred concerned a commercial arbitration, the seat of which was in the Netherlands.¹⁶⁰ Moreover, as the *EURAM* tribunal's seat was Stockholm, the parties could appeal its decisions before Swedish courts, which in turn could seek preliminary ruling from the ECJ on relevant questions of EU law. The tribunal also noted that if member states' courts were to enforce arbitral awards that violate EU law, the Commission may start infringement proceedings under Article 258 TFEU, which ensures the integrity of the EU legal order in all possible scenarios.¹⁶¹ As a last point, the tribunal noted that investor-state tribunals have regularly interpreted and applied EU law 'without [this] raising any problems', and the *Maffezini* arbitration was referred to as an example.¹⁶²

¹⁵⁷ *Ibid.*, para. 251. The tribunal used the example of a commercial dispute between a European and Argentinian company brought before an Argentinian court. See also *Electrabel* award, supra note 144, para. 4.149.

¹⁵⁸ *EURAM* award, supra note 83, para. 252; for a similar point, see *Electrabel* award, supra note 144, para. 4.148. According to the settled case law of the ECJ 'it is solely for the national courts...to determine in the light of the particular facts of each case both the need for a preliminary ruling in order to enable them to deliver judgment and the relevance of the questions which they submit to the Court'. See Case C-373/95, *Gazzetta et al.*, ECLI:EU:C:1997:348, para. 26.

¹⁵⁹ *EURAM* award, supra note 83, para. 256.

¹⁶⁰ *Idem.*, footnote 263 (as in *Eureko*, the tribunal referred to the *Eco Swiss* case, see supra note 145).

¹⁶¹ *Ibid.*, para. 264.

¹⁶² *Ibid.*, para. 266. See *Emilio Agustín Maffezini v. Spain*, ICSID Case No. ARB/97/7, Award, 13 November 2000, para. 69. The claimant investor argued that he was entitled to be compensated for the costs of an environmental impact assessment (EIA) made in connection with a construction project. The EIA was mandated by an EEC directive and by Spain's national law, and the tribunal held that the claimant was well aware that he was obligated to carry out an EIA prior to commencing the project. Hence, the tribunal treated the Directive as evidence (i.e. as a fact) only and not as part of applicable law. Chapter 4 discusses extensively the 'roles' that EU law may have in investment arbitration.

To sum up, the tribunal held that the ECJ has no power to control all contexts where EU law is interpreted and applied, but there is always a way to involve the Court at the post-award stage, ultimately through the Commission if the latter finds that compliance with an award violates EU law. It is useful to note that, as the *EURAM* tribunal pointed out, there are instances where member state courts and the ECJ are excluded from reviewing how arbitral tribunals have interpreted and applied EU law. To give an example, national courts cannot (in principle) review the contents of ICSID awards or submit related preliminary questions to the ECJ, and as the *Eureko* tribunal observed, the ECJ cannot become involved in arbitrations taking place and enforcements of awards transpiring outside the EU. If in such cases a member state refuses to comply with an award and the investor seeks enforcement within the EU, national courts have limited possibilities to review the award or refer preliminary questions concerning the tribunal's treatment of EU law, and this topic is addressed in Chapter 5. It is also noteworthy that neither the parties nor the *EURAM* tribunal addressed directly the autonomy of the EU legal order, but focused solely on the BIT's compatibility with Articles 258 and 267 TFEU. These articles relate to specific cases where national courts and the Commission can seize the ECJ to ensure that EU law is interpreted correctly and that member states comply with EU law. The more principled question of whether arbitration clauses breach the autonomy of the EU legal order as a matter of EU law is not, arguably, addressed exhaustively through a discussion of these two articles. As to Article 344 TFEU, the *EURAM* tribunal held that it has no relevance for member state BITs as it only relates to disputes between member states. Conversely, the Commission has argued that Article 344 TFEU reflects a more general principle under which member states are not authorized to conclude treaties, which create dispute settlement mechanisms under which questions of EU law may be raised. Chapter 5 will address the scope of Article 344 TFEU.

In its discussion on discrimination, the *EURAM* tribunal relied heavily on the claimant's expert whose point of departure was that discrimination 'is an internal EU law problem and not an issue of treaty compatibility'.¹⁶³ The logic was that even if intra-EU BITs discriminate between EU investors, this cannot affect the applicability of the arbitration clause, because it is up to the Commission to take action against the discriminating member states.¹⁶⁴ The tribunal also cited the *Eastern Sugar* and *Eureko* awards when

¹⁶³ *EURAM* award, supra note 83, para. 270 (quoting the opinion of Reinisch).

¹⁶⁴ *Idem*.

instructing EU investors to 'seek enforcement' of the BIT rights they are not entitled to.¹⁶⁵ Another suggestion was that EU investors are able to utilize the relevant BIT by structuring their investments so as to qualify as investors under it. After all, investors enjoy freedom of establishment within the EU internal market.¹⁶⁶ The tribunal also drew inspiration from the *D v Inspecteur* case, which concerned the Dutch-Belgium double taxation treaty, and claimed that the judgment is relevant in the intra-EU BIT context.¹⁶⁷ The *D v Inspecteur* case concerned a Dutch wealth tax allowance granted to non-resident Belgian citizens in the Dutch-Belgium treaty, which the claimant, a German citizen owning property in the Netherlands, was not entitled to utilize. The ECJ held that Mr. D was not in a situation equivalent to non-resident Belgian citizens, which meant that the different treatment resulting from the bilateral tax treaty was not discriminatory. By analogy, the *EURAM* tribunal claimed that EU investors from other member states are not in the same situation as the BIT parties' investors and that the arbitration clause is thus non-discriminatory.¹⁶⁸ The *D v Inspecteur* case and other findings of the tribunal will be discussed extensively in Chapters 4 and 5.

To summarize, arbitral tribunals have produced a *jurisprudence constant*, under which intra-EU BITs are compatible with EU law. Some tribunals have recognized that arbitration clauses may breach the principle of non-discrimination, but this problem is resolved by extending their scope of application to cover all EU investors. Such solution finds some support in the case law of the ECJ, and in Chapter 4 I discuss whether its application is plausible in the BIT context. As to the exclusive jurisdiction of the ECJ, the tribunals saw that the Court's jurisdiction is not absolute but subject to (de jure and de facto) exceptions, with the Court's jurisprudence on commercial arbitration applying with equal force in respect of investment arbitration. What also undercuts the 'exclusive jurisdiction' argument, though the tribunals did not refer to this, is that in most cases EU law had no bearing on the investors' causes of action. For example, in *IP Busta*, the question was whether the actions of the Czech Police breached the fair and equitable treatment standard of the Czech-UK BIT. The claimants were UK citizens who had formed a joint venture with a Czech company, and the latter had moved (or stolen) certain goods owned by the claimants, which the local police later seized and returned to Messrs. Busta

¹⁶⁵ Ibid., paras. 270-272.

¹⁶⁶ Ibid., para. 273.

¹⁶⁷ Case C-376/03, *D v Inspecteur*, ECLI:EU:C:2005:424.

¹⁶⁸ *EURAM* award, supra note 83, para. 278.

and Busta. The claimants alleged that the police had not returned all of the goods and had also failed to make an itemized list of the goods 'as required by Czech law'.¹⁶⁹ This allegedly breached the BIT's protection standards and the claimants sought compensation in the amount of 2.4 million euros. In *WNC Factoring*, the claimant argued that the Czech Republic had, inter alia, provided 'misleading and inaccurate information' about a state-owned company, which the claimant had acquired through a public tender process.¹⁷⁰ The investment turned out to be a disaster, and the claimant argued that Czech authorities had withheld vital information during the due diligence process preceding the acquisition.

In neither case was any question of EU law raised on the merits, and the short case descriptions available at UNCTAD's database testify that the same holds true with a high number of other claims raised under intra-EU BITs. This indicates that in many intra-EU arbitrations the exclusive jurisdiction of the ECJ (or the uniform interpretation of EU law) are not under threat, and conflict arguments that rely on Article 344 TFEU will appear immaterial in such circumstances. Of course, the member states have to respect the internal market freedoms and the principle of non-discrimination even in areas that are not subject to EU harmonization, but domestic policy may comply with these cornerstones of EU law and still breach BIT standards as the above case examples testify. Similarly, in each case the tribunal's seat was in a member state, which supported the argument that the tribunals' decisions were subject to (however limited) review by member state courts and the ECJ.

3.5. Conclusion and a Prelude to the Question of Values and Interests

In retrospect, the conflict arguments had little chance of convincing the tribunals as the surrounding political and legal landscape pointed in the opposite direction. The Commission recognized that EU accession had had no effect on the validity or applicability of intra-EU BITs and neither had the Commission raised the matter at any point on its own initiative,¹⁷¹ with the Czech government's 2006 letter taking the

¹⁶⁹ *Busta* award, supra note 111, para. 6.

¹⁷⁰ *WNC* award, supra note 110, para. 101.

¹⁷¹ For this view, see *Eureka* award, supra note 74, para. 187 (the Commission noted that EU member states 'should terminate' intra-EU BITs, but also acknowledged 'that neither party appears to have taken any decisive step formally to terminate this BIT.' Further, the Commission acknowledged that the 2003 Act of Accession did not contain 'any intention of the parties to abrogate earlier intra-EU BITs', which meant that in the Commission's eyes the Dutch-Slovak BIT was not 'implicitly terminated or suspended by virtue of Article

Commission staff by surprise. A related point raised by some tribunals was that the ECJ had not rendered a relevant judgment on intra-EU BITs;¹⁷² for example, having rejected the conflict arguments, the *WNC Factoring* tribunal noted that the ECJ might eventually adopt a 'different view' on the matter.¹⁷³ The respondent states' failure to take formal action to terminate the relevant BITs also spoke in volumes against the argument that the parties had entertained a relevant intent (implied or express) over the relationship of the treaties prior to or upon their EU accession. That the treaties governing EU accession provided no such evidence on party intent either, further supported this conclusion.

The political context of the conflict arguments was expressly referred to in most awards. For example, the *Binder* tribunal noted that the question 'whether measures should be envisaged to terminate intra-EU BITs...has given rise to some debate within the EU but has not been finally settled even as a policy matter to this date.'¹⁷⁴ In *Eastern Sugar*, the tribunal observed that the Commission had not started 'infringement proceedings against the Netherlands and the Czech Republic', or against other member states for failing to terminate their mutual BITs.¹⁷⁵ Similarly, the *Oostergetel & Laurentius* tribunal noted that the Slovak Republic 'has not implied that at any point in time there had been an effort on either part of Slovakia and the Netherlands to terminate or re-negotiate the BIT'.¹⁷⁶ The view of old member states that intra-EU BITs cause no problems for EU law was also invoked a number of times, so as to accentuate the 'weakness' of the respondents' conflict

59(1)' of the VCLT.); the EU Commission's amicus curiae brief in *US Steel*, supra note 124, para. 19 (the Commission noted that it 'is common ground that no provision of the Europe Agreement, the Treaty on Accession or the Treaty of Lisbon explicitly terminates or suspends the operation of the [Dutch-Slovak] BIT.'). However, in the state aid decision concerning the *Micula* award, the Commission argued that intra-EU BITs 'are contrary to Union law, incompatible with provisions of the Union Treaties and should therefore be considered invalid'. This, of course, is an internal EU law argument and is explained by its context. See *Micula* state aid decision, supra note 5, para. 128.

¹⁷² The *Oostergetel & Laurentius* tribunal noted that the 'Dutch-Slovak BIT was not terminated upon Respondent's accession to the EU and therefore the EC Treaty is not an obstacle for this Tribunal to settle the present dispute under the applicable BIT. *This is especially so considering the absence of any conclusive position of the EC or the ECJ on this question*' (emphasis added). *Oostergetel & Laurentius* award, supra note 109, para. 109

¹⁷³ *WNC* award, supra note 110, para. 311.

¹⁷⁴ *Binder* award, supra note 107, para. 64.

¹⁷⁵ *Eastern Sugar* award, supra note 98, para. 121. The tribunal also noted (in para. 122) that 'neither the Czech Republic nor the Netherlands, nor anybody else, did file a complaint to the European Commission against the Netherlands and the Czech Republic and other members in similar position, concerning their failure to comply with EU Law by leaving their BITs in place'. Likewise, in para. 155, the tribunal noted that 'the Netherlands and the Czech Republic still list their BIT as one of the international treaties to which they are a Party'.

¹⁷⁶ *Oostergetel & Laurentius* award, supra note 109, para. 84. See also *Anglia Auto* award, supra note 112, para. 116 ('the Tribunal notes that the parties to the BIT, the Czech Republic and the United Kingdom [have] never sought to terminate the BIT following the procedures set out by that instrument.').

arguments.¹⁷⁷ The Commission also took part in some of the proceedings on the invitation of the tribunals, and some of its observations were not necessarily conducive to the argument it was making. In *Eureko*, for example, the Commission noted that the 'arguments in favour of maintaining an investor-State arbitration mechanism for intra-EU BITs are not persuasive from an internal EU law perspective.'¹⁷⁸ This amounts to recognizing that such internal perspective is by and large immaterial in an international law context, and some of the respondent member states were less than impressed by the Commission's intervention.¹⁷⁹ Of course, the Commission did start infringement proceedings in respect of intra-EU BITs, but only in 2015, and such proceedings do not necessarily change the position of arbitral tribunals vis-à-vis conflict arguments. As the *Eastern Sugar* tribunal put it, 'the answer to the [conflict] questions raised must be given by *judicial authorities*, which clearly excludes the European Commission'.¹⁸⁰

On top of these considerations, the disputing parties, the Commission and hence the tribunals used much energy on the question of whether BITs and EU law relate to the same subject-matter in the meaning of Articles 30 and 59 VCLT. While it is unnecessary to go into the details of the matter, it is important to note that the question of subject-matter is closely tied to the question of treaty conflict. If EU law and BITs are understood as relating to different subject-matters, then it is intuitively more plausible to find that there is no conflict between them either. For the tribunals, a central distinguishing factor between BITs and EU law was the ability of investors to bring claims against the host state. This fact was raised again and again by the tribunals both in their analysis of the question of subject-matter and the question of treaty conflict. Such remedy, they reminded, is not available under EU law, and the fact that the EU has not legislated in the area of investment protection (in part for want of competence) also supported the perception that BITs and EU law are distinct species. The tribunals emphasized that the BIT's arbitration clause 'is the best guarantee that the investment will be protected against potential undue infringements by the host state', with EU law not providing 'such a guarantee'.¹⁸¹ This fact alone was 'sufficient to reject the...argument' that EU law and BITs relate to the same

¹⁷⁷ See e.g. *Oostergetel & Laurentius* award, supra note 109, para. 108.

¹⁷⁸ *Eureko* award, supra note 74, para. 179.

¹⁷⁹ The Slovak Republic (as respondent) politely noted that 'the Commission did not examine in depth the question of incompatibility of the BIT and EU law [in its written observations]'. Ibid., para. 200.

¹⁸⁰ *Eastern Sugar* award, supra note 98, para. 124.

¹⁸¹ Ibid., para. 165.

subject-matter.¹⁸² Here are some other relevant excerpts: 'there is at least one fundamental distinction between' BITs and EU law which renders 'them incomparable: the EC Treaty provides no equivalent to one of, if not the most important feature of the BIT regime, namely, the dispute settlement mechanism providing for investor-State arbitration',¹⁸³ 'the TFEU does not address' investment protection 'at all' , and the tribunal 'is not convinced' that the... TFEU provisions are substantive equivalents of the provisions of the BIT, in particular in light of the absence of an important substantive protection in the TFEU, that of investors' access to an international and neutral dispute resolution forum in the form of international arbitration'.¹⁸⁴ These descriptions are premised on a mental image where the relevant treaties are seen as operating in isolation of each other, with each treaty having a distinct sphere of application.

Another distinguishing factor raised by a number of tribunals relates to the distinction between pre-establishment and post-establishment treatment of investments. The *EURAM* tribunal noted that the two treaties have 'a generally different approach', with EU law 'being more focused on the pre-establishment period, and the BIT on the post-establishment period'.¹⁸⁵ The *WNC Factoring* tribunal, in turn, endorsed the idea that EU law is concerned with 'capital inflows and outflows', whereas BITs afford protection 'to investments whilst operating',¹⁸⁶ and the *Eastern Sugar* tribunal echoed this by remarking that the relevant BIT provided protection 'during the investor's investment', while EU law 'guarantees the free movement of capital'.¹⁸⁷ In other words, in the tribunals' view EU law focuses on keeping member state borders open but is less interested in what happens within those borders as long as the member states comply with the principle of non-discrimination and the internal market freedoms.¹⁸⁸ EU investors are free to choose where to invest and choose the form of establishment (primary or secondary) according to their preferences, but post-establishment treatment of intra-EU investments is not similarly regulated under EU law. This is not to say that the internal market is not subject to dense regulation, but as the discussion in section 3.4. pointed out, many claims raised under

¹⁸² Ibid., para. 180. See also *WNC* award, supra note 110 (paras. 298-300) where the tribunal quoted the *Eastern Sugar* and other tribunals with respect to the distinctiveness of BIT arbitration clauses.

¹⁸³ *Oostergetel & Laurentius* award, supra note 109, para. 77.

¹⁸⁴ *Anglia Auto* award, supra note 112, para. 116.

¹⁸⁵ *EURAM* award, supra note 83, para. 180.

¹⁸⁶ *WNC* award, supra note 110, para. 305.

¹⁸⁷ *Eastern Sugar* award, supra note 98, paras. 163-164.

¹⁸⁸ See *WNC* award, supra note 110, para. 305; *Eastern Sugar* award, supra note 98, paras. 161, 163-164; *EURAM* award, supra note 83, paras. 180-182.

intra-EU BITs relate to purely domestic 'misconduct', and the scope and influence of EU law does not always extend to the quotidian practices of member state institutions.

In sum, these differences support the perception that EU law and BITs operate in different ways and at different stages of the life-span of investments, have different subject-matter, and also differ in terms of the 'depth' of the protections they provide. Clearly, if EU law and BITs have different content and foci, and have no formal institutional relationship either, a commonsense corollary is that they are not in conflict either. It is also quite interesting that some of the tribunals confused the issues of subject-matter and treaty conflict,¹⁸⁹ which backs the perception that analyzing the subject-matter of two treaties will influence the analysis of the attendant conflict arguments. As noted, the possibility of arbitration was described as a guarantee against undue interferences by the host state, and the tribunals emphasized that such neutral and effective remedy is not available under EU law or the domestic laws of the member states. Generally speaking, these characterizations create the impression that the tribunals understood BITs as being premised on similar type of considerations as international human rights treaties, with investors largely seen as the underdogs facing the risk of arbitrary behavior on the part of the host state once the investment is made. If human rights treaties strive to affect structural inequalities between individuals and state institutions, BITs strive to counterweigh such inequalities between investors and host states.¹⁹⁰ As Judge Schwebel put it, the ability of the investor to bring direct claims should be seen against the fact that host states have

'many means, legal and not, for bringing pressure to bear upon the foreign investor. The government has not only the police power; it has the police. It can bring the weight of its bureaucracy, and its politicians, to bear. It can prescribe, delay, decree, tax, incite, and strangle.'¹⁹¹

Arbitrators are subject to various background influences which shape their view on the relative weight of different type of arguments. As human rights talk has become ubiquitous, it seems plausible to assume that the larger post-1945 idea concerning the

¹⁸⁹ This is a problem that plagued in particular the analysis of the *Eureko* tribunal. See *Eureko* award, supra note 74, paras. 231-277.

¹⁹⁰ This is the argument of Brower and Schill, although they do not refer expressly to human rights when making it. See Brower and Schill, 'The Legitimacy of International Investment Law', supra note 18, p. 478

¹⁹¹ Stephen M. Schwebel, 'The Overwhelming Merits of Bilateral Investment treaties', 32 *Suffolk Transnational Law Review* (2009), pp. 263-269, at 268.

relationship of the state and the individual has affected the understanding that arbitrators have of BITs, alongside other similar background influences. To argue that investment protection has a link to the ideational continuum whose origins stretch back to the Universal Declaration of Human Rights, if not much further back in time, may be a provocative statement, but the point is that in many situations foreign investors have to operate in an unpredictable political environment where the risk of interference by public authorities is real, and this resembles the situation of individuals facing arbitrary treatment at the hands of state authorities. Likewise, as is the case with a number of human rights courts, the state is invariably the respondent and never the claimant in investment arbitration, and the state's behavior is assessed solely in light of international legal standards as provided by the applicable BIT. Property rights are also an integral part of what is commonly referred to as first-generation human rights, and in many investment arbitrations the claimant has argued either that the host state's actions violated other core human rights such as the right to a fair trial, or constituted a political witch hunt aimed at ousting the investor from the host state. For example, in *Al-Warraq v. Indonesia*, the tribunal's analysis of the claimant's fair and equitable treatment argument 'relied extensively - and almost exclusively' - on international human rights law, in particular on Article 14 of the International Covenant on Civil and Political Rights dealing with the right to a fair trial.¹⁹² In *Biloune v. Ghana* the claimant investor had been detained, held in remand without charge, and later on exiled, whereas in *Mitchell v. Democratic Republic of the Congo* the claimant's business premises were raided, documents were confiscated, and some of his employees imprisoned.¹⁹³

These cases provide support to the argument (or perception) that small- and medium-sized investors 'make up a large part of the claimants in contemporary investment-treaty arbitration'.¹⁹⁴ Many of the arbitrations where conflict arguments were raised also supports this argument as the claimant investors ranged from Mr. Binder, a German national who had formed a Czech company to provide forwarding services, to a Dutch couple who had invested in a Slovak Bank through a public tender offer, and to brothers Busta (UK

¹⁹² See Hesham Talaat M. *Al-Warraq v. The Republic of Indonesia*, UNCITRAL Arbitration, Final Award, 15 December 2014. The quote is from Lorenzo Cotula, 'Human Rights and Investor Obligations in Investor-State Arbitration', 17 *Journal of World Investment & Trade* (2016), pp. 148-157.

¹⁹³ *Biloune and Marine Drive Complex Ltd v. Ghana*, UNCITRAL, Award on Jurisdiction and Liability, 27 October 1989; *Mitchell v. Democratic Republic of the Congo*, ICSID Case No. ARB/99/7, Award, 9 February 2004.

¹⁹⁴ Brower and Schill, 'The Legitimacy of International Investment Law', supra note 18, p. 481.

citizens) who owned a wholesale business of automobile parts and accessories in the Czech Republic. While investing in a foreign country is not equivalent to setting up a small business in one's native country, the argument about small- and medium-sized investors strives to draw a parallel between the rationale of human rights treaties and investment treaties. As Brower and Schill note, BITs are important in particular for small- and medium-sized investors who, unlike large multinationals, lack the 'necessary market strength and bargaining power to negotiate [BIT-]comparable protection mechanisms'.¹⁹⁵ If the human rights movement strives to protect those who lack a basic social and economic safety-net, BITs strive to protect those economic actors who fall to the cracks of local remedies and whose cause their home state refuse to take up in the form of diplomatic protection (a much weaker remedy to begin with).

The human rights analogy and other arguments for investment treaties and arbitration are analyzed in Chapter 6. The following two chapters look at the conflict arguments from the perspective of EU law and strive to answer, inter alia, the following questions: are BIT arbitration clauses compatible with the principle of non-discrimination? Do they breach the autonomy of the EU legal order? What is the relevance of Article 344 TFEU and the ECJ's case law on commercial arbitration in this regard? I also provide some preliminary remarks on how the critical debate could be taken account of in answering these and other relevant questions.

¹⁹⁵ *Idem.*

4. The Principle of Non-Discrimination: Treaty Conflict or an Internal EU Law Problem?

4.1. General Remarks

In June 2015, the Commission started infringement proceedings against five member states because of their refusal to terminate their mutual BITs.¹⁹⁶ The Commission threatened to start similar proceedings against the other member states as well, and in the press release concerning the proceedings, the Commission argued that by conferring 'rights on a bilateral basis to investors from some Member States only', intra-EU BITs lead to nationality-based discrimination which is prohibited under EU law.¹⁹⁷ Conversely, as Chapter 3 discussed, arbitral tribunals have either rejected the discrimination argument or suggested that

¹⁹⁶ These states are Austria, the Netherlands, Romania, Slovakia and Sweden. As regards these proceedings, the only publicly available document is the Commission's letter (see supra note 77) to the Swedish Government and the latter's response, parts of which will be discussed in the following. In September 2016, the Commission informed that it had sent formal requests (i.e. reasoned opinions under Article 258 TFEU) to the five member states, requesting them to terminate their intra-EU BITs. Out of the member states that have concluded a large number of intra-EU BITs, Italy is the only one to have terminated its existing treaties. For background information on this, see Jarrod Hepburn and Luke Eric Peterson, 'Italy is the EU's model citizen, when it comes to following the European Commission demands to terminate intra-EU investment treaties', *IARepporter News*, 2 June 2015. There have been some other notable developments as well. In April 2016, Austria, Finland, France, Germany and the Netherlands issued a Non-Paper, in which they proposed the conclusion of an investment protection agreement between all EU member states, which agreement would replace all pre-existing intra-EU BITs. See 'Intra-EU Investment Treaties. Non-paper from Austria, Finland, France, Germany and the Netherlands', submitted to the Trade Policy Committee, 7 April 2016. However, the proposal has little chance of success, also because a number of member states have expressly stated that they plan to terminate intra-EU BITs. For example, in September 2016, the President of Romania submitted a draft legislation to the Romanian parliament under which Romania's 22 intra-EU BITs are terminated, and in March 2017, the Romanian parliament adopted a bill which 'cancelled' these treaties. It is unclear whether this latter development implies that Romania has sent notifications to the other parties to the effect that Romania wishes to terminate the BITs in accordance with the procedure they outline (or whether it means something else). See Markus Burgstaller and Agnieszka Zarowna, 'Romania to terminate its intra-EU Bilateral Investment Treaties', *Hogan Lovells ARBlog*, 29 September 2016. Available at <http://www.hlarbitrationlaw.com/2016/09/romania-to-terminate-its-intra-eu-bilateral-investment-treaties/> (accessed 14 January 2017). See also 'In-depth: Where we are in the intra-EU BIT saga', *Borderlex news portal*, 5 April 2017. Available at <http://borderlex.eu/in-depth-where-we-are-in-intra-eu-bit-saga/> (accessed 16 May 2017, requires subscription). Likewise, in February 2016, Poland announced that it plans to terminate its intra-EU BITs because it 'has reached a "level of democracy" that guarantees its courts are free from political influence'. See Marta Waldoch and Maciej Onoszko, 'Poland plans to cancel bilateral investment treaties with EU', *Bloomberg Markets*, 26 February 2016. Available at <https://www.bloomberg.com/news/articles/2016-02-25/poland-seeks-to-end-bilateral-investment-deals-with-eu-members> (accessed 14 January 2017). Finally, in 2016 the Czech Republic and Romania made official notifications to Poland in respect of their mutual BITs. As a consequence, the two BITs were terminated with immediate effect and without the application of sunset clauses. See Marcin Orecki, 'Bye-bye BITs? Poland reviews its investment policy', *Kluwer Arbitration Blog*, 31 January 2017. Available at <http://kluwerarbitrationblog.com/2017/01/31/bye-bye-bits-poland-reviews-investment-policy/> (accessed 1 February 2017).

¹⁹⁷ EU Commission press release, 'Commission asks member states to terminate their intra-EU bilateral investment treaties', IP/15/5198, 18 June 2015.

discrimination is remedied by extending BIT rights to all EU investors. The matter is of course more complex than these two general arguments imply.

The first question is what form of discrimination member state BITs bring about - who discriminates against who - and the second what legal consequences flow from a finding of discrimination as a matter of EU law and international law. The discrimination articles in primary EU law are highly general, which means that the case law of the ECJ is central to understanding the scope of the non-discrimination principle and the forms of remedy that may come into play under EU law. What might complicate matters is that the scope and content of the non-discrimination principle varies to an extent from one fundamental freedom to the next, and the findings of the ECJ may only be relevant in relation to a particular freedom or in the specific circumstances of the case. BITs relate to the free movement of capital, freedom of establishment, and freedom to provide services, but it suffices that they fail to pass the discrimination test in relation to just one of these. In other words, when an EU investor has made an investment in another member state, he has utilized the fundamental freedoms and is entitled to equal treatment in that member state. The purpose of the following discussion is to look at the general building blocks of the EU non-discrimination regime and to analyze cases that commentators and arbitral tribunals have invoked in the context of member state BITs.

4.1.1. Primary Law Provisions

Article 18 TFEU stipulates that 'any discrimination on grounds of nationality shall be prohibited'. This general rule is supplemented by a number of provisions in sections dealing with the fundamental freedoms. For example, Article 45(2) TFEU states that freedom of movement for workers 'shall entail the abolition of any discrimination based on nationality between workers of the Member States'. The general prohibition of discrimination extends to all four fundamental freedoms even though some of the relevant TFEU provisions contain no explicit references to the term 'discrimination'.¹⁹⁸ Article 18 TFEU applies when a matter falls within the scope of EU law but there is no specific

¹⁹⁸ By way of an example, Article 63 TFEU, which prohibits restrictions on capital movements and payments, does not refer to discrimination, but non-discrimination nonetheless applies also in this area. See e.g. Steffen Hindelang, *The Free Movement of Capital and Foreign Direct Investment: The Scope of Protection in EU Law* (Oxford University Press, 2009), pp. 115-116; Alexander Honrath, *Umfang und Grenzen der Freiheit des Kapitalverkehrs. Die Möglichkeiten zur Einführung einer Devisenzwangsbewirtschaftung in der Europäischen Union* (Nomos, 1998), p. 64.

discrimination provision in primary law that could be invoked.¹⁹⁹ One could also refer to Articles 20 and 21 of the Fundamental Rights Charter. The former provides that '[e]veryone is equal before the law', whereas Article 21 establishes a more general principle of non-discrimination.²⁰⁰

At the outset, it is useful to note that BITs typically promise national treatment and most-favored nation treatment to the contracting states' investors. When a foreign investor from state B invests in the territory of state A, the latter is obligated to treat the investor in the same manner as its own or any third country investors, and the 'best' available treatment applies. This means, in principle, that third state investors with which the member states have concluded BITs are entitled to the beneficial treatment accorded to nationals and companies of the member states within the internal market. To prevent this, most BITs contain so called Regional Economic Integration Organization (REIO) clauses, which provide that the contracting states are not obliged to grant to investors of the other party 'the benefit of any treatment, preference or privilege by virtue of any existing or future... free trade area, customs union, common market, economic and monetary union or regional economic integration agreement'.²⁰¹ While there is variation in the content of REIO clauses, in most cases they effectively exclude preferential treatment based on EU law from the scope of BITs.²⁰² However, this chapter is not concerned with the non-discrimination rules of BITs, but with the relevant EU law rules and their implications for member state BITs.

To further delimit the scope of the discussion, it is useful to say a few words on the TFEU's freedom of establishment provisions. Article 54 TFEU provides that companies established in accordance with the laws of a member state are to 'be treated in the same way as natural persons who are nationals of' member states. Article 55 TFEU, in turn, provides that member states have to grant the same treatment to nationals of other member

¹⁹⁹ See e.g. *D v Inspecteur*, supra note 167, para. 97 (footnote 52).

²⁰⁰ See also Article 9 TEU under which the EU shall observe, in all its activities, the principle of the equality of its citizens, who shall receive equal attention from its institutions, bodies, offices and agencies'. Finally, equality is also one of the EU's foundational values in accordance with Article 2 TEU.

²⁰¹ See Article 7 of Agreement between the Government of the Hong Kong Special Administrative Region of the People's Republic of China and the Government of the Republic of Finland for the Promotion and Protection of Investments (SopS 18/2014). Available at <http://investmentpolicyhub.unctad.org/Download/TreatyFile/3177> (accessed 24 April 2016).

²⁰² For some examples of REIO clauses, see Anca Radu, 'Foreign Investors in the EU - Which "Best Treatment"? Interactions between Bilateral Investment Treaties and EU Law', 14 *European Law Journal* (2008), pp. 237-260, at 247-249.

states 'as their own nationals as regards participation in the capital of companies or firms within the meaning of Article 54, without prejudice to the application of the other provisions of the Treaties'.²⁰³ These two provisions indicate that EU nationals can take part in the incorporation of a company in another member state, which is called primary establishment, or, alternatively, they can establish branches, agencies or subsidiaries in another member state, which is called secondary establishment. As to third state nationals (companies or individuals), Article 54 TFEU does not distinguish between companies on the basis of nationality of the owners. In other words, the article applies similarly to companies established in a member state, but which are owned by third state nationals. However, both the EU and the member states can provide different treatment to companies owned by nationals of the other member states and third states under specific primary law provisions.²⁰⁴ For example, Article 52 TFEU provides that the articles on freedom of establishment 'shall not prejudice the applicability of provisions...providing for special treatment *for foreign nationals* on grounds of public policy, public security or public health'.²⁰⁵ Similarly, under EU law companies owned or controlled by third country nationals are often expressly excluded from receiving similar treatment as companies owned or controlled by nationals of member states. For example, Article 9 of the Decision No 1718/2006/EC of the European Parliament and of the Council provides that 'enterprises which benefit from the programme shall be owned and shall continue to be owned, whether directly or by majority participation, *by Member States and/or Member State nationals*'.²⁰⁶ Similarly, participation in procedures awarding grants and contracts financed under EU external assistance is limited to companies of member states and companies of a number of other states depending on the type of financing instrument as outlined in Regulation 236/2014.²⁰⁷ Clearly, while EU law sanctions this type of discrimination, these

²⁰³ The company's seat has the same function as nationality does for individuals, and the seat is the state (of incorporation) where the company has its registered office, central administration, or principal place of business. See e.g. Case C-330/91, *Commerzbank AG*, ECLI:EU:C:1993:303, para. 13.

²⁰⁴ See e.g. Articles 51 and 52 TFEU.

²⁰⁵ Emphasis added. Article 51 TFEU also provides that the European Parliament and the Council 'may rule that the freedom of establishment articles 'shall not apply to certain activities'.

²⁰⁶ See Decision No 1718/2006/EC of the European Parliament and of the Council of 15 November 2006 concerning the implementation of a programme of support for the European audiovisual sector (MEDIA 2007), OJ L 327, 24.11.2006, pp. 12-29 (at 17, emphasis added).

²⁰⁷ See Regulation (EU) No 236/2014 of the European Parliament and of the Council of 11 March 2014 laying down common rules and procedures for the implementation of the Union's instruments for financing external action, OJ L 77, 15.3.2014, pp. 95-108 (see esp. Arts 8-11). For other examples, see Ramon Torrent, 'The Contradictory Overlapping of National, EU, Bilateral, and Multilateral Rules on Foreign Direct Investment: Who is Guilty of such a Mess?', 34 *Fordham International Law Journal* (2011), pp. 1377-1399, at 1377-1381; Radu, 'Foreign Investors in the EU', *supra* note 202, at 252-253.

examples have no relevance to the question whether member state BITs breach the principle of non-discrimination as a matter of EU law.

The relevant point is that when a company having its seat in member state B or third state C has established itself in member state A in pursuance of an investment either through primary or secondary establishment, and A has concluded BITs with B and C, the investors of B and C are entitled to treatment, which investors from other member states and third states are not entitled to.²⁰⁸ The national treatment obligation, read literally, requires that member states treat non-national investors on equal terms with domestic investors. To return to the example, since member state A grants BIT rights only to investors and investments originating from member state B and third state C, but not to its domestic investors, the BITs cannot breach the national treatment obligation. However, when investors of B and C have established themselves in member state A through primary establishment, the incorporated company is considered a national of the latter under EU law, while under the BIT it may qualify as an investor of B or C. From this stems the argument that the BITs concluded with B and C discriminate against companies established in member state A, which are effectively owned or controlled by investors of other member states and third states (assuming they have not concluded BITs with A).²⁰⁹ The question is if this latter approach is the 'best' way to bring member state BITs within the scope of the non-discrimination rules or whether the case law of the ECJ could support the argument that member state A has to extend BIT privileges to nationals of other member states and third states established therein on the basis of a most-favored-nation type of obligation.

Generally speaking, the ECJ has held that discrimination takes place 'when two categories of (corporate or natural) persons, whose legal and factual circumstances are not fundamentally different, are treated differently and when situations which are not comparable are treated in the same way'.²¹⁰ The Court has also held that 'similar situations

²⁰⁸ The company's seat has the same function as nationality does for individuals, and the seat is the state (of incorporation) where the company has its registered office, central administration, or principal place of business. See e.g. Case C-330/91, *R v. Inland Revenue Commissioners, ex p. Commerzbank AG*, ECLI:EU:C:1993:303, para. 13.

²⁰⁹ See Dimopoulos, 'The Validity and Applicability of International Investment Agreements', supra note 26, p. 83.

²¹⁰ Case C-431/01, *Philippe Mertens v Belgian State*, ECLI:EU:C:2002:492, para. 32. Other cases where the Court has expressed this general principle include Joined Cases C-27/00 and C-122/00, *Omega Air*, ECLI:EU:C:2002:161, para. 79; Joined Cases C-128/03 and C-129/03, *AEM and AEM Torino*,

shall not be treated differently unless differentiation is objectively justified'.²¹¹ In some of the cases discussed below, the ECJ has analyzed in detail the comparability of two situations, whereas in other cases the comparability of two situations has been assumed, as the parties or the Court have not engaged with the issue. Prima facie, the only distinguishing criterion in terms of enjoyment of BIT rights is the nationality of investors, which is strictly prohibited, but the question of whether the situation of investors established in a member state can be considered comparable in relation to enjoyment of BIT rights will be analyzed below. In terms of presentation, I will first summarize each case and then make some general observations about its relevance for member state BITs, but the more general analysis and conclusions are saved to the end.

4.2. The Case Law

4.2.1. Matteucci, Gottardo and Open Skies

The *Matteucci* case concerned a bilateral treaty in the area of cultural cooperation between Belgium and Germany.²¹² This treaty provided for certain scholarships, the purpose of which was to enable Belgium and German nationals to study in the other contracting state. Nationals of other EU member states resident in either country were not eligible to apply for the scholarships. The claimant was an Italian living and working in Belgium and had applied for a scholarship to carry out vocational training in Berlin but was considered ineligible due to her nationality. In essence, the question before the Court was whether the provisions of the founding treaties and Regulation 1612/68, which dealt with free movement of workers within the EU, made Ms. Matteucci eligible to apply for the scholarships on similar terms as Belgium nationals. Regulation 1612/68 had specified the scope and content of free movement of workers. Article 7(2) stipulated that nationals of member states resident in another member state were to enjoy the same 'social advantages' as nationals of the latter.²¹³ The Court referred to its previous judgment in which grants for vocational training were held as 'social advantages' in the meaning of Article 7(2), which

ECLI:EU:C:2005:224, para. 58; Case C-137/00, *Milk Marque*, ECLI:EU:C:2003:429, para. 126. Hindelang notes that the Court's approach to comparing situations is not consistent. See Hindelang, *The Free Movement of Capital*, supra note 198, p. 149.

²¹¹ Joined Cases 117/76 and 16/77, *Ruckdeschel & Co. and Hansa-Lagerhaus Ströh & Co.*, ECLI:EU:C:1977:160, para. 7.

²¹² Case 235/87, *Matteucci v Communauté Francaise of Belgium*, ECLI:EU:C:1988:460.

²¹³ Regulation (EEC) No 1612/68 of the Council of 15 October 1968 on freedom of movement for workers within the Community, OJ L 257, 19.10.1968, pp. 2-12.

brought the scholarships within the regulation's scope.²¹⁴ The EC had no competences in the area of culture, which prompted the argument that 'the pursuit of legitimate objectives of bilateral cooperation in...[the cultural sphere] may not be frustrated by the development of Community law'.²¹⁵ The ECJ disagreed, noting that the implementation of a cultural agreement between two member states cannot impede the application of EU law and, more specifically, that such agreement may not 'jeopardize the right of Community workers to equal treatment'.²¹⁶ In other words, even though 'culture' was outside the scope of EU law, member states were not authorized to conclude bilateral cultural agreements leading to nationality-based discrimination of EU workers.

There were two other arguments presented to the Court, which are relevant to the following discussion. During the national proceedings Belgian authorities had argued that the Regulation imposes obligations on the host member state (i.e. Belgium) 'only in respect of training provided in its own territory'.²¹⁷ Thus, when the vocational training is carried out in the territory of another member state (i.e. Germany), Article 7 of the Regulation and the principle of equal treatment do not apply in respect Belgium.²¹⁸ Likewise, the fact that the scholarships were awarded by a German authority on the basis of a list of candidates put together by Belgian authorities led to the argument that to impose obligations on Belgium that go beyond the treaty's scope would be unavailing, because German authorities remain bound by the provisions of the treaty and Ms. Matteucci does not qualify for the scholarship under its terms.²¹⁹ In other words, even if Belgium adds Ms. Matteucci to the list of applicants, Germany has no choice but to disregard her application. As to the first argument, the ECJ held that Article 7(2) of the Regulation imposes a general obligation on member states to grant national treatment to workers of other member states established in the territory of another member state. Therefore, when a member state grants its national workers possibility of pursuing vocational training provided in another member state, 'that opportunity must be extended to Community workers established in its territory'.²²⁰ As to the second argument, the Italian government had made the claim that German authorities cannot 'refuse to respect the choice made by' Belgium authorities when

²¹⁴ Case 39/86, *Sylvie Lair v Universitaet Hannover*, [ECLI:EU:C:1988:322, paras. 18-24.

²¹⁵ *Matteucci*, supra note 212, para. 13.

²¹⁶ *Ibid.*, para. 14.

²¹⁷ *Ibid.*, para. 15.

²¹⁸ *Idem.*

²¹⁹ *Ibid.*, para. 17.

²²⁰ *Ibid.*, para. 16.

the latter has listed a non-Belgium applicant pursuant to Regulation 1612/68. Since the Regulation required Belgium to grant the same 'social advantages' to resident EU workers, German authorities 'may not prevent' Belgium 'from fulfilling the obligations imposed on it by Community law'.²²¹ The Court concurred and saw the argument as a manifestation of the principle of sincere cooperation, which requires member states to 'ensure fulfillment of the obligations arising out of the Treaty', even when the bilateral agreement impeding the application of EU law concerned an area falling under the competence of the member states.²²² Further, in such situations member states have 'a duty to facilitate the application' of free movement of workers and to assist each other to that end.²²³ The conclusion was that a 'bilateral agreement which reserves the scholarships in question for nationals of the two Member States which are the parties to the agreement cannot prevent the application of the principle of equality of treatment between national and Community workers established in the territory of one of those two Member States'.²²⁴

This construction allowed the Court to extend the national treatment obligation to cover the situation where a treaty between two member states provides for more favorable treatment of their respective nationals and where the treatment is actually accorded by the other member state (Germany), although the Court attributes the obligation first to Belgium and then to both parties. It seems incorrect to speak of national treatment when the treatment is not accorded by the beneficiary's home state but by the other contracting state under a bilateral treaty based on reciprocity. After all, if both Belgium and Germany had obligated themselves to grant scholarships to their respective nationals, then surely the scholarships given to nationals of Belgium reflect an obligation on the part of Germany to provide such 'treatment' and vice versa. That the Court said that the scholarships flowed from the contracting states' mutual agreement is of course true, but such construction does little

²²¹ Ibid., para. 18.

²²² Ibid., para. 19.

²²³ Idem.

²²⁴ Ibid., para. 23. Weiler discusses an analogous case related to Regulation 1612/68 from the perspective of competences, and notes that the Court held that 'to the extent that national measures, even in areas over which the Community has no competence, conflict with the Community rule, these national measures will be absorbed and subsumed by the Community measure. The Court said that it was not the Community policy that was encroaching on national educational policy; rather, it was the national educational policy that was impinging on Community free-movement policy and thus must give way'. In other words, the EU clearly had the 'original' competence over the establishment of the internal market freedoms, and when domestic legislation or a treaty falling within a field over which the EU has no competences threaten these freedoms, the EU 'competence', which is manifested in primary law provisions and secondary legislation dealing with the fundamental freedoms, takes precedence. See Weiler, 'The Transformation of Europe', supra note 30, pp. 2438-2441. The relevant case is Case 9/74, *Donato Casagrande v Landeshauptstadt München*, ECLI:EU:C:1974:74.

justice to the reciprocal nature of the treaty. This approach creates an artificial façade over the original treaty configuration and creates what is in practical terms a most-favored nation type of obligation, though the invocation of the principles of loyalty and primacy of EU law enabled the Court to construe it as a national treatment issue. Translated into the member state BIT context, *Matteucci* supports the argument that member states have to cooperate to extend *intra-EU BIT* rights to all EU investors. Likewise, though member state A grants such benefits to investors of member state B, under the Court's construction the former also grants them to its own investors in member state B, bringing the benefits within the scope of the national treatment obligation.

The *Gottardo* case dealt with a social security treaty concluded between Italy and Switzerland.²²⁵ While each member state has its own social security laws, the EU has some competences in the area as well.²²⁶ There was secondary legislation dealing with social security treaties, but its applicability to the case was unclear.²²⁷ The Court dodged the argument that the treaty did not become within the scope of Regulation 1408/71,²²⁸ and thus within the scope of EU competence, by relying directly on the principle of equal treatment of EU workers laid down in Article 45 TFEU. It noted that the 'question submitted in the present case is based on application of the principles flowing directly from the provisions of the Treaty',²²⁹ and then held that when member states conclude agreements, whether between themselves or with third states, they have to comply with their obligations under EU law.²³⁰ The social security treaty provided that working periods completed by Italian nationals in Switzerland were taken into account when their entitlement to Italian old-age pension was considered. Mrs. Gottardo was a French national resident in Italy and had worked successively in Italy, Switzerland and France. She applied for an Italian pension but since the periods of insurance completed in Switzerland were not taken into account (the Italy-Swiss treaty did not apply to her) due to her nationality, she did not 'achieve the minimum period of contributions required under Italian legislation for entitlement to an Italian pension'.²³¹ Mrs. Gottardo argued that as a national of a member state resident in Italy she was entitled to a pension under the same conditions as Italian

²²⁵ Case C-55/00, *Elide Gottardo v Istituto Nazionale della Previdenza Sociale*, ECLI:EU:C:2002:16.

²²⁶ See Article 4 and Title X TFEU.

²²⁷ See *Gottardo*, supra note 225, paras. 5-7, 25-29 and 35.

²²⁸ See Regulation (EEC) No 1408/71 of the Council of 14 June 1971 on the application of social security schemes to employed persons and their families moving within the Community, OJ L 149, 5.7.1971.

²²⁹ *Gottardo*, supra note 225, para. 29.

²³⁰ *Ibid.*, para. 33.

²³¹ *Ibid.*, para. 16.

nationals and that the periods of insurance completed in Switzerland had to be taken into account by Italian authorities.²³²

The ECJ agreed and noted that Mrs. Gottardo was treated differently than Italian nationals on the sole ground of nationality and in contrast to *Matteucci* the Court relied, as noted, solely on Article 45 TFEU to find that the treatment of Mrs. Gottardo violated the principle of national treatment.²³³ Another difference with *Matteucci* was that the relevant treaty was concluded between a member state and a third country, which prompted the ECJ to consider the argument that the unilateral extension of the benefit to nationals of other member states by Italy could affect the rights and obligations of Switzerland under the treaty, which implied that Switzerland's consent might be necessary for the extension to take effect. However, the Court held that such unilateral extension created no problems in this regard as it would not compromise the rights of nor impose any new obligations on Switzerland.²³⁴

Though the treatment stemmed from a bilateral treaty, it was less artificial to attribute it to Italy as Italian authorities granted that treatment to Italian nationals, even though this, presumably, hinged on a reciprocal treatment of Swiss nationals in Switzerland. Likewise, and similarly to *Matteucci*, the judgment did affect the original balance of the treaty (e.g. by increasing Italy's fiscal burden), but the Court held that such consequences 'cannot justify the Italian Republic's failure to comply with its Treaty obligations',²³⁵ also because the extension of the benefits to nationals of other member states did not affect the rights and obligations of Switzerland. In *Gottardo*, the Court did not dwell on the specifics of the question of competence, but relied directly on the free movement of workers provisions to bring the treaty within the scope of community law. Like *Gottardo*, intra-EU BITs concern an area of shared competence, and the treaties clearly come within the scope of the fundamental freedoms, even if no relevant secondary legislation exists.²³⁶ Whether *Gottardo* and *Matteucci* imply that BIT rights granted to third state investors in extra-EU BITs have to be extended to all EU investors was discussed in an analogous manner in the *Open Skies* cases, to which I now return.

²³² Ibid., para. 18.

²³³ Ibid., para. 24.

²³⁴ Ibid., para. 36.

²³⁵ Ibid., para. 38.

²³⁶ Another question is whether the specific division of powers between the EU and member states in an area of shared competence could in some cases render a different conclusion.

The *Open Skies* cases dealt with a number of bilateral air transport agreements between the US and eight member states.²³⁷ The agreements provided that only carriers whose substantial ownership or effective control was in the hands of the member states or their nationals were eligible to acquire operating licenses from US authorities. The ECJ held that such clauses discriminated against EU carriers established in the eight member states but substantially owned or effectively controlled by nationals of other member states.²³⁸ As to the question of competence, the Court found that at least in relation to some of the provisions of the *Open Skies* treaties an external exclusive competence existed on the basis of specific secondary law acts, but the finding of discrimination appeared to stem, analogously to *Gottardo*, directly from primary law provisions on the freedom of establishment.²³⁹ As in *Gottardo*, the respondent governments claimed that the rights and obligations of the *Open Skies* treaties were based on reciprocity, and the air traffic rights granted by US authorities could not be extended to other EU carriers.²⁴⁰ More specifically, since US carriers could obtain operating licenses only in the member states with which the *Open Skies* agreements had been concluded, the extension of the beneficial treatment by the US to nationals of other member states would upset the balance of the treaty and the principle of reciprocity in particular. Another argument was that the alleged discrimination was attributable to the US, and not to the eight member states, since US authorities had exclusive jurisdiction to take decisions on the US operating licenses.²⁴¹

The ECJ rejected both arguments. As to the issue of reciprocity, the Court held that the freedom of establishment is unconditional and member states cannot maintain conflicting obligations, whatever their source.²⁴² Likewise, discrimination did not originate in the decisions of US authorities but in the treaty provision on the ownership and control of carriers, which enabled them to take such decisions.²⁴³ As in *Matteucci*, the Court held that while the preferential treatment flowed from the ownership and control clauses, whose enforcement was in the hands of the US, that treatment was nonetheless accorded by the eight member states to their own nationals, bringing it within the purview of the freedom

²³⁷ See e.g. Case C-467/98, *Commission v. Denmark (Open Skies)*, ECLI:EU:C:2002:625.

²³⁸ *Ibid.*, paras. 131-132.

²³⁹ *Ibid.*, paras. 111-113. For an illuminating discussion on the complexity of the question of competence in the *Open Skies* cases, Klabbers, *Treaty Conflict and the European Union*, supra note 22, paras. 186-188.

²⁴⁰ *Open Skies*, supra note 237, para. 119.

²⁴¹ *Ibid.*, para. 120.

²⁴² *Ibid.*, para. 134.

²⁴³ *Ibid.*, para. 132.

of establishment rules.²⁴⁴ In contrast to *Matteucci*, but similarly to *Gottardo*, the *Open Skies* agreements were concluded with a third state so the Court could not invoke the principle of sincere cooperation nor rely on the primacy of EU law. Contra *Gottardo*, the unilateral extension of the treatment to all EU carriers by the concerned member states was not possible as its enforcement would have affected the rights and obligations of the US and required its acceptance and input. Thus, the Court merely held that the freedom of establishment had been violated and left it to the EU Commission and the concerned member states and the US to take necessary action.²⁴⁵ As in *Matteucci*, an obligation normally attributable to the 'host' state was attributed to the 'home' state, which enabled the invocation of the national treatment obligation.

If member state BITs are discriminatory as a matter of EU law, then *Open Skies* is relevant to the extent that it introduces similar principles as *Matteucci* to the area of freedom of establishment: when a member state negotiates benefits for its own nationals in another state (whether in another member state as in *Matteucci* or in a third country as in *Open Skies*), those benefits are 'attributable' to the former even if it is only the latter that can effectuate them. In relation to extra-EU BITs, it is clear that member states cannot unilaterally extend BIT rights to other EU investors established in third states with which they have concluded BITs. The only option would be to engage in negotiations with the concerned third states. On the other hand, member states can extend BIT rights granted to third state investors under extra-EU BITs to *EU investors* established in their territories, as this has no impact on the rights and obligations of the third states in question. However, *Open Skies* suggests that this would not eliminate the problem of discrimination, because member states would still provide better treatment to their own nationals in the third states with which they have concluded BITs. *Gottardo*, *Matteucci* and *Open Skies* also demonstrate that although the circumstances of companies and individuals are not always comparable, similar non-discrimination principles may apply across the four freedoms.

4.2.2. The Tax Cases

Arbitral tribunals and commentators have also referred to a number of cases dealing with double taxation treaties in their analysis of the question of discrimination. Generally

²⁴⁴ *Ibid.*, paras. 128-131.

²⁴⁵ The *Open Skies* treaties were not denounced, but the EU Commission was granted a negotiating mandate, which resulted in the signing of the EU-US Air Transport Agreement in 2007. See Panos Koutrakos, *EU International Relations Law* (Hart Publishing, 2nd ed. 2015), pp. 342-343.

speaking, direct taxation remains within the competence of the member states, although the EU has adopted a number of directives in the area of direct taxation. As to double taxation, with the exception of a single convention of limited relevance,²⁴⁶ the EU has not adopted any harmonizing measures for the elimination of double taxation. Article 293 of the Treaty Establishing the European Communities encouraged member states to conclude double taxation treaties, but the Lisbon Treaty repealed that provision. Yet such treaties remain crucially important, as the threat of double taxation creates a strong disincentive for the utilization of the internal market freedoms. Hence, member states are free to conclude double taxation treaties, and this includes the power to determine the criteria for the allocation of fiscal jurisdiction as between them.²⁴⁷ The qualification is that these 'direct taxation powers have to be exercised consistently with Community law'²⁴⁸ and any 'discrimination by reason of nationality'²⁴⁹ is strictly prohibited. Taxation cases involving varied cross-border situations are very complex and their relevance to non-tax situations is not always clear, also because the question of comparability of the situation of national and resident taxpayers on the one hand, and resident and non-resident taxpayers on the other hand is more complex than the question of comparability in the above three cases. I will limit the discussion to those aspects of the cases that are relevant for present purposes.

The *EURAM* tribunal invoked the hotly debated *D v Inspecteur* case concerning the relationship of EU non-discrimination rules and double taxation treaties.²⁵⁰ Relying on the ECJ's findings in that case, the *EURAM* tribunal claimed that EU investors established in a member state, but not entitled to protections under an intra-EU BIT concluded by that member state, are not in a comparable situation to EU investors protected by an intra-EU BIT and no discrimination takes place.²⁵¹ This analogy requires critical analysis. *D v Inspecteur* concerned a Dutch wealth tax allowance granted to non-resident Belgian nationals (owning property in the Netherlands) under the Dutch-Belgium tax treaty. Dutch

²⁴⁶ This is the Convention on the elimination of double taxation in connection with the adjustment of profits of associated enterprises of 23 July 1990, OJ 1990, L 225, 20.8.1990, p. 10.

²⁴⁷ See e.g. Case C-336/96, *Gilly v. Directeur des Services Fiscaux du Bas-Rhin*, ECLI:EU:C:1998:221, para. 30.

²⁴⁸ Case C-264/96, *Imperial Chemical Industries v. Kenneth Hall Colmer*, ECLI:EU:C:1998:370, para. 19 and cases cited therein.

²⁴⁹ Case C-80/94, *Wielockx*, ECLI:EU:C:1995:271, para. 16. Article 293 of the EC Treaty authorized member states to 'enter into negotiations with each other with a view to securing for the benefit of their nationals...the abolition of double taxation within the Community.' This Article was repealed from the Lisbon Treaty.

²⁵⁰ *D v Inspecteur*, supra note 167.

²⁵¹ See *EURAM* award, supra note 83, paras. 273-278.

tax legislation granted the allowance to non-residents if at least ninety percent of their assets were located in the Netherlands, but in the tax treaty the allowance was granted to all Belgians regardless of the percentage of their Dutch assets. The claimant was a German national not entitled to the allowance under Dutch law as his Dutch assets amounted to just ten percent of his combined assets. Mr. D argued that the refusal to grant the allowance to him constituted discrimination on the ground of nationality in respect of the provisions on the free movement of capital. The essential question was whether Mr. D and Belgians owning property in the Netherlands were in a comparable situation, both being non-residents for the purposes of Dutch taxation and liable to similar wealth tax apart from the allowance.

Against the suggestions of Advocate General Ruiz-Jarabo, the Court held that Belgian and German non-residents having assets in the Netherlands were not in a comparable situation for the purposes of the tax allowance. Hence, the extension of the allowance to Mr. D was not called for. To understand the Court's reasoning, the underlying framework of double taxation treaties requires elaboration. As noted, member states remain masters of direct taxation and may determine the connecting factors for the allocation of tax jurisdiction in double taxation treaties on various types of income. When such treaties are negotiated, the fiscal equilibrium established will reflect the specific features of national tax systems as well as the varied macroeconomic and political circumstances of the contracting states. Likewise, and for similar reasons, the balance of each double taxation treaty as regards the allocation of fiscal jurisdiction and the contents of priority of taxation rules will be different.²⁵² This backdrop explains the Court's holding that it is an 'inherent consequence' of bilateral double taxation treaties that the 'reciprocal rights and obligations' established in them 'apply only to persons resident in one of the two Contracting Member States',²⁵³ and the corollary that the wealth tax allowance 'cannot be regarded as a benefit separable from the remainder of the Convention, but is an integral part thereof and contributes to its overall balance'.²⁵⁴ From the same premise stemmed also the finding that 'a taxable person resident in Belgium is not in the same situation as a taxable person outside Belgium so far as concerns wealth tax on real property in the Netherlands'.²⁵⁵

²⁵² On this background, see Case C-374/04, Opinion of Advocate General Geelhoed, *Test Claimants in Class IV of the ACT Group Litigation v Commissioners of Inland Revenue*, ECLI:EU:C:2006:139, paras. 94-95.

²⁵³ *D v Inspecteur*, supra note 167, para. 61.

²⁵⁴ *Ibid.*, para. 62.

²⁵⁵ *Ibid.*, para. 61.

In other words, in the absence of harmonizing taxation measures, EU law does not, as a rule, impose an obligation on the member states to harmonize the treatment of non-resident taxpayers, as this would encroach upon their competence to conclude double taxation treaties, which, by their very nature, entail disparities with respect to the treatment of non-resident taxpayers.²⁵⁶ As this thesis was about to go to press, Advocate General Wathael gave his opinion in the *Achmea* case.²⁵⁷ Similarly to the *EURAM* tribunal, he held that the Court's findings in *D v Inspecteur* apply, by analogy, in the intra-EU BIT context. In his view, 'that the reciprocal rights and obligations created by the [Dutch-Slovak] BIT apply only to investors from one of the two Contracting Member States is a consequence inherent in the bilateral nature of BITs', and from this followed the finding 'that a non-Netherlands investor is not in the same situation as a Netherlands investor so far as an investment made in Slovakia is concerned'.²⁵⁸ Further, just as the wealth tax allowance in *D v. Inspecteur*, the arbitration clause is 'not a benefit separable from the remainder of the BIT, but is an integral part thereof to such an extent that a BIT without an ISDS mechanism would be pointless since it would not achieve its aim, which is to encourage and attract foreign investment'.²⁵⁹ Wathael also supported the analogy by pointing to how double taxation treaties and BITs 'are aimed at the same economic activities, both the entry and the exit of capital', and that member states 'may attract the entry of foreign capital to its territory by affording a high level of legal protection to the investment in the context of a BIT and also by granting tax advantages'. Finally, he argued that similarly to double

²⁵⁶ Advocate General Ruiz-Jarabo had argued that the broader framework of double taxation treaties was not relevant because there was no wealth tax in Belgium and granting the allowance was thus not based on reciprocity, but was a mere privilege having no connection to the elimination of double taxation. In other words, the equilibrium and balance established in the Dutch-Belgium tax treaty was not a relevant argument in respect of the allowance, and Mr. D was clearly in a comparable situation with Belgians entitled to the allowance in all other respects. Advocate General Ruiz-Jarabo went even further and held that the principle of equal treatment 'is independent from the principle of reciprocity [with respect to double taxation treaties] and therefore, in the event of a conflict, it takes precedence over mutual commitments [established in double taxation treaties]'. See Case C-376/03, *D v Inspecteur van de Belastingdienst/Particulieren/Ondernemingen buitenland te Heerlen*, Opinion of Advocate General Ruiz-Jarabo, ECLI:EU:C:2004:663, paras. 72-106 (the quote is from para. 101).

²⁵⁷ Unfortunately, and apart from these remarks on discrimination, I did not have time to incorporate the opinion in the thesis. It is noteworthy that as a preliminary point, the Advocate General noted that the Dutch-Slovakia BIT's arbitration clause does not 'come within the scope *ratione materiae* of either freedom of establishment, of free movement of capital, or any other [TFEU] provision..., since EU law does not create remedies that allow individuals to take proceedings against the Member States before the Court'. In light of the above cases, this is a clear misunderstanding. While the EU has not adopted legislation akin to investment protection *vis-à-vis* intra-EU investments, *Matteucci* leaves no doubt that treaties concluded between two member states have to respect the fundamental freedoms and the principle of equal treatment, and in this way they come within the scope of EU law. Case C-284/16, *Achmea*, Opinion of Advocate General Wathael, ECLI:EU:C:2017:699, para. 56.

²⁵⁸ *Ibid.*, para. 75.

²⁵⁹ *Ibid.*, para. 76.

taxation treaties, 'the reciprocity of the commitments given by the Member States is an essential ingredient of BITs'.²⁶⁰

These comments of course assume that the purpose and contents of double taxation treaties are similar to investment treaties. Generally speaking, one could argue that double taxation treaties do not grant benefits (as BITs do), but create a web of taxation rules that allocate fiscal jurisdiction between the contracting states over different types of income. Likewise, domestic laws determine which tax breaks companies and individuals are entitled to and double taxation treaties simply lay out rules on which domestic law applies in a given scenario. Investment treaties, on the other hand, provide a prospective remedy for investors which allows them to challenge domestic policy measures before an arbitral tribunal. Each treaty may have an underlying equilibrium, but the equilibriums of double taxation treaties and BITs are clearly different. Moreover, had the Court decided that Mr. D was entitled to enjoy the allowance under the double taxation treaty, this would have created a most-favored nation obligation in the area of direct taxation and allowed individuals and corporations to demand that they are entitled to treatment under a member state's double taxation treaty that is most favorable to them. In other words, as each member state has concluded a double taxation treaty with all the other member states, a most-favored nation obligation would effectively 'destroy' the respective equilibriums of the treaties. In *Gottardo* and *Matteucci* the purpose of the relevant treaties could not justify the different treatment, and in the latter the Court held that Italy could not justify the different treatment on the ground that it affected the original balance of the relevant treaty. Similarly, in *Matteucci*, for example, the treaty between Germany and Belgium was based on reciprocal rights and obligations, but this had no impact on the Court's finding on discrimination. Arguably, these two cases, or the *Open Skies* cases, could just as well be applied, by analogy, in the intra-EU BIT context.

Wathelet also argued that there is no most-favored nation obligation under EU law, which supported his conclusion that by granting BIT rights only to Dutch investors, the Slovak Republic did not discriminate investors from *other* member states. In other words, EU law only requires that EU investors receive *national treatment* instead of treatment granted to nationals of other member states. Again, however, *Matteucci* and *Open Skies* suggest that

²⁶⁰ Ibid., para. 79.

by concluding the BIT, the Netherlands is granting its investors BIT treatment in the Slovak Republic and vice versa, which implies that they are breaching the national treatment obligation. Similarly, *D v Inspecteur* implies that EU law does recognize a most-favored nation obligation: if and when two companies are in a comparable situation, they have to be treated equally, and this extends to benefits granted in a treaty between two member states. This would also mean that it would be unnecessary to rely on the Court's construction in *Matteucci* and *Open Skies* where it transformed the most-favored nation treatment obligation into a national treatment obligation. Hence, arguably, Wathelet's reasoning is not entirely convincing as it ignores the Court's principal findings in the other relevant cases and fails to take into account the political context of *D v Inspecteur*. He also argued that a finding of discrimination would allow all EU investors to rely on intra-EU BITs by noting that the arbitration clause is 'not a benefit separable from the remainder of the BIT, but is an integral part thereof to such an extent that a BIT without an ISDS mechanism would be pointless since it would not achieve its aim, which is to encourage and attract foreign investment'. However, a finding of discrimination does not necessarily mean that the privileged treatment would need to be extended to all EU investors. The Court could simply declare that the treaties constitute discrimination without laying out what steps the member states should take so as to eliminate the incompatibility.

There is another aspect to *D v Inspecteur* case that should be pointed out. In tax cases the distinction between resident and non-resident taxpayers is often decisive in terms of case outcomes. The term 'resident' refers both to nationals living in their state of origin as well as to non-nationals living and working in that same state. Mr. D had also claimed that even in the absence of the Dutch-Belgium tax treaty the wealth tax allowance had to be extended to him as he was entitled to similar treatment (i.e. national treatment) as Dutch nationals and nationals of other member states resident in the Netherlands. In other words, the argument was that non-resident and resident property owners were in a comparable situation. The Court again disagreed and held that Mr. D was not in a similar situation to Dutch property owners. In doing so, the Court relied on the *Schumacker* doctrine, which holds that in the area of personal income tax the situation of resident and non-resident taxpayers is not, as a rule, comparable.²⁶¹ The rationale is that when the major part of the income or assets of non-residents is concentrated in their state of residence, it is the state of

²⁶¹ Case C-279/93, *Roland Schumacker*, ECLI:EU:C:1995:31, para. 31.

residence which in the best position to 'assess the taxpayer's overall ability to pay, taking account of his personal and family circumstances',²⁶² which includes the granting of tax allowances. Conversely, in situations where non-residents receive the bulk of their taxable income from the state of employment, or when the bulk of their assets are located in another state, the state of residence 'is not in a position to grant...[them] the benefits resulting from the taking into account of...[their] personal and family circumstances'.²⁶³ In such circumstances there is no objective difference between residents and non-residents justifying their different treatment in relation to available tax benefits. As the property that Mr. D owned in the Netherlands formed just ten percent of his overall assets, the *Schumacker* doctrine applied and his situation was not comparable to Dutch property owners.²⁶⁴

In contrast, in *Gottardo* and *Matteucci* the claimants were residents (though non-nationals) of the state from which they sought national treatment and they were entitled to that treatment even though its source was a bilateral treaty. In other words, the claimants were entitled to similar treatment as nationals because their lives were 'concentrated' in their state of residence, whereas Mr. D's personal and economic interests were centered on Germany. The question that arises is not whether the distinction between resident and non-resident taxpayers is transposable to the area of corporate taxation (it is) but whether the principle established in *D v Inspecteur* regarding the non-comparability of the situation of resident and non-resident individual taxpayers could be transposable to the situation of resident and non-resident companies and to non-tax situations more generally. Generally speaking, whether an investor opts for primary or secondary establishment is irrelevant to the question of whether his investment qualifies for protection under a BIT as the matter is resolved through other criteria.²⁶⁵ In both cases the investor's 'interests' may or may not be centered in another state than the host state, but as this distinction has no impact on the ability of investors to invoke a BIT, it cannot be used to make the argument that the

²⁶² *Idem*.

²⁶³ *Ibid.*, para. 29, 32-33, 37.

²⁶⁴ Again, Advocate General Ruiz-Jarabo had a different view. He noted that the value of the assets of resident taxpayers and Mr. D was calculated similarly; as Mr. D was not liable to wealth tax in Germany for his German assets, his situation was identical with a Dutch resident taxpayer whose assets were similarly divided between Germany and the Netherlands; Germany could not take account of Mr. D's personal circumstances with respect to his ability to pay wealth tax, since there was no wealth tax in Germany. Thus, for AG Ruiz-Jarabo, it was clear that Mr. D was in a comparable situation to Dutch resident taxpayers and entitled to the allowance. See *D v Inspecteur*, Opinion of Advocate General Ruiz-Jarabo, *supra* note 256, paras. 61-71.

²⁶⁵ The distinction between portfolio and direct investments might be of some relevance in this context.

situation of investors who enjoy BIT protections and those who do not is non-comparable. In other words, both resident and non-resident investors can rely on BITs if they meet the other relevant criteria.

The *Test Claimants* case is the second tax case raised in literature and it concerned a number of double taxation treaties concluded between the United Kingdom and other member states/third countries.²⁶⁶ Only some of these treaties granted a tax credit on dividends paid by UK companies to companies of the other contracting state. The question was if this different treatment of non-resident companies constituted prohibited discrimination in relation to the freedom of establishment and free movement of capital, that is to say, whether those provisions required that such treatment is extended to all EU companies receiving dividends from UK companies. Analogously to *D v Inspecteur*, the Court analyzed whether the 'non-resident companies concerned are in an objectively comparable situation',²⁶⁷ and its reasoning and conclusions were fundamentally similar. The tax credit was granted only in treaties where the dividends were liable to tax in the UK, but not in treaties where the dividends were not subject to a UK tax.²⁶⁸ Further, the UK tax rate varied (in particular) according to whether the tax treaty provided for a full or partial tax credit. Thus, there was a 'direct link' between the tax credit and the taxation of dividends by the UK; in other words, the tax credit was not granted when the treaties did not make the dividends liable to tax in the UK.²⁶⁹ Put differently, the balance of each double taxation treaty was different and reflected different ways of eliminating double taxation through different priority of taxation rules.

After this, the Court repeated its findings in the *D v Inspecteur* case. The tax credit could not be 'regarded as a benefit separable' from the other provisions of the tax treaties as it was 'an integral part' of the treaties and contributed 'to their overall balance'; second, the fact that the reciprocal rights and obligations, of which the tax credit was just one part, apply only to persons resident in the contracting member states 'is an inherent consequence of bilateral double taxation conventions'; and finally, a company resident in a member state which has a double taxation treaty with the UK not providing for the tax credit *is not in a*

²⁶⁶ Case C-374/04, *Test Claimants in Class IV of the ACT Group Litigation v Commissioners of Inland Revenue*, ECLI:EU:C:2006:773.

²⁶⁷ *Ibid.*, para. 83.

²⁶⁸ *Ibid.*, para. 85.

²⁶⁹ *Ibid.*, para. 87.

similar situation to a company resident in another member state which has a double taxation treaty with the UK providing for the tax credit.²⁷⁰ As in *D v Inspecteur*, the non-comparability of the situation of non-resident companies stemmed from the special characteristics of double taxation treaties, which implies that both cases are unfit for use in non-tax situations.

Finally, *Saint-Gobain* concerned double-taxation treaties concluded by Germany with the Switzerland and the US respectively.²⁷¹ Under the treaties, German resident companies were exempted from paying tax on dividends received from Swiss and US companies. Non-resident companies of other member states receiving such dividends through German branches or permanent establishments were not entitled to the exemption, placing them in a less favorable position in comparison to resident companies. The *Finanzgericht* of Cologne asked the ECJ if it is compatible with the freedom of establishment to not accord the exemption to the permanent establishment of Saint-Gobain (a French company) situated in Germany.²⁷² If the two previous cases necessitated a comparison between the situations of non-residents, then *Saint-Gobain* required comparing the situation of resident and non-resident companies. The Court held that resident German companies and non-resident companies having a permanent establishment in Germany were in objectively comparable situations because both were liable to tax in Germany in respect of the relevant shareholdings and dividends.²⁷³ The circumstances to be taken into account in the comparability assessment were thus limited to the national tax rules that applied to both resident and non-resident companies, which is quite different approach when compared with the circumstances taken account of in *D v Inspecteur*.

The Court's finding was similar to *Commission v France* where it had held that the non-granting of certain tax benefits to French branches and agencies of companies whose seat was in another member state was discriminatory, because, apart from the benefits in question, those branches and agencies were placed on the same footing with resident companies for taxation purposes.²⁷⁴ The Court had also noted in that case that the national treatment obligation cannot be made 'subject to the contents of...[a double taxation]

²⁷⁰ Ibid., paras. 88, 91-92.

²⁷¹ Case C-307/97, *Compagnie de Saint-Gobain v Finanzamt Aachen-Innenstadt*, ECLI:EU:C:1999:438.

²⁷² Ibid., para. 32.

²⁷³ Ibid., paras. 48-49.

²⁷⁴ Case 270/83, *Commission v. France*, ECLI:EU:C:1986:37, para. 20.

agreement concluded with another member state', nor subject to 'a condition of reciprocity imposed for the purpose of obtaining advantages in other member states'.²⁷⁵ In other words, and in more general terms, if resident and non-resident companies are subjected to similar tax treatment in a member state, then that national treatment has to be extended to any and all tax privileges granted to resident companies, and the integrity and balance of double taxation treaties cannot preclude the extension of the benefits to non-resident companies as well. The Court's approach in *Saint-Gobain* was analogous to *Gottardo*, as in both cases the treatment was provided by the home state and not by the other contracting state as in *Matteucci* and *Open Skies*.

In *Saint-Gobain*, the argument was presented that if the tax exemption is extended to companies established in member states not parties to the double taxation treaties, the inherent balance of such treaties is upset. The Court held, as it had in *Gottardo*, that the 'balance and reciprocity' of the treaties would not be affected by a unilateral extension of the exemption by Germany, 'since such an extension would not in any way affect the rights of the non-member countries [i.e. Switzerland and the US] which are parties to the treaties and would not impose any new obligation[s] on them'.²⁷⁶ Conversely, one can extrapolate that in case of intra-EU treaties such extension is required (at least in circumstances similar to *Saint-Gobain*) even if it disturbs the balance of the treaty and imposes new obligations on the other contracting party; as the Court noted in *Matteucci*, the principle of sincere cooperation and the primacy of EU law require that the contracting member states cooperate so as to provide national treatment to all EU nationals established in their territories. In relation to third country treaties the situation is different and member states would have to engage in negotiations with the third state to eradicate the discriminatory treatment, as was the case in the *Open Skies* cases, unless the discrimination can be eliminated by the member state without affecting the rights and obligations of the third country, as was the situation in *Saint-Gobain*.

Before proceeding to analyze the implications of these cases for member state BITs, it is useful to repeat why the argument about the integrity of the fiscal equilibrium of double taxation treaties was decisive in *D v Inspecteur* and *Test Claimants* but not in *Saint-Gobain*. In the former cases, it was the different treatment of non-residents of two or more

²⁷⁵ Ibid., para. 26.

²⁷⁶ *Saint-Gobain*, supra note 271, para. 60.

member states by another member state that was the crux of the matter, whereas *Saint-Gobain* centered on the different treatment of resident and non-resident companies, which the Court found to be in a comparable situation. Further, national treatment arguments were raised also in *D v Inspecteur* and *Test Claimants*, and in the former national treatment was denied, because Mr. D was not in a similar situation to resident taxpayers. Though *Test Claimants* was a more complex case in this regard, there was no difference in the treatment of resident and non-resident companies in respect of the relevant dividends under UK tax law. Though direct taxation falls within the competence of the member states, the national treatment obligation applies in that area as well and cannot be made subject to the contents of double taxation treaties. Whatever the source from which national treatment flows, it has to be extended to non-residents if the latter are in a comparable situation to resident taxpayers. In sum, and arguably, the justifications for double taxation treaties are confined to the area of direct taxation.²⁷⁷ If double taxation treaties take account of a number of fiscal variables to establish an acceptable equilibrium as between the contracting states, the *raison d'être* of intra-EU BITs related to the *general* perception that investors from the old member states needed additional protection against the whims of domestic politics in the formerly socialist member states, which were unfamiliar with the economic, political and legal corollaries of the rule of law. Whether that perception holds true is discussed in Chapter 6.

4.3. Implications of the Cases for the Question of Discrimination in the Context of Member State BITs

Commentators have read the above cases in different ways. Tietje refers to *D v Inspecteur* and *Test Claimants* and argues that these constituted an outright rejection of any most-favored nation obligation under EU law.²⁷⁸ Similarly, Dimopoulos makes the following conclusion on the basis of *D v Inspecteur* and *Test Claimants*: 'the different treatment provided by one Member State to nationals of other Member States as a result of the bilateral nature of intra-EU BITs is compatible with the principle of non-discrimination

²⁷⁷ Cf. Juliane Kokott and Christoph Sobotta, 'Investment Arbitration and EU Law', 18 *Cambridge Yearbook of European Legal Studies* (2016), pp. 3-19, p. 9 (arguing that the ECJ has 'decided that the benefits of these conventions [i.e. double taxation treaties] don't need to be extended to persons from other Member States. In particular, specific rules on the allocation of taxation powers cannot be regarded as a benefit separable from the remainder of the convention. They are integral parts thereof and contribute to their overall balance. In principle, a similar reasoning could be applied to BITs between Member States. Their specific benefits form part of an overall balance and therefore cannot be granted separately.').

²⁷⁸ Tietje, 'Bilateral Investment Protection Treaties between EU Member States', *supra* note 17, pp. 16-17.

under EU law and does not affect the validity or applicability of intra-EU BITs.²⁷⁹

Wehland also reads the cases similarly and finds that 'the fact that BITs grant advantages only to investors from selected Member States would not appear to be incompatible with EC law'.²⁸⁰ Conversely, Eilmansberger invokes *Gottardo* and *Saint-Gobain*, though both cases only dealt with national treatment, to make the sweeping statement that 'preferential treatment not only of own nationals but also of nationals of other Member States or third countries constitutes forbidden discrimination of other EU nationals'.²⁸¹

These statements gloss over important distinctions. *Gottardo* and *Saint-Gobain* were most clearly about national treatment, as the relevant treatment could have been accorded to the nationals of the member states in question even in the absence of the treaties. In *Matteucci* and *Open Skies*, the treatment was based on reciprocity and put into practice by the authorities of the other contracting state. However, the ECJ still held that the cases were about national treatment, as it attributed that treatment, in essence, to both contracting states. In *D v Inspecteur* and *Test Claimants* the tax benefits related to national treatment, but the relevant parts of the cases centered not on national treatment but on treatment granted in double taxation treaties to nationals of the other contracting state (but not to nationals of other member states which led to the MFN argument). That the ECJ did not require the extension of the tax benefits to nationals of other member states was not based on the non-existence of a most-favored nation obligation under EU law (as Dimopoulos and Tietje claim), but hinged on the finding that residents and non-residents were not in a comparable situations vis-à-vis the benefits in question, which, in turn, was premised on the special nature of double taxation treaties and the absence of EU legislation (and competence) in the area of direct taxation. In neither case did the Court address the issue of most-favored nation treatment head on.

Perhaps it is useful to remind who is entitled to treatment flowing from a typical BIT. By way of example, Article 1(3) of the Finland-Bulgaria BIT holds that any natural person who is a national of either contracting state and any company incorporated in accordance with the laws of either contracting state and having its seat in the territory of the same

²⁷⁹ See Dimopoulos, 'The Validity and Applicability of International Investment Agreements', supra note 26, pp. 81-82.

²⁸⁰ Hanno Wehland, 'Intra-EU Investment Agreements and Arbitration: Is European Community Law an Obstacle?', 58 *International and Comparative Law Quarterly* (2009), pp. 297-320, at 317.

²⁸¹ Eilmansberger, 'Bilateral Investment Treaties and EU Law', supra note 26, p. 402.

contracting state qualify as investors under the treaty and receive protection in respect of investments made in the territory of the other contracting state.²⁸² If this definition is viewed from the perspective of Bulgaria,²⁸³ it is evident that investments made by investors of other member states than Finland, whether through a company incorporated in Bulgaria (but owned by nationals of other member states) or through secondary establishment, are not protected under the BIT. Leaving aside the fact that Bulgaria is party to a number of other intra-EU BITs, it is clear that the exclusion of other EU investors from the scope of BIT treatment places them in a less favorable position, as they cannot resort to arbitration to challenge Bulgarian measures affecting their investment. The same general observation applies in relation to other intra-EU BITs, although the scope of protected investors and investments vary to some extent from one treaty to the next.²⁸⁴ In this way, it would appear that intra-EU BITs discriminate between EU investors, both in relation to the freedom of establishment (some EU companies are treated more favorably than others) and free movement of capital (some EU capital movements are treated more favorably than others). To substantiate the argument that BIT *protection standards* constitute more favorable treatment than EU law treatment standards would require some effort, but the possibility to have recourse to arbitration clearly constitutes more favorable treatment.²⁸⁵ I will now look more closely into the above cases to see if they support this general finding of discrimination in relation to intra-EU and extra-EU BITs, after which I look at whether valid counter-arguments exist and whether the different treatment could be justified on other objective grounds.

²⁸² Article 1(3) of the Agreement between the Government of the Republic of Finland and the Government of the Republic of Bulgaria on the Promotion and Protection of Investments (Sops 50/1999).

²⁸³ One can raise a number of questions about the scope of this definition. If interpreted literally it would exclude companies incorporated and having their seat in Bulgaria, though owned by Finnish companies or individuals. Neither is it clear whether it covers third country investors investing in Bulgaria and operating through a company incorporated and having its seat in Finland. Likewise, what about Bulgarian investors operating through a Finnish parent company and investing in Bulgaria through a local subsidiary? For general analyses of such questions, see Markus Burgstaller, 'Nationality of Corporate Investors and International Claims against the Investor's Own State', 7 *Journal of World Investment and Trade* (2006), pp. 857-881; Stephan W. Schill, *The Multilateralization of International Investment Law* (Cambridge University Press, 2009), pp. 221-236.

²⁸⁴ It seems clear that the argument could be made that intra-EU BITs discriminate as between the investors covered under them, because the standards of protection and the arbitration options vary from one treaty to the next. This topic is not addressed in the discussion.

²⁸⁵ Of course, if the treaties did not contain arbitration clauses they could still constitute discrimination on the ground that only some EU investors could invoke the (presumably more favorable) protection standards before national courts (though the direct effect of international agreements is subject to various conditions under national legal systems).

It is also useful to remind which state bears the obligation for providing BIT treatment. To use the above example, commonsense dictates that it is only Bulgaria that it is obligated to provide BIT treatment to qualified investments in its territory, but the Court's creative reasoning in *Matteucci* and *Open Skies* points to a different conclusion. *Matteucci* dealt with free movement of workers and *Open Skies* freedom of establishment, but both cases appear, in principle, to be transposable to the BIT context. By analogy, Finland and Bulgaria are obligated to grant BIT treatment to all EU investors established in either member state on the ground of the principle of non-discrimination, and they have to assist each other to this end under the principles of sincere cooperation and primacy of EU law. Since the obligation is mutual, it is unnecessary to dwell on the national/most-favored nation treatment issue. Following the Court's logic, Finland accords the BIT treatment to its own nationals in Bulgaria and is obligated to grant that treatment to EU investors established in its territory, and Bulgaria is required to cooperate to that end (i.e. it has to grant that treatment to all EU investors) and vice versa. Admittedly, this construction is somewhat 'engineered' because only a small percentage of EU investors established in Finland have an investment in Bulgaria or are planning to invest therein.

This issue relates to another argument of the *EURAM* tribunal, namely, that if investors from other member states wish to enjoy intra-EU BIT treatment, they can utilize the internal market freedoms and structure their investments so as to receive that treatment, which makes the question of discrimination redundant.²⁸⁶ In *Saint-Gobain* the French parent company, *Saint-Gobain SA*, would have received the tax benefit if it had set up a subsidiary instead of a branch in Germany, as the former is a resident company under German law. The ECJ held that the different treatment of subsidiaries and branches restricted 'the freedom to choose the most appropriate legal form for the pursuit of activities in another member state', which was conferred to economic operators in Article 49 TFEU. This finding overrules, indirectly, the *EURAM* tribunal's argument, and the more general implication is that the limitation of BIT treatment to nationals of the contracting states can also be viewed as a restriction to the freedom of establishment as it reduces the attractiveness of, say, Bulgaria in the eyes of non-Finnish EU investors.²⁸⁷ On the other hand, the existence of discrimination, too, can be viewed as generally restricting

²⁸⁶ *EURAM* award, supra note 83, para. 273.

²⁸⁷ The Commission made this argument in its letter to the Swedish Government concerning the instigation of infringement proceedings. See Commission letter, supra note 76.

the creation of an integrated internal market, in addition to restrictions flowing from divergent treatment of specific forms of establishment.

In the three tax cases the distinction between resident and non-resident taxpayers played a central role. BITs make no distinction between forms of corporate establishment. The most common form through which investments are made is a subsidiary, which qualifies as a resident company for taxation purposes. Branches, agencies and permanent establishments are considered non-resident companies and are subject to limited taxation only. If the tax cases are analyzed against this background, none of them dealt with the specific situation created by intra-EU BITs, which grant preferential treatment to non-resident *and* resident companies owned by nationals of a given member state in another member state to the exclusion of other EU companies, including those of the host state. *Saint-Gobain* set the principle that resident and non-resident companies in a comparable situation have to receive equal tax treatment. From *D v Inspecteur* flows the principle (*argumentum e contrario*) that when non-resident *individual* taxpayers are in a comparable situation, they have to be treated on equal terms. *Test Claimants* set the principle that when non-resident corporate taxpayers are in a comparable situation, they have to be treated on equal terms. Tax cases may be based on sui generis doctrinal constructions, but at the same time the Court's findings support the applicability of the non-discrimination principle in the situation of intra-EU BITs as well. When member states provide more favorable treatment to companies of another member state, then clearly the distinction between non-resident and resident companies cannot be invoked to claim that only one or the other of these categories is entitled to particular benefits. There is no rationale for such differentiation and it could also be challenged on the ground that it constitutes a restriction on the freedom of establishment, as the Court reasoned in *Saint-Gobain*. Moreover, if *Saint-Gobain* reflects the idea that resident and non-resident companies have to be treated on equal terms, then it can only mean that when a member state grants benefits to resident and non-resident companies owned by nationals of another member state, that treatment has to be accorded to all EU companies established in that state, regardless of the form of establishment.

As to the most-favored nation issue, Hindelang argues for a most-favored nation obligation in the context of free movement of capital and notes that such 'an interpretation also seems

to find sufficient support in systematic and teleological considerations'.²⁸⁸ Having discussed *D v Inspecteur*, he invokes Article 350 TFEU, which sanctions 'the existence or completion of regional unions' between the Benelux countries 'to the extent that the objectives of these regional unions are not attained by application of the Treaties'. The purpose of Article 350 TFEU is to enable 'the three member countries concerned to apply, in derogation from the Community rules, the rules in force within their Union in so far as it is further advanced than the common market'.²⁸⁹ From this Hindelang makes the *e contrario* argument that in the absence of other provisions permitting the application of more advanced market rules between certain member states only, member states appear 'not to be entitled to grant specific benefits to' one or more member states or to their nationals.²⁹⁰ *Ergo*, benefits reserved for nationals of some member states only constitute discrimination. Yet, *contra* Hindelang, as Article 350 TFEU sanctions more developed internal market rules, a plausible argument is that it allows member states to apply such rules in their mutual relations even in the absence of specific authorization. If intra-EU BITs are perceived as catalysts for cross-border investments due to the privileged treatment they provide, then surely their contents qualify as being, in the ECJ's words, 'further advanced' than the equivalent internal market rules. This would mean that the continued existence of intra-EU BITs is justified on the ground that they serve, ultimately, an essential *Existenzberichtigung* of the EU, namely, the peace through trade dictum as they contribute to 'an ever closer union among the peoples of Europe'.²⁹¹ But this argument is highly tentative and Article 350 TFEU awaits to be raised in practice in this manner. Hindelang also assimilates national and MFN treatment on the basis that both stem 'from the idea of equal treatment of economic activities and non-discrimination in cross-border situations'.²⁹² If the purpose of the non-discrimination provisions is to create a level playing field between economic actors within the internal market, an 'internal' MFN obligation can only be consistent with such purpose.²⁹³ This is a plausible argument.

²⁸⁸ Hindelang, *The Free Movement of Capital*, supra note 198, p. 133. Similarly, Georg W. Kofler, 'Most-Favored-Nation Treatment in Direct Taxation: Does EC Law Provide for Community MFN in Bilateral Double Taxation Treaties?', 5 *Houston Business and Tax Law Journal* (2005), pp. 1-89, at 64-65.

²⁸⁹ Case 105/83, *Pakvries BV v Minister van Landbouw en Visserij*, ECLI:EU:C:1984:178, para. 11.

²⁹⁰ Hindelang, *The Free Movement of Capital*, supra note 198, p. 133.

²⁹¹ As provided in the first sentence of the 'operative' part of the TFEU preamble.

²⁹² Hindelang, *The Free Movement of Capital*, supra note 198, p. 133-134.

²⁹³ *Idem*. This 'integrationist' argument is also supported by the text of Article 18 TFEU, which prohibits 'any discrimination on grounds of nationality' (emphasis added). It should be remembered that Article 18 applies independently only when the more specific non-discrimination rules do not apply. See e.g. Case C-1/93, *Halliburton Services*, ECLI:EU:C:1994:127, para. 12.

To summarize, the six cases under discussion indicate that arbitration clauses in both intra-EU and extra-EU BITs constitute prohibited discrimination under EU law. As to extra-EU BITs, it is relatively easy to make the argument that their arbitration clauses actually breach the national treatment principle. The *Open Skies* is most directly relevant, because it concerned benefits granted in third state treaties based on reciprocity, and the ECJ held that it was the eight member states that conferred the benefits to their own nationals in the third country, although the actual decisions, by which the benefits were conferred to EU nationals, were taken by the authorities of the latter. Analogously, and *Matteucci* can also be invoked here, the Court's logic in *Open Skies* means that BIT rights accorded to EU investors in extra-EU BITs by third states are also granted by the member state parties, implying that the treaties violate the national treatment obligation. While the Grandfathering regulation sanctions the continued existence of extra-EU BITs under certain conditions, and while it is unlikely that the Commission will raise the discrimination issue in respect of extra-EU BITs, in strictly legal terms the treaties are problematic from the perspective of the non-discrimination rules. Before discussing what the legal implications of a finding of discrimination are (both under EU law and international law), I will address the issue of competence as it has the potential of complicating the above conclusions.

4.4. The Issue of Competence

Some commentators have made the argument, related to Article 350 TFEU, that as the object and purpose of intra-EU BITs is to increase cross-border capital flows, it is difficult to maintain that they 'contravene the TFEU capital freedoms'.²⁹⁴ This view, in turn, relates to the argument that as the internal market is an area of shared competence, member states remain free to conclude intra-EU BITs in the absence of BIT equivalent legislation, on the condition that the treaties respect the fundamental freedoms of the internal market.²⁹⁵ Member states have not taken cue from such advice, but the question of competence

²⁹⁴ Rumiana Yotova, 'The New EU Competence in Foreign Direct Investment and intra-EU Investment Treaties: Does the Emperor Have New Clothes?', in Freya Baetens (ed.), *Investment Law within International Law: Integrationist Perspectives* (Cambridge University Press, 2013), pp. 387-414, at 391.

²⁹⁵ See Tietje, 'Bilateral Investment Treaties between EU Member States, supra note 17, p. 9 (arguing that member states can conclude *inter se* BITs, but 'must respect the fundamental freedoms of Union law' when doing so); Yotova, 'The New EU Competence', supra note 295, p. 391 ('Given that the EU has not so far purported to regulate intra-EU investment or investors in the comprehensive and targeted way in which intra-EU BITs encourage and protect FDI, it can be concluded that the member states may continue to adopt legally binding treaties in the area [of intra-EU investments]...to the extent that this does not contravene the [EU] treaty freedoms.').

requires some elaboration. Without going into details, the division of competences varied considerably in the above cases. *Matteucci* and the three tax cases concerned areas over which the member states had competence, whereas the EU had at least some competences in the areas that *Gottardo* and *Open Skies* dealt with. In *Open Skies* the freedom of establishment provisions applied in the area of air transport, though the specific division of competences was a complex matter. As to the tax cases, the EU's competences over direct taxation are highly limited, but when member states exercise their direct taxation powers, they have to comply with the non-discrimination rules. In *Matteucci* the Court relied on secondary legislation to bring the scholarships within the scope of the fundamental freedoms, but in *Gottardo* the primary law provision on the free movement of workers was invoked directly as the applicability of the relevant regulation was unclear.²⁹⁶ It is clear that EU law does not provide for, inter alia, fair and equitable treatment, nor allows investors to resort to arbitration against the member states. In the absence of BIT equivalent secondary legislation, could one argue that member states are free to uphold the treaties and limit their application to their respective nationals (with the support of Article 350 TFEU) as long as they respect the fundamental freedoms? The answer is no. *Matteucci* demonstrated how the principle of non-discrimination applied fully even in an area of exclusive member state competence and in respect of intra-EU treaties related to such area.

As to extra-EU BITs, in Opinion 2/15 the ECJ held that investment protection, to the extent it relates to non-direct investments, and investment arbitration fall within a competence shared between the EU and the member states.²⁹⁷ This indicates that member state parliaments have to ratify EU agreements containing provisions on investment protection and arbitration before they can enter into force. What implications does this have for extra-EU BITs? The Grandfathering regulation was adopted in 2012 and it was

²⁹⁶ With respect to *Matteucci*, Klamert makes the curious argument that the principle of 'loyalty extended a prohibition of discrimination in an act of secondary law to an area not covered by Union law, and afforded it precedence over a provision in a bilateral treaty limiting benefits to nationals of two Member States'. This is incorrect in two ways; first, the relevant regulation did not deal with discrimination but specified that the scholarships granted in the treaty came within the scope of the free movement of workers provisions, including the non-discrimination rules, and, second, it was not the principle of loyalty that 'afforded precedence' to the regulation over the treaty, but the primacy of EU law over conflicting inter se treaties. The principle of loyalty was relevant to the construction of the obligations under the treaty as being attributable to both contracting parties, to the attendant finding that the scholarships came under the national treatment obligation, and to the conclusion that all EU nationals resident in the contracting states were eligible to apply for the scholarships. See Marcus Klamert, *The Principle of Loyalty in EU Law* (Oxford University Press, 2014), p. 283.

²⁹⁷ There were some additional FDI issues that remain an area of shared competence, but it is necessary to discuss these in the present context. See *Opinion 2/15*, supra note 66, para. 305.

based on the assumption that extra-EU BITs had come 'under the Union's exclusive competence' with the entry into force of the Lisbon Treaty.²⁹⁸ On the other hand, it also provided that member states have to 'eliminate incompatibilities' from extra-EU BITs, and left the Commission's powers under Article 258 TFEU intact in respect of such incompatibilities. However, it seems clear that the Commission will not raise the issue of discrimination for political reasons, and the main purpose of the Grandfathering regulation is to allow extra-EU BITs to remain in force, even if their provisions may conflict with EU law. That member states are obligated to eliminate conflicting provisions from extra-EU BITs is a truism, but this obligation should be seen against the broader political context. Extra-EU BITs are perceived as important (in particular) for the protection of outbound investments of the old member states, and the Commission has no interest in challenging them under the principle of non-discrimination, also because investment protection and arbitration has been a central part of the EU's own investment policy. In this light, whether extra-EU BITs breach the principle of non-discrimination is an academic concern. Moreover, the question of how the EU's competences in a given area affect the status of treaties concluded between member states and third states that relate to that area is riddled with uncertainty and complexity. Given this, and given the political context of extra-EU BITs, I will only make some tentative comments on the basis of the *Open Skies* judgments.

Before the entry into force of the Lisbon Treaty, the EU had some investment related competences (for example, over trade in services) and it had also adopted a number of investment related secondary acts, some of which dealt with third state companies as well.²⁹⁹ The EU Council also had the power to impose restrictions on investment related payments under a number of primary law arguments.³⁰⁰ However, these competences did not extend to FDI in general, or to investment protection in particular, as the EU had no general powers to legislate on matters typically covered by BITs. In *Open Skies*, the Court held that the EU had an exclusive external competence with respect to some of the provisions of the agreements concluded between a number of member states and the US. This exclusive competence stemmed from the provisions of two regulations, which were adopted before the *Open Skies* agreements were concluded, and which included provisions dealing with the same subject-matter as the *Open Skies* agreements. This EU competence

²⁹⁸ Grandfathering Regulation, supra note 58, recital, para. 4.

²⁹⁹ On these, see Hoffmeister and Ünüvar, 'From BITS and Pieces towards European Investment Agreements', supra note 94.

³⁰⁰ See Articles 64(2), 66, 75 and 215 TFEU.

meant that by concluding the agreements, the member states in question had breached the principle of sincere cooperation as well as the relevant regulations. In an area of exclusive EU competence, member states are allowed to take action only if the EU authorizes them to do so.

The Court also made a finding of discrimination with respect to the freedom of establishment, but this finding was not expressly connected to the question of competence - but were the two findings connected? In other words, was it necessary to establish the existence of an exclusive external competence vis-à-vis parts of the *Open Skies* agreements in order to make a finding of discrimination? And related, if the two findings were connected in the suggested manner, did the nature of the EU's competence (exclusive) play a role? In the judgment concerning the UK, the Court held that application of what is now Article 49 TFEU

'in a given case depends, not on the question whether the Community has legislated in the area concerned by the business which is carried on, but on the question whether the situation under consideration is governed by Community law. Even if a matter falls within the power of the Member States, the fact remains that the latter must exercise that power consistently with Community law. Consequently, the claim by the United Kingdom that the Community has not legislated on air transport outside the Community, even if substantiated, is not capable of rendering Article 52 of the Treaty inapplicable in that sector.'³⁰¹

This excerpt, which is replicated almost verbatim in the other judgments as well, could be read in two ways. First, the reference to member state competence could imply that when member states conclude treaties with third states, they have to respect, without exception, the principle of equal treatment vis-à-vis EU nationals even if the EU has no competences over the subject-matter of the treaties. Second, the Court held that even if the EU had not 'legislated on air transport *outside* the Community...[this would not be] capable of rendering Article 52 of the Treaty inapplicable in that sector'. This could be read as implying that it is necessary that internal legislation exists for the principle of non-discrimination to apply vis-à-vis member states' extra-EU treaties governing the same area

³⁰¹ See Case C-466/98, *Commission v United Kingdom*, ECLI:EU:C:2002:624, paras. 41-42.

as internal legislation. In other words, once the EU has legislated in an area, treaties between member states and third states falling in that area come within the scope of the principle of non-discrimination.³⁰² It is also noteworthy that the existence of exclusive external competence in *Open Skies* was *not* connected to a finding of discrimination in another way: discrimination stemmed from the ownership and control clauses of the *Open Skies* agreements, whereas the exclusive external competence stemmed from EU law provisions dealing with computerized reservation systems, which were also regulated in the *Open Skies* agreements. In other words, the finding of discrimination related to provisions of the *Open Skies* agreements over which the EU appeared to have no competences. This supports the first reading of the *Open Skies* agreements, that is, the reading where it is not necessary that EU legislation/competence exists in a given area for third state treaties to come within the scope of EU law in relation to the non-discrimination rules. When transposed to the BIT context, this would mean that it does not matter that the EU had no competence over FDI (including investment protection) before the Lisbon Treaty, as extra-EU BITs breached the principle of non-discrimination as of their respective dates of conclusion.

Generally speaking, to hold that it is irrelevant whether or not the EU has adopted legislation or has any competences in a given area for the principle of non-discrimination to become relevant vis-à-vis treaties between the member states and third states seems an overly categorical position. Such strict approach would imply that the member states' ability to conclude treaties with third states in areas falling within their competence is severely undermined, given also the typical reciprocal nature of such treaties. In sum, it is not entirely certain what the undergirding logic of the Court's finding of non-discrimination was in the *Open Skies* judgments. Depending on how the Court's approach is understood, one could argue that since extra-EU BITs create a situation of direct discrimination on the basis of nationality between investors from different member states, they breached the principle of non-discrimination in the context of freedom of establishment already before the entry into force of the Lisbon Treaty. This argument could be based on two distinct assumptions: first, on the assumption that extra-EU BITs

³⁰² Another question is whether it was necessary that there was a substantive equivalence between the regulations and the relevant provisions of the *Open Skies* treaties on the basis of which the EU had an exclusive competence. Put differently, if both the *Open Skies* treaties and the regulations had not contained provisions on computerized reservation systems, would the Court have made a finding of discrimination? In yet other words, if the regulations had not contained provisions similar to those found in the *Open Skies* agreements, would the Court have been in a position to invoke discrimination?

came within the scope of the freedom of establishment regardless of the existence of relevant EU legislation; or on the assumption that the pre-Lisbon investment related EU legislation created an EU competence (however narrow) over some aspects of foreign investment, which brought extra-EU BITs within the scope of the non-discrimination principle. I find the first assumption more plausible, although it is, as noted, problematic from a political perspective. The second assumption is not entirely convincing given the differences between the content of the relevant EU legislation in *Open Skies* and the pre-Lisbon investment related EU legislation: there was a clear substantive equivalence between the relevant parts of the *Open Skies* agreements and the two EU regulations, whereas no such equivalence existed between extra-EU BITs and the EU's pre-Lisbon investment related legislation.

There are of course a number of differences between extra-EU BITs and the *Open Skies* agreements. First, the Council had used its competence (under what is now Article 100(2) TFEU) to regulate air transport, whereas prior to the Lisbon Treaty the EU's competences over FDI were not express (whether shared or exclusive) in the sense that the competences related to areas that touched upon some aspects of foreign investments. Second, the provisions of the *Open Skies* agreements over which the EU had exclusive competence regulated narrow technical matters in a particular business sector, whereas extra-EU BITs regulate across-the-board, as all qualified investors and investments in all business sectors come within their protective scope. Third, investment protection (in respect of non-direct investments) and investment arbitration is an area of shared competence, whereas the EU's competences in the area of air transport were exclusive. Whether these differences matter, and what the Court *really* meant in the relevant parts of the *Open Skies* judgments, remain open questions. This short discussion shows that the question of competence is shrouded in uncertainty. Generally speaking, the above discussion has demonstrated that it would appear that member state BITs violate the principle of non-discrimination as a matter of EU law. The following section discusses whether this finding is undermined by countervailing considerations and what the implications of such finding are as a matter of EU law and international law.

4.5. Implications of a Finding of Discrimination for Member State BITs

In principle, to remedy discrimination, member states could extend BIT rights to all EU investors in case of intra-EU BITs and engage in negotiations with concerned third states to effectuate such extension in respect of extra-EU BITs. Another option would be to terminate the BITs either unilaterally or consensually. Some member states have terminated a number of intra-EU BITs,³⁰³ and some third states have terminated a number of extra-EU BITs,³⁰⁴ but it seems clear that this policy will remain the exception rather than the rule. The extension of the scope of intra-EU BITs is an equally implausible option for a number of reasons. In the *D v Inspecteur* case the Commission and a number of member states argued that

'a Member State party to a bilateral convention is not in any way required, by virtue of the Treaty, to extend to all Community residents the benefits which it grants to residents of the Contracting Member State. Those governments and the Commission refer to the danger which the extension of the benefits provided for by a bilateral convention to all Community residents would entail for the application of existing bilateral conventions and of those which the Member States might be prompted to conclude in the future, and to the legal uncertainty which that extension would cause.'³⁰⁵

This statement related specifically to double taxation treaties, but it is also relevant in relation to intra-EU BITs. All intra-EU BITs were originally extra-EU BITs,³⁰⁶ and their central object and purpose was to safeguard investors of the capital exporting member states in the formerly socialist states, which were not yet 'ready' for EU membership at the time of the treaties' conclusion. The general assumption was that (not just intra-EU) BITs would increase the inflow of western investments in those states, as investors could rely on arbitration instead of domestic courts in case of disputes with the host state. Such

³⁰³ See supra note 196.

³⁰⁴ See the discussion in Chapter 7.

³⁰⁵ *D v Inspecteur*, supra note 167, para. 48.

³⁰⁶ Prior to the 2004 EU enlargement, only two intra-EU BITs existed, namely, the Germany-Greece and Germany-Portugal BITs concluded in 1961 and 1980 respectively (i.e. prior to the EU accession of the latter parties). Even without statistical support, it seems evident that these treaties, in practice, protected German investments in Greece and Portugal.

assumption was undergirded by the perception that in the immediate post-communist environment the domestic institutions of the formerly socialist states lacked the necessary quality to make policy (across the three branches of government) in a predictable manner and in accordance with pre-established rules of law. Under such circumstances, investment arbitration provided a neutral forum for the settlement of investment disputes.³⁰⁷ As was the case with the earlier BITs concluded between western states and newly decolonized states, the underlying reciprocity of intra-EU BITs was not reflected in practice, as investment flows remained unidirectional, travelling mostly eastwards from the old member states to the post-2004 member states. Even today, only a tiny fraction (if even that) of the investment stocks of the old member states consist of investments coming from the new member states, with an overwhelming majority originating from the other old member states. Similarly, the bulk of the investment stocks of the formerly socialist states consist of investments coming from the old member states.

A few examples illustrate this dynamic. Finland has eleven intra-EU BITs with states that acceded to the EU in 2004 at earliest.³⁰⁸ According to the Central Bank of Finland, at the end of 2013 the value of the foreign investment stock in Finland was € 73 459 million, out of which more than ninety percent was of European origin.³⁰⁹ However, investors from just three of the eleven BIT partner states had investments in Finland and these counted for little less than 0,001 percent of the overall FDI stock. In contrast, more than ninety-five percent of the stock comprised of investments coming from the old member states. In case of Romania, almost eighty percent of its FDI stock consists of investments coming from the old member states,³¹⁰ while the investments of Romanian investors in the main European economies are virtually non-existent.³¹¹ Though these figures vary from one member state to the next, they are representative of the general trend as regards

³⁰⁷ For a general argument on the virtues of investor-state arbitration vis-à-vis national courts, see Brower and Schill, 'The Legitimacy of International Investment Law?', supra note 18, at 477-483.

³⁰⁸ With Bulgaria, Croatia, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovakia, and Slovenia.

³⁰⁹ The statistic is available at http://www.suomenpankki.fi/en/tilastot/maksutase/pages/tilastot_maksutase_ja_suorat_sijoitukset_maksutase_suorat_sijoitukset_suomeen_kanta_maittain_en.aspx (accessed 9 August 2016).

³¹⁰ See National Bank of Romania, *Foreign Direct Investment in Romania in 2015*, pp. 11-12.

³¹¹ Of the major economies, only the UK data referred expressly to Romanian investments which stood at zero at the end of 2015. Since Romanian investments were not broken down in respect of the inward FDI stocks of Belgium, France, Italy and the Netherlands, it is safe to assume that these were Lilliputian. The UK data is available at <https://www.ons.gov.uk/economy/nationalaccounts/balanceofpayments/bulletins/foreigndirectinvestmentinvoivingukcompanies/2015/relateddata> (accessed 14 January 2017).

investments that qualify for protection under intra-EU BITs; they only have relevance for investments flowing from the old member states to the formerly socialist states, and an overwhelming majority of intra-EU investments are not protected under existing BITs.³¹²

In light of such data, the argument that EU law requires member states to extend the scope of application of intra-EU BITs to cover all EU investors is implausible. Such imposition would also go against the object and purpose of intra-EU BITs and exponentially increase the exposure of old member states to arbitration claims and financial liability, if and when specific claims result in awards for damages.³¹³ In *Gottardo*, the ECJ argued that the increase in Italy's fiscal burden flowing from the extension of the pension benefit to all resident EU nationals 'could not justify' Italy's failure to comply with its EU law obligations. In other words, that benefit had to be extended to resident EU nationals regardless of the costs Italy incurred.³¹⁴ Similarly, in *Saint-Gobain*, the ECJ held that a decrease of tax revenue flowing from the extension of the relevant tax benefit 'cannot be regarded as a matter of overriding general interest which may be relied upon in order to justify unequal treatment that is in principle incompatible with Article 52 of the Treaty'.³¹⁵ However, the consequences of the extension of the benefits in these two cases are very different when compared to intra-EU BITs. It is one thing to impose an obligation to grant clearly defined individual tax or other benefits to all EU workers and companies established in a member state, and quite another to allow all EU investors to bring claims against a wide range of legislative, administrative and judicial acts, the success of which depends on the interpretation of vaguely formulated BIT standards by ad hoc arbitral tribunals. Arguably, this 'general consequence' was reflected in Opinion 2/15 where the Court held that member states had to give their consent to the CETA investment protection provisions on the ground that such provisions were not 'of a purely ancillary nature' as they removed 'disputes from the jurisdiction of the courts of the member states'.³¹⁶ Extending

³¹² The ECT, however, provides protection to all intra-EU investments in the energy sector.

³¹³ Legal costs of investment arbitration appear to be relatively high as well. A 2014 study found that the average costs in cases where such information was available was circa US\$ 4,437,000 for claimants and circa US\$ 4,559,000 for respondents. These figures exclude arbitrator and administrative fees. See Matthew Hodgson, 'Counting the Costs of Investment Treaty Arbitration', *Global Arbitration Review* (24 March, 2014), at 2. The average cost figures were based on 73 (claimant) and 66 (respondent) cases respectively. Hodgson also points out that 'a few cases with extremely high costs distort the figures' (*idem.*) and the median costs were circa US\$ 3,145,000 for claimants and circa US\$ 2,286,000 for respondents (*ibid.*). The average administrative and arbitrator costs, in turn, were US\$ 746,000 (median US\$590,000), *ibid.* at 3.

³¹⁴ *Gottardo*, supra note 225, para. 38.

³¹⁵ *Saint-Gobain*, supra note 271, para. 51.

³¹⁶ *Opinion 2/15*, supra note 66, para. 292.

the scope of intra-EU BITs to cover all EU investors would also be difficult to put into practice. For example, as the contents of Finland's intra-EU BITs vary, on which arbitration clause could EU investors established in Finland rely? Assuming that such extension would also cover the substantive protection standards and other provisions, which definitions of investments and investors, and which protection standards in intra-EU BITs are most investor-friendly? Could investors pick-and-choose BIT provisions according to their preferences and would this right extend to investors already protected by an intra-EU BIT? To quote the statement of the Commission and member states in *D v Inspecteur*, much 'legal uncertainty' would follow if member states were required to extend the scope of intra-EU BITs. Moreover, the Court cannot force the member states to expand the scope of intra-EU BITs as a matter of international law.

One of the preliminary questions that the BGH submitted to the ECJ asked whether Article 18 TFEU precludes the application of the Dutch-Slovak BIT's arbitration clause when the BIT was concluded before the EU accession of the Slovak Republic and when the claimant investor raised the relevant claim after the Slovak Republic's EU accession. The hearings on the BGH's preliminary questions were held in June 2017, and while the transcripts of the hearings are not publicly available, some attendees have revealed some of the arguments. One of the arguments was that the preliminary question concerning discrimination is inadmissible because the BGH proceedings do not involve a third party claiming discrimination.³¹⁷ In other words, since there is no third party (a company or 'investor') claiming that the Dutch-Slovak BIT's arbitration clause breaches the principle of non-discrimination, the BGH or the ECJ should not address such hypothetical argument. Should the ECJ accept this argument, the question of discrimination in the context of intra-EU BITs would remain unsettled. Conversely, and hypothetically speaking, should the ECJ address the question and follow the reasoning outlined above, it should find that intra-EU BITs breach the principle of non-discrimination under EU law, with reference to its previous case law, the principle of sincere cooperation and primacy of EU law.

As to arbitral tribunals, they have conceded that intra-EU BITs may breach the non-discrimination rules of EU law and suggested that the problem is resolved by extending

³¹⁷ See Alexander Gross, 'Zwischen Skylla und Charybdis. Die Kollision von völkerrechtlichen Intra-EU BITs mit dem Unionsrecht', *Völkerrechtsblog*, 4 August 2017. See at <https://voelkerrechtsblog.org/zwischen-skylla-und-charybdis/> (accessed 18 August 2017).

those rights to all EU investors, and that in any case it is up to the EU Commission to take action to correct the alleged discrimination. In *EURAM*, the expert witness of the claimant argued that discrimination 'is an internal EU law problem and not an issue of treaty compatibility'.³¹⁸ In one way, this statement goes in the right direction. The above cases indicated that under EU law member states are obligated to provide equal treatment to economic actors in a comparable situation, but it is not the material content of BIT rights that breaches the non-discrimination principle but their exclusivity in terms of beneficiaries. Likewise, the conflicting obligations can be construed as being owed to different subjects. BIT obligations are owed to the contracting states' investors (or the other contracting state) and the non-discrimination obligation to other EU investors (or their home states). Hence, as a matter of international law, because no material conflict exists between the two set of obligations, and because they are owed to different parties, the BIT obligations continue to apply and the problem of discrimination is to be resolved 'internally' by the competent EU institutions.

It is also useful to note that discrimination is not an academic problem, particularly in the context of intra-EU BITs. To give two examples, in 2011 and 2012 Hungary introduced two laws under which foreign owned companies were excluded from taking part in the so called 'social voucher' business (companies offer such vouchers to employees as benefits). As a response, the Commission started infringement proceedings against Hungary arguing that the laws breached a directive³¹⁹ as well as the freedom of establishment and freedom to provide services. Around the same time, three companies affected by the laws (all French) brought claims against Hungary under the France-Hungary BIT.³²⁰ In February 2016, the ECJ declared that the legislative changes violated the directive and the fundamental freedoms,³²¹ and somewhat later one of the tribunals in the three BIT cases decided that the laws violated the French-Hungary BIT and awarded around 23 million euros as compensation to the claimant investor.³²² Clearly, and in principle, if some of the

³¹⁸ *EURAM* award, supra note 83, para. 270.

³¹⁹ This was Directive 2006/123/EC of the European Parliament and of the Council of 12 December 2006 on services in the internal market, OJ L 376, 27.12.2006, pp. 36–68

³²⁰ The cases are *Edenred S.A. v. Hungary*, ICSID Case No. ARB/13/21; *Le Chèque Déjeuner and C.D Holding Internationale v. Hungary*, ICSID Case No. ARB/13/35; *Sodexo Pass International SAS v. Hungary*, ICSID Case No. ARB/14/20.

³²¹ See Case C-142/4, *Commission v Hungary*, ECLI:EU:C:2016:108.

³²² The *Edendred* tribunal rendered the final award on 13 December 2016, but it is not publicly available. The other two arbitrations are pending and no information on the cases has been released. See Luke Eric Peterson, 'French investor wins 23 million EUR under France-Hungary BIT', *IAR Reporter News*, 16 December 2016;

companies affected by the legislative changes come from member states with which Hungary has not concluded a BIT, those companies are in a worse position than French and other companies that can rely on an intra-EU BIT, regardless of the remedies available to them under EU law and Hungarian law.

The *Eureko* arbitration provides another useful example. The claimant investor had filed a complaint with the Commission around the same time it had initiated the arbitral proceedings. The claimant's cause of action was the same in both instances and related to the reversal of the privatization of the Slovak Republic's health insurance market, which had taken place in 2007 after a change in government. The claimant argued that the reversal had 'effectively destroyed the value' of its investment and the complaint led the Commission to start infringement proceedings against the Slovak Republic.³²³ In the letter of formal notice the Commission noted that the 'prohibition on health insurance companies to freely dispose of any profits resulting from the provision of public health insurance in Slovakia...constitutes an unjustified restriction on the freedom of capital movements guaranteed by Article 63' TFEU.³²⁴ Similarly, in January 2011, the Slovak Republic's constitutional court ruled that such 'ban on profits' was unconstitutional, and thus null and void,³²⁵ and it seems that this ruling prompted the Commission to discontinue the infringement proceedings. As to the remedies available under EU law, the claimant noted that it had little influence on how the Commission pursues the complaint, and that in any case the 'ancillary proceedings in the European Court of Justice can by their very nature not result in a damages award', and neither can its damages 'be redressed through other EU-channels'.³²⁶

First, these remarks are no entirely convincing, because the Court's case law suggests that primary law provisions establishing the internal market freedoms can create vertical direct effect. In other words, those provisions 'confer on individuals rights upon which they are entitled to rely directly before the national courts'.³²⁷ Second, the ECJ has also held that a

Jarrod Hepburn, 'An update on three investment treaty claims against Hungary', *IAReporter News*, 24 February 2016.

³²³ *Eureko* award, supra note 74, paras. 7, 55-56.

³²⁴ See Commission Decision (EU) 2015/248 of 15 October 2014, OJ L 41, 17.2.2015, pp. 25-40, at footnote 8.

³²⁵ *Achmea B.V. (formerly known as "Eureko B.V.") v. the Slovak Republic*, PCA Case No. 2008-13, Final Award (hereinafter *Achmea* award), 7 December 2012, paras. 115-116.

³²⁶ *Eureko* award, supra note 74, para. 56.

³²⁷ Joined Cases C-46/93 ja C-48/93, *Brasserie du Pêcheur and Factortame*, ECLI:EU:C:1996:79, para. 23

breach of the fundamental freedoms may give rise to compensation if three conditions are met. First, the infringed rule 'must be intended to confer rights on individuals [i.e. must have direct effect]'; second, 'the breach must be sufficiently serious'; and, third, 'there must be a direct causal link between the breach of the obligation resting on the State and the damage sustained by the injured parties'.³²⁸ In policy areas where the member states enjoy wide discretion, a breach is sufficiently serious only if the member state 'manifestly and gravely disregarded the limits on its discretion'.³²⁹ *Eureko* concerned the privatization of the Slovak Republic's healthcare system, an area which has not been harmonized at the EU level, which implies that the member states enjoy wide discretion in that area. Assuming that the claimant investor had raised a claim for damages on the basis of Article 63 TFEU before the Slovak Republic's courts, it is difficult to predict whether the claim would have succeeded and what amount of compensation it could have received.³³⁰ However, what is clear that the criteria of liability under BITs is less strict. The seriousness of a breach may affect the calculation of damages, but is not an independent criterion, and whether the damages were caused by a state's legislative, executive or judicial branch does not play a *formal* role in the quantum of damages either, whereas under EU law the threshold of liability is higher when the loss is caused by a general legislative act. In this light, it is not surprising that the claimant in *Eureko* decided to pursue a claim only under the BIT; damages claims under national laws and EU law, particularly when they relate to a general legislative act, are less likely to succeed, and even if they succeed the amount of damages may not provide sufficient restitution.³³¹ The *Eureko* tribunal awarded the claimant around 22 million euros in damages, which implies, similarly to the first example, that the Dutch-Slovak BIT placed the claimant investor in a more favorable position than EU investors that could not rely on an intra-EU BIT but were equally affected by the challenged

³²⁸ Ibid., para. 51.

³²⁹ Ibid., para. 55. The Court noted that the factors that should be taken into consideration in assessing the seriousness of the breach 'include the clarity and precision of the rule breached, the measure of discretion left by that rule to the national or Community authorities, whether the infringement and the damage caused was intentional or involuntary, whether any error of law was excusable or inexcusable, the fact that the position taken by a Community institution may have contributed towards the omission, and the adoption or retention of national measures or practices contrary to Community law'. Ibid., para. 56.

³³⁰ In its statement of claim, *Eureko* argued that its case 'is further supported by Article 56 EC, which prohibits all (unjustified) restrictions on movements of capital'. This meant that the challenged measures 'constitute breaches of this Article 56 EC as well'. Similarly, *Eureko* argued that the challenged measure constituted a 'blatant disregard' of EU law, which 'supports a finding that the Slovak Republic has failed to offer fair and equitable treatment to *Eureko*'s investment and restricted the freedom of capital movement'. See paras. IV.90 and IV.114 of the Statement of Claim, *EUREKO B.V. v. Slovak Republic*, PCA Case No. 2008-13, 16 June 2009.

³³¹ It is noteworthy that the *Eureko* tribunal ordered the Slovak Republic to pay to the claimant around €22.1 million in damages. See *Achmea* award, *supra* note 325, para. 352.

measure. This would imply that foreign investors operating in a given business sector are always in a comparable situation in relation to general legislative and administrative acts that affect that business sector, but only some of them are able to rely on BIT protections. Similarly, investors are in a comparable position in respect of the available remedies; whether a state measure has general application or whether it targets a specific company, the affected investors can rely on the same remedies, apart from investors whose investments qualifies for protection under a BIT. These points provide indirect support to the argument that investors are in a comparable situation and that the existence of an investment treaty does not render their situation incomparable.

As a final matter, the question of interests and values merits a few comments. One general argument for maintaining the status quo is that intra-EU BITs continue to be essential for protecting eastbound investments within the EU, because the rule of law remains weak and fragile in the formerly socialist member states. Such understanding receives support from various corruption indexes and Commission reports dealing with the member states' regulatory environment, including reports on the (lack of) institutional reforms that the new member states have taken after EU accession.³³² For example, a recent Commission report expressed concerns about the 'independence, quality and efficiency' of Bulgaria's judicial system, 'including a certain lack of predictability due to inconsistent rulings'.³³³ The report outlines similar types of concerns in respect of a number of other post-2004 member states, and the proponents of intra-EU investment treaties have used this and other similar reports to attack the Commission's policy on intra-EU BITs.³³⁴ The rule of law may lack a universally accepted definition, but it is more or less uncontested that the domestic institutions of the old member states meet the criteria commonly associated with the concept, and this observation is supported by the fact that the old member states have not concluded any BITs between them.³³⁵ In this light, one could argue that it is a matter of 'overriding general interest' to the old member states to maintain intra-EU BITs, and that the different treatment is 'objectively justified' on the ground of the rule of law concerns, as well as on the ground that the treaties increase investment flows.

³³² See EU Commission, *The 2017 EU Justice Scoreboard* (Publications Office of the European Union, 2017); EU Commission, *Member States Investment Challenges*, SWD(2015)400 final/2, Brussels, 18 December 2015.

³³³ European Commission, *The 2017 EU Justice Scoreboard*, p. 13.

³³⁴ See e.g. the Non-paper from Austria, Finland, France, Germany and the Netherlands, *Intra-EU Investment Treaties*, submitted to the Trade Policy Committee, 7 April 2016.

³³⁵ Apart from, as noted, the Germany-Greece and Germany-Portugal BITs which were concluded in 1961 and 1980 respectively (i.e. prior to the EU accession of Greece and Portugal).

Chapter 7 will analyze the rule of law argument as well as the correlation between BITs and investment flows in more detail, but already here it is worth pointing out that while some of the new member states have faced and continue to face multiple BIT claims, the old member states with more developed rule of law systems are also facing an increasing number of claims, particularly under the Energy Charter Treaty.³³⁶ This suggests that what the rule of law means in case specific circumstances is a perspectival matter in the sense that investors will naturally resort to investment arbitration if such possibility exists, however strong the rule of law may be in a given member state. More generally, interest groups are prone to think that their constituencies are never adequately protected, not even in western democracies, so the rule of law argument is always available to them in this sense. There probably is no shortage of domestic court cases across the EU where, for example, a foreign investor has been left uncompensated for economic loss. Another point is that it is equally possible that many of the claims against the new member states relate to requirements imposed by EU law, or they may be 'frivolous' claims, or then stem from what are widely considered as legitimate public interest concerns. A good example is the case against Romania, initiated in August 2015, where the claimant investor argues that the delay in the issuance of an environmental permit, a precondition for starting a mining project, breaches the Romania-UK and the Romania-Canada BITs. Rather than reflecting legal backwardness or administrative inertia and corruption, the non-issuance of the permit may well reflect (as reported by news agencies) justified concerns about the implications of the project for the environment, which is a 'modern' concern par excellence.³³⁷ This indicates that statistics are not a substitute for a more rigorous analysis of the relevant cases and the circumstances out of which they arose. To paraphrase an old idiom, whoever invokes the rule of law, *may* want to cheat.

The above discussion has focused on intra-EU BITs, and while the status of extra-EU BITs is now governed by the Grandfathering regulation, for the sake of completeness it is useful to say a few words on how the issue of discrimination *could* impact their continued application and validity. Assuming that extra-EU BITs constitute prohibited discrimination under EU law, Article 351 TFEU and the principle of sincere cooperation would be relevant alongside the Grandfathering regulation. As discussed in Chapter 3, Article 351

³³⁶ For example, investors have raised more than thirty claims against Spain under the ECT. The cases will be discussed in Chapter 5.

³³⁷ See Adam Cernea Clark, 'Whose Resources? Gabriel Resources v. Romania', *Huffington Post*, 6 August 2015.

TFEU holds that rights and obligations under *pre-accession* treaties concluded with *third states* 'shall not be affected by the provisions of this Treaty'.³³⁸ However, this protective ambit is subject to the limitation in the second paragraph, which provides that in case of conflict member states 'shall take all appropriate steps to eliminate the incompatibilities established'.³³⁹ In other words, Article 351 TFEU allows the member states to honor their pre-accession treaty obligations, but simultaneously requires them to take 'appropriate steps' to eliminate such obligations if and when they conflict with EU law. Von Papp has characterized this ambiguity by noting that the article's first paragraph 'shows an openness towards public international law', whereas paragraph two is 'essentially... a statement of EU supremacy'.³⁴⁰ The ECJ has clarified the scope of Article 351 TFEU by finding that it also protects *individuals* who enjoy rights under a pre-accession treaty,³⁴¹ such as rights of investors under extra-EU BITs. In essence, Article 351 TFEU creates a similar obligation as the Grandfathering regulation,³⁴² but is more specific as it expressly protects the rights of third states and their nationals under pre-accession BITs. Article 4(3) of the Treaty on European Union (TEU), in turn, establishes the principle of sincere cooperation, which

³³⁸ The ECJ has specified that the term 'rights' refers to the rights of third states and the term 'obligations' to obligations of EU member states under earlier treaties. The provision also applies to treaties concluded by the founding member states of the EU prior to the creation of the Union. See Case 10/61, *Commission v Italy*, ECLI:EU:C:1962:2, p. 10; Case C-158/91, *Jean-Claude Levy*, ECLI:EU:C:1993:332, para. 12. For a critique of this construction, see Konstanze von Papp, 'Resolving Conflicts with International Investment Treaty Law from an EU Law Perspective: Article 351 TFEU Revisited', 42 *Legal Issues of Economic Integration* (2015), pp. 325-356, at 340-341. For an analysis of the components of Article 351 TFEU, see Julie M. Grimes, 'Conflicts between EC Law and International Treaty Obligations: A Case Study of the German Telecommunications Dispute', 35 *Harvard Journal of International Law* (1994), pp. 535-564, at 542-557.

³³⁹ Article 351 TFEU reads: '[1.] The rights and obligations arising from agreements concluded before 1 January 1958 or, for acceding States, before the date of their accession, between one or more Member States on the one hand, and one or more third countries on the other, shall not be affected by the provisions of the Treaties. [2.] To the extent that such agreements are not compatible with the Treaties, the Member State or States concerned shall take all appropriate steps to eliminate the incompatibilities established. Member States shall, where necessary, assist each other to this end and shall, where appropriate, adopt a common attitude. [3.] In applying the agreements referred to in the first paragraph, Member States shall take into account the fact that the advantages accorded under the Treaties by each Member State form an integral part of the establishment of the Union and are thereby inseparably linked with the creation of common institutions, the conferring of powers upon them and the granting of the same advantages by all the other Member States.' In the context of implementing UN Security Council resolutions taken under Chapter VII of the UN Charter, the ECJ has held that Article 351 'could, if the conditions for application have been satisfied, allow derogations even from primary law', but that 'in no circumstances [does Article 351] permit any challenge to the principles that form part of the very foundations of the Community legal order, one of which is the protection of fundamental rights'. See Joined Cases C-402/05P and 415/05P, *Kadi & Al Barakaat*, ECLI:EU:C:2008:461, para. 301; Case C-124/95, *Queen v HM Treasury and Bank of England*, ECLI:EU:C:1997:8, paras. 56-61. Given the content of Article 103 of the UN Charter and the nature of Chapter VII resolutions, it is safe to say that this case law has no bearing vis-a-vis member state BITs.

³⁴⁰ Von Papp, 'Article 351 TFEU Revisited', supra note 338, pp. 333-334.

³⁴¹ See Case C-812/79, *Attorney General v Burgoa*, ECLI:EU:C:1980:231, para. 10.

³⁴² See Grandfathering Regulation, supra note 58, recital, para. 11 ('Member States are required to take the necessary measures to eliminate incompatibilities, where they exist, with Union law, contained in bilateral investment agreements concluded between them and third countries').

requires member states to take appropriate measures 'to ensure fulfillment' of their EU law obligations, to 'facilitate the achievement of the Union's tasks', and to 'refrain from any measure which could jeopardize the attainment of the Union's objectives'.³⁴³ These two provisions create a similar obligation and bind the member states as a matter of EU law only, just as the Grandfathering regulation does. While the scope and content of the three provisions is somewhat different, their cumulative scope of application extends to all existing extra-EU BITs.

This begs the hypothetical question of what implications the existence of discrimination could have for the status of extra-EU BITs as a matter of international law. As to conflict rules, Articles 30(3) and 59 VCLT are not relevant for extra-EU BITs, because they only concern successive treaties between identical parties. Third states with which member states have concluded BITs are not parties to the EU founding treaties. As noted in Chapter 2, two basic principles govern the position of third states in situations where their treaty party has or undertakes conflicting obligations under another treaty to which the former is not party: the *res inter alios acta* principle stipulates that treaties only bind their parties and are valid as between them, and the *pacta tertiis nec nocent nec prosunt* principle stipulates that 'no treaty may create obligations' for a third state 'without its consent'.³⁴⁴ These principles, enshrined in Article 30(4)(b) VCLT,³⁴⁵ indicate that the principle of non-discrimination, as it stands under EU law, has no effect on the rights of third states and their investors under extra-EU BITs as a matter of international law. The discussion on intra-EU BITs also showed that member states are obligated to provide equal treatment to economic actors in a comparable situation, but that it was not the material contents of BIT provisions that breached the non-discrimination principle, but the limitation of their application to the contracting states' investors. Hence, the problem of discrimination is again to be resolved 'internally' by the competent EU institutions.

³⁴³ The full text of Article 4(3) TUE reads as follows: 'Pursuant to the principle of sincere cooperation, the Union and the Member States shall, in full mutual respect, assist each other in carrying out tasks which flow from the Treaties. The Member States shall take any appropriate measure, general or particular, to ensure fulfillment of the obligations arising out of the Treaties or resulting from the acts of the institutions of the Union. The Member States shall facilitate the achievement of the Union's tasks and refrain from any measure which could jeopardize the attainment of the Union's objectives.'

³⁴⁴ Ranganathan, *Strategically Created Treaty Conflicts*, supra note 51, p. 56.

³⁴⁵ Article 30(4)(b) VCLT reads as follows: '4. When the parties to the later treaty do not include all the parties to the earlier one... (b) As between a State party to both treaties and a State party to only one of the treaties, the treaty to which both States are parties governs their mutual rights and obligations.'

The above discussion has strived to show that the Court's case law implies that member state BITs constitute prohibited discrimination, and that it is difficult to think of 'objective justifications' that could authorize the different treatment, although Advocate General Wathelet's arguments suggest that the Court could still go either way. However, even if such objective justifications were to exist, this would not end the debate on member state BITs. The concern about the autonomy of the EU legal order remains, and it is to that complex issue that I now turn.

5. The Autonomy of the EU Legal Order: Treaty Conflict or Co-operation?

5.1. Preliminary Remarks

The ECJ has rendered a number of decisions which examine the compatibility with EU law of court systems established under agreements to which the Union is party (or was to become a party) either alone or alongside its member states and/or third states. Apart from the *MOX Plant* judgment, these decisions were rendered pursuant to Article 218(11) TFEU, which provides that the member states and the main EU institutions 'may obtain the opinion of the Court of Justice as to whether an agreement envisaged is compatible with the Treaties. Where the opinion of the Court is adverse, the agreement envisaged may not enter into force unless it is amended or the Treaties are revised'. The agreements that the Court has analyzed have varied in terms of content and party constellation, but these opinions establish, arguably, principles that are transposable to the member state BIT context and enable an assessment of the compatibility of investment arbitration with the autonomy of the EU legal order. The following discussion analyzes the *MOX Plant* case and four opinions: Opinion 1/91 (concerning the creation of the European Economic Area), Opinion 1/00 (concerning the European Common Aviation Area agreement), Opinion 1/09 (concerning the creation of a Patent Court) and Opinion 2/13 (concerning the accession of the EU to the European Convention on Human Rights). Before proceeding to discuss them, however, it is useful to summarize how the question of autonomy has been dealt with in arbitral practice.

5.2. Autonomy Related Arguments in Arbitral Practice

Express references to the concept of autonomy of EU law are rare in arbitral practice. The respondent member states have relied, above all, on Article 344 TFEU to establish the incompatibility of BIT arbitration clauses with EU law, as has the EU Commission both in its *amicus curiae* submissions and in its letter of formal notice to the Swedish Government concerning the Romania-Sweden BIT. The basic argument is that the ECJ has exclusive jurisdiction over EU law related disputes under Article 344 TFEU,³⁴⁶ and in one of the

³⁴⁶ See e.g. *EURAM* award, supra note 83, paras. 98 and 101.

Commission's submissions this exclusive jurisdiction was linked with the autonomy of EU law.³⁴⁷ The Commission specified that the Court's exclusive jurisdiction extends to disputes between the member states and private parties, at least when such disputes involve questions of EU law. To support this argument, the Commission invoked the *MOX Plant* case,³⁴⁸ which concerned the relationship of EU law and the United Nations Convention on the Law of the Sea (UNCLOS), to which both the EU and its member states are parties. In essence, the Commission argued that the Court's reasoning in *MOX Plant*, when read in connection with the text of Article 344 TFEU, reflects a 'more general principle' under which the member states 'cannot agree that disputes concerning the interpretation or application of Union law' are 'subject to a method of dispute settlement different from those provided in' the EU founding treaties.³⁴⁹ The Commission pointed out that arbitration under intra-EU BITs 'presupposes' that two member states have consented to the jurisdiction of arbitral tribunals under certain conditions, and that mutual consent breaches Article 344 TFEU.³⁵⁰

The Commission made a similar argument in its letter of formal notice to the Swedish Government concerning the Romania-Sweden BIT. The difference was that in the *US Steel* arbitration (where the Commission referred to *MOX Plant*) the subject matter of the dispute was of direct concern to the Commission,³⁵¹ whereas in the letter of formal notice the mere existence of the BIT's arbitration clause was argued as breaching Article 344 TFEU. The Commission argued that arbitral tribunals constituted under the BIT may have to interpret and apply EU law in individual disputes, which constitutes a breach of Article 344 TFEU as such.³⁵² The Commission also contended that Article 344 TFEU should be

³⁴⁷ EU Commission, *amicus curiae* brief in *US Steel*, supra note 124, para. 36.

³⁴⁸ Case C-459/03, *Commission v Ireland*, ECLI:EU:C:2006:345 (hereinafter *MOX Plant*). For a discussion of the case and the attendant legal instruments, see Nikolaos Lavranos, 'The MOX Plant and IJzeren Rijn Disputes: Which Court is the Supreme Arbiter?', 19 *Leiden Journal of International Law* (2006), pp. 223-246; Cesar P. R. Romano, 'Commission of the European Communities v. Ireland. Case C-459/03. Judgment', 101 *American Journal of International Law* (2007), pp. 171-179.

³⁴⁹ EU Commission, *amicus curiae* brief in *US Steel*, supra note 124, paras. 37 and 44. The case was discontinued at an early stage before the tribunal had decided the jurisdictional challenges of the respondent and the EU Commission.

³⁵⁰ *Ibid.*, para. 44.

³⁵¹ The claimant's cause of action in the *US Steel* arbitration concerned the revocation of certain investment incentives by the Slovak Republic. As in *Micula*, the Commission argued that the investment incentives had constituted illegal state aid under EU law and had to be revoked, although the Commission had not taken a formal decision in this regard. See *ibid.*, paras. 6-12.

³⁵² See Commission letter, supra note 76, pp. 12-13 ('Genom sitt samtycke att avgöra tvister om frågor som omfattas av det bilaterala investeringsavtalet med relevant skiljedomsförfarande tar vardera avtalsparten, genom godtagande av artikel 7 i det bilaterala investeringsavtalet, upp tvister som även gäller tolkningen

interpreted against the principles of primacy, effectiveness and unity of EU law. Although the Romania-Sweden BIT did not prevent investors from taking the dispute to national courts in parallel to arbitral proceedings, the Commission argued that once an investor initiates arbitral proceedings, 'national courts can no longer preside over the same cause of action'.³⁵³ As a consequence, the preliminary reference procedure under Article 267 TFEU is bypassed, which threatens the primacy, effectiveness and unity of EU law, because arbitral tribunals interpret and apply EU law outside the ECJ's controlling arm.³⁵⁴

Arbitral tribunals have not expressly referred to the concept of autonomy, and their consensus on Article 344 TFEU is that it is only relevant in respect of disputes between two member states. Further, in the absence of an EU law provision expressly prohibiting investment arbitration, the only plausible conclusion is that arbitration clauses in intra-EU BITs are compatible with EU law.³⁵⁵ Tribunals have also referred to the existence of multiple instances where various courts and tribunals interpret EU law without the involvement of the ECJ, with the inference that the latter has no 'absolute monopoly...over the interpretation and application of EU law'.³⁵⁶ This argument received backing from the discretion that member state courts enjoy (apart from courts of last instance) in respect of the preliminary ruling procedure and from the *acte clair* doctrine.³⁵⁷ Another relevant fact was that in most of the arbitrations the tribunal's seat was in a member state, which allowed the parties to challenge the tribunal's decisions before that state's courts, and the latter could seize the ECJ through the preliminary ruling procedure. In the event that member states comply with an award that breaches EU law, the EU Commission may start

eller tillämpningen av [EU] fördragen med hjälp av en annan tvistlösningsmetod än de normala metoder som föreskrivs däri.').

³⁵³ *Ibid.*, p. 13 ('Så snart ett ärende har hänskjutits till en skiljedomstol, kan en nationell domstol inte längre pröva samma mål.').

³⁵⁴ *Idem.* ('Till följd av detta skulle de nationella domstolarna och EU-domstolen inte vara i stånd att, genom de sedvanliga rättsmedel som föreskrivs genom EU-fördragen, se till att EU-lagstiftningens företräde, enhetlighet och verkan säkerställs.'). The Commission referred to *Opinion I/09*, ECLI:EU:C:2011:123, paras. 60-89 in this context. As a final point, the Commission also argued that the arbitration clause undermines the principles of mutual trust and sincere cooperation, which require that member states trust each other's court systems (see *ibid.*, p. 14).

³⁵⁵ See *EURAM* award, *supra* note 83, paras. 248, 254-255; *Eureko* award, *supra* note 74, para. 276; *Electrabel* award, *supra* note 144, paras. 4.151 and 4.153.

³⁵⁶ *EURAM* award, *supra* note 83, para. 248.

³⁵⁷ The ECJ has placed a high threshold for the ability of member state courts to rely on the *acte clair* doctrine. In *CILFIT*, it held that before member state courts reach the conclusion that there is no reasonable doubt about the correct interpretation of EU law, 'the national court or tribunal must be convinced that the matter is equally obvious to the courts of the other Member States and to the Court of Justice. Only if those conditions are satisfied, may the national court or tribunal refrain from submitting the question to the Court of Justice and take upon itself the responsibility for resolving it'. See Case 283/81, *CILFIT*, ECLI:EU:C:1982:335, para. 16.

infringement proceedings, which again ensures the involvement of the ECJ.³⁵⁸ Taken together, these points provided a basis for the conclusion that the ECJ has no absolute monopoly to preside over EU law related disputes and that investment arbitration is compatible with EU law. What also facilitated the conclusion was that the parties did not invoke EU law arguments on the merits, which implied that the ECJ's jurisdiction was not under threat in the circumstances of the cases.

However, these arguments exclude some of the central dicta of the ECJ over the autonomy of the EU legal order. I will now look at the relevant case law and assess its implications for member state BITs.

5.3. The Autonomy of the EU Legal Order under the Case Law of the ECJ

As is well-known, originally the autonomy of EU law focused on its internal dimension in the sense that the principles of direct effect and primacy of EU law arranged and controlled the relationship of domestic legal orders and EU law in a way that ensured the full effectiveness of EU law within the member states, with the preliminary ruling mechanism ensuring its uniform interpretation. When rationalizing these cornerstones of EU law, the Court emphasized the *sui generis* nature of the EU legal order with a number of oft-quoted characterizations: 'the EEC Treaty has created its own legal system which... became an integral part of the legal systems of the Member States',³⁵⁹ and 'which constituted a new legal order of international law'.³⁶⁰ These remarks already implied that while the EU legal order was a creation of international law, the interpretation and application of its provisions take place under a distinct logic and in isolation of general international law. The implications of the external dimension of the autonomy of EU law only surfaced when the EU became more and more active on the international plane. The EU's external activities had an impact not only on the treaty-making capacity of the member states but it

³⁵⁸ See e.g. *EURAM* award, supra note 83, paras. 259 and 264. In the *Electrabel* arbitration, which was raised under the Energy Charter Treaty (ECT), the tribunal argued that the conclusion of the ECT implies that the EU has 'accepted the possibility of international arbitrations... without any distinction or reservation'. The ECT allows investors to choose between ICSID and non-ICSID arbitration venues, with tribunals possibly convening outside the EU and outside the reach of member state courts and the ECJ. Clearly, the *Electrabel* tribunal reasoned, the conclusion of the ECT implies that the EU has tacitly acknowledged the compatibility of investor-state arbitration with EU law. Both the EU and its member states are parties to the ECT. See *Electrabel* award, supra note 144, para. 4.158.

³⁵⁹ Case 6/64, *Costa v E.N.E.L.*, ECLI:EU:C:1964:66, para. 3 of the summary.

³⁶⁰ Case 26/62, *Van Gend & Loos*, ECLI:EU:C:1963:1, para. 3 of the summary.

also raised questions about the relationship of the autonomy of EU law and dispute settlement mechanisms established in treaties to which the EU was to become party.

5.3.1. Opinion 1/91

Opinion 1/91 concerned the creation of the European Economic Area (EEA) between the member states of the European Free Trade Association (EFTA)³⁶¹ and the EU and its member states.³⁶² The basic idea was to create equal conditions of competition in the area of the EEA. The EEA agreement was to contain textually identical rules with the free movement and competition rules of the EU founding treaties, and an EEA Court was to have jurisdiction over disputes between the contracting states which concerned the interpretation and application of the agreement. Similarly, EU directives and regulations concerning free movement and competition were to be duplicated and implemented by the competent EEA institutions. Article 6 provided that the agreement's provisions were to 'be interpreted in conformity with the relevant rulings' of the ECJ on the corresponding provisions of EU law, but this obligation extended only to case law issued prior to the signing of the EEA agreement.³⁶³ Article 104(1) of the agreement, in turn, stipulated that both the ECJ and the EEA Court were to 'pay due account to the principles laid down' in their respective decisions to ensure the uniform application of the EEA agreement, but this obligation did not extend to the contracting states.³⁶⁴ The EEA Court was to comprise of eight judges, the majority of which were to come from the ECJ, and one of the Protocols to the agreement provided that the EFTA states 'may authorize their courts and tribunals to ask the Court of Justice to express itself on the interpretation of a provision of the agreement'.³⁶⁵ The purpose of these rules was to contribute to achieving 'homogeneity in the interpretation and application of the law [i.e. of the free movement and competition rules] in the EEA'.³⁶⁶

To determine the compatibility of the EEA agreement with EU law, the Court analyzed two broad questions. First, it looked at whether the rules of the agreement achieved the objective of 'homogeneity of the law' and as a second matter the Court examined whether

³⁶¹ These were Austria, Finland, Iceland, Liechtenstein, Norway, Sweden and Switzerland.

³⁶² *Opinion 1/91*, ECLI:EU:C:1991:490.

³⁶³ *Ibid.*, para. 8 (emphasis added). Despite some serious effort, the text of the draft agreement turned out to be 'unGoogleable' so the discussion relies solely on the incomplete references found in the Opinion.

³⁶⁴ *Ibid.*, para. 9.

³⁶⁵ *Ibid.*, para. 11.

³⁶⁶ *Ibid.*, para. 29.

the setting up of the EEA Court undermined 'the autonomy of the Community legal order in pursuing its own particular objectives'.³⁶⁷ To answer the first question, the Court compared the objectives of the EEA agreement with those of EU law.³⁶⁸ In its typically glorified manner, the ECJ held that the EU founding treaties constituted 'the constitutional charter of a Community based on the rule of law', and in particular the principles of primacy and direct effect reflected the sui generis nature of the EU legal order.³⁶⁹ The free movement and competition rules of EU law were part of a 'new legal order for the benefit of which' member states 'have limited their sovereign rights, in ever wider fields'.³⁷⁰ As to its specific objectives, the founding treaties aimed to create a single market and establish a monetary union, and Article 1 of the 1986 Single European Act made it clear that the founding treaties were geared towards achieving 'European unity'.³⁷¹ This meant that rather than being ends in themselves, the free movement and competition rules were 'the only means' by which the single market and other objectives of the founding treaties could be reached.³⁷² The EEA agreement, on the other hand, contained no transfer of sovereign rights to the institutions it was meant to create and the objectives of its provisions paled in comparison to those of EU law. In the Court's view, they concerned the 'application of rules on free trade and competition in economic and commercial relations' between the contracting parties with no higher cause or purpose undergirding them.³⁷³

Because the respective objectives of EU law and the EEA agreement could not but influence the interpretation of the free movement and competition provisions, it was clear for the ECJ that 'homogeneity of the rules of law throughout the EEA is not secured' by identically worded provisions in the two treaties.³⁷⁴ This conclusion was supported by two additional factors. First, as noted, the case law of the ECJ was to be taken into account in the interpretation of the EEA agreement, but this obligation did not extend to case law

³⁶⁷ Ibid., para. 30.

³⁶⁸ Here, the Court invoked Article 31 VCLT, which lays down the general rule of treaty interpretation, namely, that a 'treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose.'

³⁶⁹ *Opinion 1/91*, supra note 362, para. 21.

³⁷⁰ Ibid., para. 21.

³⁷¹ Ibid., para. 17.

³⁷² Ibid., para. 18.

³⁷³ Ibid., paras. 15.

³⁷⁴ Ibid., para. 22.

issued after the signing of the agreement.³⁷⁵ Second, and more generally, the EEA agreement did not expressly recognize the primacy and direct effect of EU law as the contracting states merely agreed to introduce into their national legal orders a statutory provision pronouncing that EEA rules prevail over conflicting domestic law provisions.³⁷⁶ As a result, the Court held that the requirement of complying with its case law, imposed on the contracting parties of the EEA agreement, 'does not extend to [its] essential elements' and the agreement 'cannot secure the objective of homogeneity [in the interpretation and application] of the law throughout the EEA'.³⁷⁷

These points did not yet constitute a finding of incompatibility, but provided a stepping stone to the question of whether the proposed EEA court 'may undermine the autonomy of the Community legal order in pursuing its own particular objectives'.³⁷⁸ The EEA Court was to have jurisdiction over disputes between the contracting parties. Both the EU and its member states were 'contracting parties' of the agreement and the EEA Court was to determine in each case whether it was the EU or the member states or both together that were 'contracting parties' for the purposes of adjudicating a dispute. Such finding hinged not only on the relevant provisions of the EEA agreement but also on the respective competences of the EU and its member states in a given area. Hence, the EEA Court would necessarily have to rule on the division of competences between the EU and its member states in relation to the subject-matter of a dispute brought before it.³⁷⁹ The inference was that this was 'likely adversely to affect the allocation of responsibilities defined in the Treaties and, hence, the autonomy of the Community legal order, respect for which must be assured by the Court of Justice pursuant to Article 164 of the EEC Treaty'.³⁸⁰ That is to say, the ECJ has exclusive jurisdiction to ensure that the 'law is observed' in the interpretation and application of the founding treaties, which includes the power to determine the division of competences between the EU and its member states. The Court also invoked Article 344 TFEU to emphasize the exclusive nature of its jurisdiction in this

³⁷⁵ Article 104(1) of the draft agreement did oblige the ECJ and the EEA Court to 'pay due account' to the case law of the other court without any time limitations, but this obligation did not extend to the contracting parties.

³⁷⁶ *Opinion 1/91*, supra note 362, paras. 26-27.

³⁷⁷ *Ibid.*, para. 28.

³⁷⁸ *Ibid.*, para. 30.

³⁷⁹ *Ibid.*, paras. 32-34.

³⁸⁰ *Ibid.*, para. 35. Article 164 of the EEC Treaty read: 'The Court of Justice shall ensure observance of law and justice in the interpretation and application of this Treaty'. This article is now Article 19(1) TEU, the relevant part of which reads: 'The Court of Justice of the European Union... shall ensure that in the interpretation and application of the Treaties the law is observed.'

regard and the conclusion was that the proposed jurisdiction of the EEA Court was incompatible with EU law.³⁸¹

The second source of incompatibility³⁸² originated in the legal effects of treaties concluded under Article 216 TFEU, under which the EEA agreement would have been 'binding on the institutions of the Community and on member states'.³⁸³ The Court noted that the EEA agreement would become 'an integral part of the Community legal order' and be subject to the preliminary ruling mechanism and infringement proceedings in case the member states or the EU institutions breached its provisions.³⁸⁴ Moreover, the decisions of the EEA Court would bind the latter, including the ECJ, as those decisions also were to become an 'integral part' of the EU legal order. As noted, the EEA Court was obliged to interpret the EEA agreement in conformity with the case law of the ECJ, but this obligation extended only to decisions given prior to the signing of the agreement.³⁸⁵ Although the EEA Court was to interpret the EEA agreement with the objective of homogeneity in mind, it was clear that its interpretations could deviate from those of the ECJ, not only because the objectives of the two regimes were different but because the EEA court was not obliged to follow the ECJ's most recent jurisprudence. Since the (possibly deviating) decisions of the EEA court were binding on the ECJ, the latter held that this 'conditioned' the future interpretation of the EU free movement and competition rules on the rulings of the EEA

³⁸¹ *Ibid.*, paras. 35-36.

³⁸² There was a third source of incompatibility, but as it is not directly relevant in the BIT context it is summarized here. The Court found that the preliminary reference system established in the EEA agreement in respect of the courts of EFTA states was incompatible with EU law. This was so because the Court's answers to the preliminary questions of these courts were to be 'without any binding effects' (paras. 61 and 65). Such advisory role 'would change the nature of the function of the Court of Justice as conceived...by the EEC Treaty' and potentially affect the legal value of the Court's preliminary rulings in the eyes of the courts of EU member states. Further, that ECJ judges were to form a majority in the EEA Court did not reduce the threat which the court system posed to the autonomy of the EU legal order (para. 47). This was because the judges would still have to use 'different approaches, methods and concepts in order to take account of the nature of each treaty and of its particular objectives' (para. 51), indicating that it might be impossible for the judges to approach the legal issues 'with completely open minds' (para. 52).

³⁸³ At the time of the opinion Article 228(2) of the EEC Treaty. The 'conditions' to which the paragraph refers are found in the first part of paragraph 1, which reads as follows: 'Where this Treaty provides for the conclusion of agreements between the Community and one or more States or an international organization, such agreements shall be negotiated by the Commission. Subject to the powers conferred upon the Commission in this field, such agreements shall be concluded by the Council after the Assembly has been consulted in the cases provided for by this Treaty'.

³⁸⁴ *Opinion 1/91*, supra note 362, paras. 37-38.

³⁸⁵ See Article 6 of the EEA agreement (the content of the article remained unchanged in the final version of the agreement). As noted above, Article 104(1) of the agreement stated that both the ECJ and the EEA Court were to 'pay due account to the principles laid down' in their respective decisions so as to ensure the uniform application of the EEA agreement, and unlike in Article 6 this 'paying account' had no temporal limitation. Why the Court did not refer to Article 104(1) in this context is unclear. Yet Article 104(1) only concerned the EU and EEA court systems and did not require the contracting parties to 'pay due account' to the decisions of the courts.

Court, which meant that the 'machinery of courts' established in the EEA agreement was incompatible with what is now Article 19(1) TEU and, more generally, 'with the very foundations of the Community'.³⁸⁶ In other words, had the EEA agreement entered into force as proposed, the Court would not have been in a position to ensure that the 'law is observed' in the interpretation and application of the founding treaties, because the EEA Court could affect the content of EU law in a binding way.

Admittedly, the Court's reasoning is not easy to follow, and commentators have also failed to reach a higher level of clarity on how exactly the EEA court's decisions 'conditioned' the future interpretation of the relevant EU law rules.³⁸⁷ In the hierarchy of EU law international agreements concluded by the EU are inferior to primary law, but superior to secondary law. This appears to mean that the decisions of the EEA court could not bind the ECJ when they concerned the interpretation of EEA provisions that were equivalent to primary law provisions on free movement and competition.³⁸⁸ On the other hand, if the EEA court interpreted EEA rules that duplicated EU acts (directives and regulations in particular), the relevant decisions would have overruled the ECJ's interpretation of the parallel EU acts as they outranked the latter as a matter of EU law. As one commentator put it, the ECJ would have had to take account of the EEA's decisions when interpreting the parallel EU act as those decisions and the EEA agreement outranked secondary law and as the Court had to keep the objective of homogeneity in mind.³⁸⁹ Brandtner, in turn, notes that from the perspective of international law the EU 'could not plead its own "constitutional" order against a failure to comply with EEA rules or their binding interpretation'.³⁹⁰ Be that as it may, what is clear is that the Court held that if a non-EU

³⁸⁶ *Opinion 1/91*, supra note 362, para. 46.

³⁸⁷ As Hix puts it, it 'is not clear from the Opinion on what reasons the Court founded' the conclusion that the EEA court's decisions were binding on the ECJ. See Jan-Peter Hix, 'Indirect Effect of International Agreements: Consistent Interpretation and other Forms of Judicial Accommodation of WTO Law by the EU Courts and the US Courts', *Jean Monnet Working Paper Series* (03/13), p. 98.

³⁸⁸ Analogously, in 1990, the ECJ has held that the decisions of the Turkey-EEC association council were 'directly connected with the Agreement to which they give effect' and 'form an integral part' of EU law 'in the same way as the Agreement itself'. See Case C-192/68, *S. Z. Sevince v. Staatssecretaris van Justitie*, ECLI:EU:C:1990:322, paras. 8-9. For the argument that dispute settlement rulings stemming from agreements to which the EU is party do not form an integral part of the EU legal order, see Hix, 'Indirect Effect of International Agreements', supra note 388, pp. 97-99.

³⁸⁹ See Kirsten Schmalenbach, 'Struggle for Exclusiveness: The ECJ and Competing International Tribunals', in Isabelle Buffard, James Crawford, Alain Pellet and Stephan Wittich (eds.), *International Law Between Universalism and Fragmentation: Festschrift in Honour of Gerhard Hafner* (Martinus Nijhoff, 2008), pp. 1045-1068, at 1048-1049.

³⁹⁰ See Barbara Brandtner, 'The "Drama" of the EEA Comments on Opinions 1/91 and 1/92', 3 *European Journal of International Law* (1992), pp. 300-328, at 309-310 (footnote 55).

court or tribunal's interpretation of EU law has a binding effect on the EU institutions, the ECJ in particular, this poses a threat to the autonomy of EU law.³⁹¹

When the Court's findings are transposed to the BIT context, the essential question is whether BIT arbitration clauses have similar implications as the two aspects of the EEA agreement which led to a finding of incompatibility. In other words, are there situations where arbitral tribunals rule on the division of competences between the EU and its member states? And when arbitral tribunals interpret and apply specific EU law provisions, does this have a similar 'conditioning effect' on those provisions, even if such interpretations (or the provisions of member state BITs) are not binding on the EU institutions? As to the EEA Court's findings on the question of competence, the binding effect of the findings would have been of the *de facto* type in the sense that they would have determined the question of competence in that specific case, even if the findings would not have bound the ECJ as a matter of EU law. One question is whether the decisions of arbitral tribunals can 'bind' the EU institutions in a similar manner when, for example, a tribunal rules on the division of competences between the EU and its member states. Decisions of tribunals are only binding on the disputing parties, but since those decisions are subject to limited review, they may have a *de facto* binding effect in individual cases in the sense that the relevant EU law interpretation is final and affects the outcome of the dispute (this issue is discussed further below).

The Court also connected Article 344 TFEU to the EEA Court's ability to rule on the division of competences between the EU and its member states, which suggests that situations where non-EU courts and tribunals deal with disputes between member states and private parties could fall under the scope of Article 344 TFEU, at least when they address the issue of competence. In sum, what the Court left unclear was whether the autonomy of the EU legal order was threatened already when a non-EU court interprets

³⁹¹ Opinion 1/91 forced the EEA contracting parties to renegotiate the agreement. After a new compromise was reached, the ECJ was approached to ensure that the amended agreement met the requirements laid down in Opinion 1/91. Opinion 1/92 was rendered just four months after the first opinion and the Court found the amended agreement to comply with the conditions established in Opinion 1/91. This 'conditioned' the future interpretation of the EU free movement and competition rules on the rulings of the EEA Court, which meant that the 'machinery of courts' established in the EEA agreement was incompatible with what is now Article 19(1) TEU and, more generally, 'with the very foundations of the Community'. See *Opinion 1/92*, ECLI:EU:C:1992:189. For the present purposes, it is unnecessary to analyze the amendments made to the agreement.

and applies EU law or whether that threat exists only when those interpretations and applications bind the Court and the other EU institutions in one or another way.

5.3.2. Opinion 1/00

Opinion 1/00 concerned the European Common Aviation Area agreement (ECAA), which was to be concluded by the EU (but not by its member states), the EFTA states and a number of Central and Eastern European states. The agreement was to extend the application of the EU air transport rules to the non-EU state parties and this was to be achieved by including in the agreement rules that were essentially similar to those of EU law.³⁹² The agreement established a Joint Committee, the central task of which was to ensure the homogenous interpretation of the ECAA agreement (i.e. to ensure that the air transport rules of the agreement were interpreted and applied in a uniform manner with the corresponding EU rules). The Court began its analysis by making the point that when 'an agreement more clearly separates' its own institutional framework from that of the EU, and when that framework does not affect 'either the exercise by the Community and its institutions of their powers by changing the nature of those powers, or the interpretation of Community law, the autonomy of the Community legal order can be considered to be secure'.³⁹³ At a higher level of abstraction, the Court held that safeguarding 'the autonomy of the Community legal order requires...that the essential character of the powers of the Community and its institutions...remain unaltered'.³⁹⁴

In case of the ECAA agreement, the protection of the autonomy of the EU legal order required 'that the procedures for ensuring uniform interpretation of the rules of the ECAA agreement and for resolving disputes will not have the effect of binding the Community and its institutions, in the exercise of their internal powers, to a particular interpretation of the [air transport] rules of Community law referred to in that agreement'.³⁹⁵ In essence, this requirement echoed the Court's finding in Opinion 1/91 that the EEA Court's decisions would have 'conditioned' the future application of the relevant EU law rules. As the member states were not to become parties to the ECAA agreement, the Joint Committee and the courts of the non-EU contracting states seized of a dispute regarding the

³⁹² *Opinion 1/00*, ECLI:EU:C:2002:231, para. 3.

³⁹³ *Ibid.*, para. 6.

³⁹⁴ *Ibid.*, para. 12.

³⁹⁵ *Ibid.*, para. 13. This was a general principle and not confined to the ECAA context (in para. 11 the Court held that it was important that the EU institutions are not bound by a 'particular interpretation' of the rules of EU law made by the organs established under an agreement to which the EU is party).

interpretation of the air transport provisions were not authorized to assess the respective competences of the EU and its member states in that field.³⁹⁶ This also meant that intra-EU disputes over the 'interpretation of the rules of Community law applicable to air transport will continue to be dealt with exclusively by the machinery [of courts] provided for by the [founding] Treaty'.³⁹⁷ The powers of the Joint Committee extended only to disputes between non-EU states and between those states and the EU. Hence, the proposed dispute settlement mechanism was not in conflict with Article 344 TFEU, and the conclusion was that the ECAA agreement 'will not affect the allocation of powers' between the EU and its member states.³⁹⁸ In other words, the Court's exclusive jurisdiction under Article 344 TFEU was tied more formally to the identity of the disputing parties, whereas in Opinion 1/91 the EEA court's ability to rule on the division of competences of the EU and its member states violated Article 344 TFEU.

The Court also found that while the ECAA agreement had some impact on the powers of the EU institutions, it did 'not alter the essential character of those powers and, accordingly, did not undermine the autonomy of the Community legal order'.³⁹⁹ As to the ECJ's powers, it was empowered to rule on all 'questions concerning the legality of decisions taken by Community institutions' under the ECAA agreement.⁴⁰⁰ This was in line with the Court's exclusive power to review 'the legality of acts of the Community institutions' established under Article 263 TFEU.⁴⁰¹ As to the nature of the ECJ's powers under the ECAA agreement, its decisions flowing from the exercise of those powers were to be binding in all respects. This meant that the ECAA agreement did not change the essential character of the Court's powers nor, to that extent, adversely affected the autonomy of the EU legal order.⁴⁰² The Court waxed eloquently that 'the indispensable conditions for safeguarding the essential character of its powers are satisfied by the provisions of the proposed ECAA Agreement'.⁴⁰³

³⁹⁶ Ibid., para. 16. Arguably, e.g. the Joint Committee could face an argument that the EU institutions do not have competence over a specific segment of air transportation, forcing the Joint Committee to analyze the division of competences under EU law.

³⁹⁷ Ibid., para. 17.

³⁹⁸ Ibid., para. 15.

³⁹⁹ Ibid., para. 21. Here, the Court referred to *Opinion 1/92*, supra note 391, paras. 32 and 41.

⁴⁰⁰ Ibid., para. 24.

⁴⁰¹ Idem.

⁴⁰² Ibid., paras. 25-26. The Court also found that the 'essential character' of the Commission's powers were not affected by the ECAA agreement (see para. 22).

⁴⁰³ Ibid., para. 23.

The second large question related to the ECAA Agreement's mechanisms designed to ensure the uniform interpretation of its provisions. As noted, if decisions taken under those mechanisms had 'the effect of binding the Community and its institutions, in the exercise of their internal powers, to a particular interpretation of the rules of Community law', the autonomy of the EU legal order could be negatively affected.⁴⁰⁴ The Court made a number of points in support of the conclusion that this was not the case. First, the ECAA contracting states had made a general commitment to make their laws compatible with those of EU law in the area of air transport.⁴⁰⁵ Second, the preliminary reference procedure established in the ECAA Agreement, which was similar to the procedure established under Article 267 TFEU, made it clear that the Court's decisions were invariably binding on the referring courts of ECAA member states.⁴⁰⁶ Third, the ECAA Agreement's provisions ensured that the ECJ's relevant case law 'will be adequately taken into account' both by the Joint Committee and the contracting states, and should the former be unable to reach a decision on the homogenous interpretation of the agreement, the matter could be referred to the ECJ for a final and binding decision.⁴⁰⁷ Accordingly, the Court held that the system of legal supervision established under the ECAA Agreement did 'not affect the autonomy of the Community legal order',⁴⁰⁸ as none of its features had a similar conditioning effect as the EEA agreement's provisions would have had.

Generally speaking, arbitral tribunals have no obligation to keep up to date and take account of the ECJ's case law when the disputing parties invoke EU law arguments. Tribunals can of course do so either on their own initiative or by hearing the parties and expert witnesses, but the essential question is whether the general ability of arbitral tribunals to interpret and apply EU law, to be discussed further below, constitutes a problem in light of Opinions 1/91 and 1/00. Situations where the ECJ's rulings are open to different interpretations, or where the Court has not clarified the meaning of specific EU law provisions may arise, and this will compel the tribunals to interpret the relevant rulings and provisions in one or another way. Should arbitral tribunals be able to submit preliminary questions to the ECJ (either directly or through member state courts), this could, arguably, safeguard the uniform interpretation of EU law and the autonomy of the

⁴⁰⁴ Ibid., para. 27.

⁴⁰⁵ Ibid., para. 29.

⁴⁰⁶ Ibid., paras. 30-33.

⁴⁰⁷ Ibid., paras. 34-44.

⁴⁰⁸ Ibid., para. 46.

EU legal order. The problem with this argument is that not only is the access to ECJ highly unlikely under the relevant case law, but that in many situations tribunals will have no access to member state courts and the ECJ, for example, when the tribunal's seat is in a third state. It is noteworthy that in a number of arbitrations the respondent member states suggested that the question of the compatibility of the arbitration clauses with EU law is submitted to the ECJ, but the tribunals rejected the requests in each case.⁴⁰⁹

5.3.3. Opinion 1/09

Opinion 1/09 has been quoted in a number of arbitral awards to make a point about the inapplicability of Article 344 TFEU to investor-state disputes. This opinion concerned the creation of a European and Community Patents Court ('the PC') composed of a court of first instance and court of appeal.⁴¹⁰ In addition to the EU and its member states, a number of third states (from Europe) were to become parties to the agreement. At the outset, the ECJ held that the planned court was compatible with Article 344 TFEU, because the PC's jurisdiction related only to 'disputes between individuals in the field of patents'.⁴¹¹ The *Electrabel* tribunal used this finding to argue that Article 344 TFEU does not apply to any dispute settlement mechanisms 'involving private parties',⁴¹² although the Court's statement (as the quote demonstrates) was much more confined.⁴¹³ But the Court did find the proposed agreement to be incompatible with the founding treaties on a number of grounds, some of which are already familiar. As to Article 19(1) TEU, the Court emphasized that both the ECJ and member state courts act as 'the guardians' of the EU legal order by ensuring that the 'law is observed' in the interpretation and application of the founding treaties.⁴¹⁴ The principle of sincere cooperation obligates the ECJ and member state courts to ensure 'judicial protection of an individual's rights' under EU law, and the preliminary reference mechanism embodies this collaborative relationship.⁴¹⁵ The Court described the

⁴⁰⁹ See e.g. Eureka award, supra note 74, paras. 148 and 242.

⁴¹⁰ *Opinion 1/09*, supra note 354, para. 8.

⁴¹¹ *Ibid.*, para. 63.

⁴¹² *Electrabel* award, supra note 144, para. 4.155.

⁴¹³ See *Opinion 1/09*, supra note 354, para. 63. The paragraph reads as follows: 'Nor can the creation of the PC be in conflict with Article 344 TFEU [formerly Article 292 EC], given that that article merely prohibits Member States from submitting a dispute concerning the interpretation or application of the Treaties to any method of settlement other than those provided for in the Treaties. The jurisdiction which the draft agreement intends to grant to the PC relates *only to disputes between individuals in the field of patents*' (emphasis added).

⁴¹⁴ *Ibid.*, paras. 66 and 69.

⁴¹⁵ *Ibid.*, paras. 68-69.

EU judicial system as 'a complete system of legal remedies and procedures designed to ensure review of the legality of acts of the [EU] institutions'.⁴¹⁶

These features were then contrasted with the characteristics of the PC. As a first matter, the PC was not to be part of the judicial system of the EU provided for in Article 19(1) TEU, as it was 'an organization with a distinct legal personality under international law'.⁴¹⁷ The PC was to replace national courts entirely in the area over which it was to have exclusive jurisdiction and that jurisdiction related to disputes in the 'Community patent field'. This meant that the PC was to 'ensure, in that field, the full application of European Union law and the judicial protection of individual rights under that law'.⁴¹⁸ The Court referred to Opinion 1/91 to remind that the EU is competent, in principle, to enter into an agreement which creates a court 'responsible for the interpretation of its provisions',⁴¹⁹ to Opinion 1/92 to remind that an international agreement concluded with third states may confer new powers to the Court if such conferral 'does not change the essential character of the function of the Court as conceived' in the founding treaties;⁴²⁰ and to Opinion 1/00 to remind that a treaty may also affect the Court's powers if the 'indispensable conditions for safeguarding the essential character of those powers are satisfied and, consequently, there is no adverse effect on the autonomy of the European Union legal order'.⁴²¹

The proposed courts in the referred opinions were to interpret and apply the provisions of the international agreements concerned (and not directly provisions of EU law, apart from the question of competence in the EEA context), whereas the PC was empowered to directly interpret and apply EU law.⁴²² Likewise, some of the proposed courts in the other opinions were mandated to submit preliminary questions to the ECJ, but the powers of member state courts to interpret and apply EU law and to request preliminary rulings were left intact. This was not the case in relation to the PC, which was to replace national courts entirely in the area of its exclusive jurisdiction, and this 'deprivation' extended to the use of the preliminary ruling procedure.⁴²³ According to the draft agreement, the PC was to base

⁴¹⁶ Ibid., para. 70.

⁴¹⁷ Ibid., para. 71.

⁴¹⁸ Ibid., paras. 72-73.

⁴¹⁹ Ibid., para. 74. With reference to *Opinion 1/91*, supra note 362, paras. 40 and 70.

⁴²⁰ Ibid., para. 75. With reference to *Opinion 1/92*, supra note 391, para. 32. This statement related to the proposed non-binding nature of the decisions of the CJEU in the first EEA draft agreement.

⁴²¹ Ibid., para. 76. With reference to *Opinion 1/00*, supra note 392, paras. 21, 23 and 26.

⁴²² Ibid., para. 77.

⁴²³ Idem.

its decisions on the provisions of that agreement, directly applicable EU law and the European Patent Convention.⁴²⁴ The Court construed that the PC was bound to interpret and apply not only the 'future regulation on the Community patent', but also other relevant regulations and directives, including rules on intellectual property, as well as the TFEU's rules on the internal market and competition law.⁴²⁵ In addition, the Court saw that the PC could be called on to interpret and apply 'the fundamental rights and general principles' of EU law and to examine the validity of the acts of EU institutions.⁴²⁶ The draft agreement entailed a preliminary ruling procedure under which both the Court of First Instance and the Court of Appeal were authorized to submit preliminary questions to the ECJ when 'a question of interpretation of the...[founding treaties] or the validity and interpretation of acts of the institutions of the European Community' are raised before them.⁴²⁷ Similarly to Article 267 TFEU, the Court of First Instance was to submit questions when 'necessary', whereas the Court of Appeal 'shall request' the ECJ to decide such questions.⁴²⁸

The Court recognized that it has no jurisdiction to rule on disputes between individuals in the field of patents, as that jurisdiction belongs to national courts.⁴²⁹ However, member states were not entitled to transfer that jurisdiction to a court such as the PC, inasmuch as this would deprive national courts of their power to apply EU law and to use the preliminary reference procedure in the patent field.⁴³⁰ The Court underlined the importance of the preliminary ruling procedure in ensuring that EU law has the same effect in all member states and in all circumstances, and described it as 'indispensable to the preservation of the very nature of the law established by the Treaties'.⁴³¹ For practical purposes, and despite textual differences, the preliminary ruling procedure in the draft agreement was identical to the one established in Article 267 TFEU,⁴³² but this was not enough for the Court, also because there were two more specific problems with the PC

⁴²⁴ Ibid., para. 9.

⁴²⁵ This led the *Electrabel* tribunal to argue that the Court's finding of incompatibility in Opinion 1/09 was not applicable in respect of BIT arbitration clauses, because unlike the Patent Court, investment tribunals settle disputes concerning alleged violations of the ECT or a BIT, and not of EU law, and neither are arbitral tribunals authorized to determine the validity of particular EU acts, as the PC would have. See *Electrabel* award, supra note 144, paras. 4.156-4.157. See also *EURAM* award, supra note 83, para. 263 and *Eureka* award, supra note 74, para. 290.

⁴²⁶ *Opinion 1/09*, supra note 354, para. 78.

⁴²⁷ Ibid., para. 12.

⁴²⁸ Idem.

⁴²⁹ Ibid., para. 80.

⁴³⁰ Idem.

⁴³¹ Ibid., paras. 82-85.

⁴³² Ibid., para. 20.

system. The first problem stemmed from the fact that under EU law member states are obligated to compensate damages (on certain conditions) that individuals incur as a result of violations of EU law, and this includes the obligation to compensate damages caused by decisions of judicial bodies. The second problem related to the fact that under EU law the Commission can start infringement proceedings against a member state if the decisions of its domestic courts violate EU law.⁴³³ In contrast, if the PC were to render decisions that violate EU law, those decisions 'could not be the subject of infringement proceedings', nor cause financial liability for any member state.⁴³⁴ Put differently, under the draft agreement the ECJ was not in a position to judicially review the decisions of the PC, and individuals incurring damages as a result of the PC's decisions (which violate EU law) could not receive compensation.

It is uncertain whether the PC court system would have been incompatible with EU law even in the absence of these two last points. On the one hand, the Court held categorically that member states 'cannot confer the jurisdiction' to resolve patent disputes on the PC, because this would deprive member state courts of their task to implement EU law and thereby 'of the power...or, as the case may be, the obligation, to refer questions for a preliminary ruling in the field concerned'.⁴³⁵ On the other hand, the Opinion's substantive part emphasized that the cooperation between member state courts and the ECJ ensured the 'judicial protection of an individual's rights' and constituted 'a complete system of legal remedies and procedures designed to ensure review of the legality of acts of the [EU] institutions.'⁴³⁶ Since the PC's decisions were not subject to such review, and since the rights of affected individuals were not adequately protected, it is arguable that these shortcomings rendered the proposed agreement incompatible with the autonomy of the EU legal order, and not the conferral of jurisdiction alone. The Court summarized its position and held that the envisaged PC system 'would deprive' national courts 'of their powers in relation to the interpretation and application' of EU law and the ECJ of 'its powers to reply, by preliminary ruling, to questions' referred by the former. This, in turn, 'would alter the essential character of the powers which the Treaties confer' on EU institutions and on the

⁴³³ Ibid., paras. 86-87.

⁴³⁴ Ibid., para. 88.

⁴³⁵ Ibid., para. 80.

⁴³⁶ Ibid., paras. 68-70.

member states, those powers being 'indispensable to the preservation of the very nature of European Union law'.⁴³⁷

BIT arbitration clauses have no impact on the powers of member state courts or the ECJ, although many BITs contain so called fork-in-the-road clauses, which stipulate that if an investor takes a dispute to arbitration, he can no longer resort to remedies available under national law (and vice versa), but it is unclear to what extent this exclusion extends to remedies investors may have under EU law. Be that as it may, it is useful to say a few words on the Court's finding that the PC's jurisdiction was not in conflict with Article 344 TFEU, because the 'jurisdiction which the draft agreement intends to grant to the PC relates only to disputes between individuals in the field of patents'.⁴³⁸ Read literally, this finding has no direct relevance for answering the question of whether BIT arbitration clauses are compatible with Article 344 TFEU, because BIT disputes can in principle relate to any field of EU law and always include a member state as a disputing party. Neither does the Court's finding answer the question of whether Article 344 TFEU reflects a more general principle, as argued by the Commission, according to which member states may not conclude treaties authorizing private parties to bring claims against them before non-EU courts and tribunals in respect of disputes involving questions of EU law.

Similarly, and as already noted, there clearly are situations where the decisions of arbitral tribunals are outside the reach of member state courts and the ECJ. While there is variation in the content of arbitration clauses, most BITs allow investors to choose between ICSID and other arbitration institutions, and the seat of a tribunal may well be outside the EU irrespective of the arbitration rules that govern the proceedings. When an arbitration takes place outside the EU, the case can end up before a member state court only at the enforcement stage, and the New York and ICSID conventions provide very limited grounds for reviewing the content of arbitral awards. Likewise, there may be situations where the disputing parties comply with the tribunal's decisions, including the final award, in which case the tribunal's interpretation of the relevant EU law provisions is not subject to review under the preliminary ruling procedure. Again, the question is whether the fact that arbitral tribunals may interpret and apply EU law 'alter the essential character of the powers' of member state courts and the ECJ as envisaged in Article 267 TFEU, because,

⁴³⁷ Ibid., para. 89.

⁴³⁸ Ibid., para. 63.

first, the latter are excluded from reviewing the 'correctness' of those interpretations in a number of situations and, second, because tribunals may have to rule on the division of competences between the EU and its member states, which led to a finding of incompatibility in Opinion 1/91.

5.3.4. Opinion 2/13⁴³⁹

The draft agreement concerning the accession of the EU to the European Convention on Human Rights (ECHR)⁴⁴⁰ was the result of lengthy negotiations between the EU Commission and the European Council, with the official history of the EU's accession having started in 1979 when the Commission drafted a memorandum on the topic.⁴⁴¹ In Opinion 2/94, the ECJ had held that the EU had no competence to become a party to the ECHR, but this deficiency was resolved through the adoption of Article 6(2) TEU, which provides that the 'Union shall accede to the European Convention for the Protection of Human Rights and Fundamental Freedoms' on the condition that the accession does not affect 'the Union's competences as defined in the Treaties'. In addition to Article 6(2) TEU, one of the protocols to the TFEU lists a number of other conditions to the accession; the accession agreement has to ensure that the 'specific characteristics of the EU and EU law' are preserved; the accession may not affect the competences of the EU or the powers of its institutions, and the accession agreement may not affect Article 344 TFEU.⁴⁴² In its lengthy analysis extending to over hundred paragraphs, the Court found the draft accession agreement to be incompatible with Article 6(2) TEU and Protocol No (8) on a number of grounds.⁴⁴³

As a first matter, the Court laid down the groundwork for its findings by outlining the contours of the 'constitutional framework' of the EU legal order, which instructs and

⁴³⁹ *Opinion 2/13*, ECLI:EU:C:2014:2454.

⁴⁴⁰ European Convention for the Protection of Human Rights and Fundamental Freedoms, as amended by Protocols Nos. 11 and 14, 213 UNTS 222.

⁴⁴¹ For this early history, see Walther Michl, *Die Überprüfung des Unionsrechts am Maßstab der EMRK* (Mohr Siebeck, 2014), pp. 51-65.

⁴⁴² Protocol (No 8) relating to Article 6(2) of the Treaty on European Union on the accession of the Union to the European Convention on the Protection of Human Rights and Fundamental Freedoms, OJ C 326, 26.10.2012, p. 273. This Protocol has the same legal value as the founding treaties.

⁴⁴³ Given the length of the analysis and the many nuances that each of the Court's findings entail, I have excluded some parts of the Court's reasoning to maintain a sufficient level of clarity and generality. I will not provide a critique the Court's findings, as such concerns are outside the scope of this study, but I will refer to some academic sources which discuss some of the issues and questions that the Court's findings raise.

controls the interpretation and application of fundamental rights within the EU.⁴⁴⁴ Some aspects of this framework are familiar by now. The founding treaties had created 'a new legal order', with its own 'founding principles' and a 'particularly sophisticated institutional structure', which have 'consequences as regards the procedure for and conditions of accession to the ECHR'.⁴⁴⁵ Primacy of EU law and its direct effect, and other 'essential characteristics of EU law', have created a 'structured network of principles, rules and mutually interdependent legal relations linking' the EU and its member states, and the member states with each other, to a 'process of creating an ever closer union'.⁴⁴⁶ From this the Court inferred that each member state shares with the other member states 'a set of common values on which the EU is founded', and that a 'mutual trust' exists between the member states that 'those values will be recognized and, therefore, that the law of the EU that implements them will be respected'.⁴⁴⁷ These values have two distinct sources: first, Article 2 TEU stipulates that the EU is founded on freedom, democracy, equality, the rule of law and respect for human rights, and second, as the Charter of the Fundamental Rights of the EU (the Charter) is now an integral part of the Union's legal order, all acts of the EU institutions must be compatible with the rights enshrined therein, as Article 6(1) TEU provides that the Charter has 'the same legal value as the Treaties'.⁴⁴⁸

The autonomy of the EU legal order requires that the fundamental rights enshrined in the Charter are interpreted and applied in isolation of both member states' legal orders and international law, and the Court referred to *Kadi* where it had held that its power to review acts of the EU institutions in light of fundamental rights 'is not to be prejudiced by an international agreement'.⁴⁴⁹ Other fundamental rules of EU law require similarly autonomous interpretation, and the preliminary ruling procedure in particular was designed to ensure that these rules receive a uniform interpretation.⁴⁵⁰ The Court invoked the principle of sincere cooperation to make the point that member states are under an obligation to 'ensure, in their respective territories, the application and respect for EU law',

⁴⁴⁴ In the Court's words: 'Fundamental rights, as recognised in particular by the Charter, must therefore be interpreted and applied within the EU in accordance with the constitutional framework referred to in paragraphs 155 to 176 above'. *Opinion 2/13*, supra note 439, para. 177.

⁴⁴⁵ *Ibid.*, para. 158.

⁴⁴⁶ *Ibid.*, para. 167.

⁴⁴⁷ *Ibid.*, para. 168.

⁴⁴⁸ *Ibid.*, para. 169.

⁴⁴⁹ *Ibid.*, para. 170. The Court referred to Case 11/70, *Internationale Handelsgesellschaft*, ECLI:EU:C:1970:114, para. 4, and to *Kadi & Al-Bakaraat*, supra note 339, paras. 281-285, the quote is from para. 316.

⁴⁵⁰ *Ibid.*, paras. 172 and 174.

and national courts are obliged to safeguard 'the full application of EU law' and to provide 'judicial protection of an individual's rights under that law'.⁴⁵¹ The preliminary ruling procedure was central to achieving the 'uniform interpretation of EU law', which entailed ensuring 'its consistency, its full effect and its autonomy as well, ultimately, the particular nature of the law established by the Treaties'.⁴⁵²

At the beginning of its analysis of the ECHR accession agreement, the Court postulated two broad questions which reflected the preconditions of the EU's accession: first, is the proposed agreement liable to have a negative impact on the specific characteristics of EU law or the autonomy of EU law in the area of fundamental rights protection; and second, do the institutional and procedural mechanisms proposed in the accession agreement ensure that the requirements for the Union's accession are satisfied.⁴⁵³ Pursuant to Article 216(2) TFEU, the provisions of the ECHR were to bind the EU institutions as of accession, and those institutions, including the ECJ, would become 'subject to external control to ensure the observance of the rights and freedoms' established in the ECHR.⁴⁵⁴ While in principle the institutions of the EU are authorized to conclude an agreement having such binding effects, the Court reminded that an international agreement can 'affect its own powers only if the indispensable conditions for safeguarding the essential character of those powers are satisfied and, consequently, there is no adverse effect on the autonomy of the EU legal order'.⁴⁵⁵ In particular, the decisions of the European Court of Human Rights (ECtHR) 'must not have the effect of binding the EU and its institutions, in the exercise of their internal powers, to a particular interpretation of the rules of EU law'.⁴⁵⁶

As to Article 344 TFEU, the Court construed that the obligation of member states to respect its exclusive jurisdiction was a 'specific expression' of the principle of sincere cooperation established in Article 4(3) TEU.⁴⁵⁷ Transposed to the ECHR context, the implication was that when a dispute arises between member states or between member states and the EU over the compatibility of a given EU law instrument with the ECHR, the

⁴⁵¹ Ibid., para. 175. With reference to *Opinion 1/09*, supra note 354, para. 68.

⁴⁵² Ibid., para. 176. With reference to *Opinion 1/09*, supra note 354, paras. 67 and 83.

⁴⁵³ Ibid., para. 178.

⁴⁵⁴ Ibid., paras. 180-181.

⁴⁵⁵ Ibid., paras. 182-183. With reference to *Opinion 1/00*, supra note 392, paras. 21, 23 and 26; and *Opinion 1/09*, supra note 355, para. 76).

⁴⁵⁶ Ibid., para. 184 (emphasis added). With reference to *Opinion 1/91*, supra note 362, paras. 30-35; and *Opinion 1/00*, supra note 392, para. 13.

⁴⁵⁷ Ibid., paras. 201-202.

ECJ has exclusive jurisdiction over the dispute.⁴⁵⁸ Article 55 of the ECHR provides that the contracting states agree not to 'avail themselves' of other dispute settlement mechanisms when their dispute concerns the interpretation or application of the ECHR.⁴⁵⁹ While the draft agreement provided that proceedings before the ECJ were excluded from the scope of Article 55 ECHR,⁴⁶⁰ the Court saw that it was 'not sufficient to preserve' its exclusive jurisdiction under Article 344 TFEU.⁴⁶¹ For the Court, the draft agreement only reduced 'the scope of the obligation laid down by Article 55 ECHR' and made it possible that either the EU institutions or the member states submit a dispute to the ECtHR which concerns the compatibility of an EU act with the ECHR.⁴⁶² As Article 344 TFEU was designed to ensure that the specific characteristics and objectives of EU law are taken account of when disputes over its contents arise, only an explicit exclusion of the jurisdiction of the ECtHR over disputes between member states and between member states and the EU 'in relation to the application of the ECHR within the scope *ratione materiae* of EU law would be compatible with Article 344 TFEU'.⁴⁶³

The second problem of the draft agreement related to the 'co-respondent mechanism'. The purpose of the mechanism was to ensure that proceedings 'by non-Member States and individual applications [to the ECtHR] are correctly addressed to Member States and/or the Union as appropriate'.⁴⁶⁴ In other words, the mechanism strove to ensure that claims against the EU and/or its member states were addressed to the correct respondent, and this attribution had to be achieved in a way that preserves the 'specific characteristics of the

⁴⁵⁸ *Ibid.*, para. 204.

⁴⁵⁹ The full text of Article 55 ECHR reads: 'Exclusion of other means of dispute settlement. The High Contracting Parties agree that, except by special agreement, they will not avail themselves of treaties, conventions or declarations in force between them for the purpose of submitting, by way of petition, a dispute arising out of the interpretation or application of this Convention to a means of settlement other than those provided for in this Convention.'

⁴⁶⁰ See Article 5 of the Draft revised agreement on the accession of the European Union to the Convention for the Protection of Human Rights and Fundamental Freedoms (hereinafter 'draft agreement'). The draft agreement is included in the Final Report to the Steering Committee for Human Rights of the Council of Europe, which is available at [http://www.coe.int/t/dghl/standardsetting/hrpolicy/Accession/Meeting_reports/47_1\(2013\)008rev2_EN.pdf](http://www.coe.int/t/dghl/standardsetting/hrpolicy/Accession/Meeting_reports/47_1(2013)008rev2_EN.pdf) (accessed 14 January 2017).

⁴⁶¹ *Opinion 2/13*, supra note 439, para. 206.

⁴⁶² *Ibid.*, para. 207. Article 33 ECHR reads: 'Inter-State cases. Any High Contracting Party may refer to the Court any alleged breach of the provisions of the Convention and the Protocols thereto by another High Contracting Party.' For a critique of this position, see Stian Øby Johansen, 'The Reinterpretation of TFEU Article 344 in Opinion 2/13 and its Potential Consequences', 6 *German Law Journal* (2015), pp. 169-178.

⁴⁶³ *Ibid.*, para. 213. For an analysis and critique of the Court's approach, see Piet Eeckhout, 'Opinion 2/13 on EU Accession to the ECHR and Judicial Dialogue: Autonomy or Autarky?', 38 *Fordham International Law Journal* (2015), pp. 955-992, at 972-979.

⁴⁶⁴ Protocol (No 8), supra note 442, Art. 1.

Union and Union Law'.⁴⁶⁵ The ECJ noted that the determination of the correct respondent depends on the division of powers between the EU and its member states and on the criteria by which an act or omission is attributed between them.⁴⁶⁶ Such determination, in the words of the Court, 'necessarily presupposes an assessment of EU law'.⁴⁶⁷ Further, Article 3(5) of the draft agreement concerned situations where either the EU or a member state requests to become a co-respondent. In such situations, the ECtHR was to 'seek the views of all parties to the proceedings' before deciding whether the conditions laid down for the use of the co-respondent mechanism were met.⁴⁶⁸ Likewise, the draft agreement provided that the respondent and co-respondent were jointly responsible for a violation of the ECHR, but the ECtHR was empowered to decide that only one of them bears responsibility.⁴⁶⁹ Both type of decisions would necessarily entail an assessment of EU law provisions 'governing the division of powers between the EU and its member states', as would the resolution of the question of attribution.⁴⁷⁰ Hence, the conclusion was that the co-respondent mechanism would 'interfere' or 'risk adversely affecting the division of powers' between the EU and its member states, and the specific characteristics of the EU and EU law would not be preserved as Article 1 of Protocol No (8) required.⁴⁷¹ This was similar to Opinion 1/91, where the Court held that the EEA court's power to determine whether the Community or a member state was the correct respondent in a specific case was 'likely adversely to affect...the autonomy of the Community legal order'.⁴⁷²

The third issue of concern related to the 'prior involvement' procedure.⁴⁷³ To understand the Court's concern, it is necessary to say a few words on the procedure's background. Generally speaking, national courts ensure that individuals enjoy the rights that EU law provides. Should an individual wish to challenge an EU act on the ground that it violates his fundamental rights, the individual can raise a claim before a national court, which may

⁴⁶⁵ Ibid., Art 1(b).

⁴⁶⁶ *Opinion 2/13*, supra note 439, para. 221.

⁴⁶⁷ Idem.

⁴⁶⁸ Art. 3(5) of the draft agreement, supra note 460.

⁴⁶⁹ Such decision was to be taken 'on the basis of the reasons given by the respondent and the co-respondent, and [after] having sought views of the applicant'. See Article 3(7) of the draft agreement, supra note 460.

⁴⁷⁰ *Opinion 2/13*, supra note 439, para. 230.

⁴⁷¹ Ibid., paras. 225, 231 and 235.

⁴⁷² *Opinion 1/91*, supra note 362, para. 35.

⁴⁷³ For a discussion and analysis of the procedure, see Roberto Baratta, 'Accession of the EU to the ECHR: The Rationale for the ECJ's Prior Involvement Mechanism', 50 *Common Market Law Review* (2013), pp. 1305-1332.

lead to the involvement of the ECJ through the preliminary ruling procedure.⁴⁷⁴ When a member state court submits a relevant preliminary question, the ECJ then assesses the validity of the EU act in light of fundamental rights provisions or, alternatively, provides an interpretation of a primary law provision that is most consistent with fundamental rights protection (the Court has no power to rule on the validity of primary law). The prior involvement procedure was meant to apply in situations where the ECJ had not previously given such a ruling on a provision of EU law which an applicant had invoked before the ECtHR. The draft agreement's text implied that the ECtHR was to determine whether the ECJ had ruled 'on the same question of law as that at issue in the proceedings before the ECtHR', and, if not, the Court was to provide an assessment of that question.⁴⁷⁵ For the ECJ, this was equal to granting to the ECtHR 'jurisdiction to interpret' its case law.⁴⁷⁶ Similarly, the draft agreement excluded from the prior involvement procedure the interpretation of secondary law acts, which meant the ECtHR alone was to interpret such acts.⁴⁷⁷ This exclusion 'most certainly' breached the Court's exclusive jurisdiction 'over the definitive interpretation of EU law'.⁴⁷⁸ In other words, if an individual files an application before the ECtHR and argues that a provision of secondary law violates his rights under the ECHR, the Strasbourg court was to interpret that provision in light of the ECHR however ambiguous the provision's text and without the ECJ's involvement. This affected 'the competences of the EU and the powers of the Court of Justice', and the general

⁴⁷⁴ Individuals can initiate proceedings before the ECJ against EU acts addressed to them or against acts which are 'of direct and individual concern to them, and against a regulatory act which is of direct concern to them and does not entail implementing measures'. See Article 263(4) TFEU.

⁴⁷⁵ *Opinion 2/13*, supra note 439, para. 238. Article 3(6) of the draft agreement is the relevant provision in this regard and it reads as follows: 'In proceedings to which the European Union is a co-respondent, if the Court of Justice of the European Union has not yet assessed the compatibility with the rights at issue defined in the Convention or in the protocols to which the European Union has acceded of the provision of European Union law as under paragraph 2 of this article, sufficient time shall be afforded for the Court of Justice of the European Union to make such an assessment, and thereafter for the parties to make observations to the Court. The European Union shall ensure that such assessment is made quickly so that the proceedings before the Court are not unduly delayed. The provisions of this paragraph shall not affect the powers of the Court.' For a discussion of this aspect of the procedure, see Baratta, 'Accession of the EU to the ECHR', supra note 473, pp. 1313-1316.

⁴⁷⁶ *Ibid.*, para. 239.

⁴⁷⁷ The draft explanatory report of the draft agreement characterized the CJEU's assessment powers in the following terms: 'Assessing the compatibility with the Convention shall mean to rule on the validity of a legal provision contained in acts of the EU institutions, bodies, offices or agencies, or on the interpretation of a provision of the TEU, the TFEU or of any other provision having the same legal value pursuant to those instruments.' See para. 66 of the Draft explanatory report to the Agreement on the Accession of the European Union to the Convention for the Protection of Human Rights and Fundamental Freedoms (Appendix 5 in the Final Report to the Steering Committee for Human Rights, see supra note 460).

⁴⁷⁸ *Opinion 2/13*, supra note 439, paras. 242-246.

conclusion was that the prior involvement procedure does not preserve 'the specific characteristics of the EU and EU law'.⁴⁷⁹

The Court also took issue with the ECtHR's powers to review EU acts adopted in the area of Common Foreign and Security policy, but there is no need to elaborate on the Court's analysis because it was by and large analogous to the analysis in Opinion 1/09.⁴⁸⁰ Many of the Court's findings were fundamentally similar to those of the previous opinions as the numerous cross-references also testify. The requirement of preserving the 'specific characteristics' of EU law stemmed from Protocol (No 8), but in substantive terms it is identical with the criteria established in the previous opinions in respect of the autonomy of the EU legal order. Similar to Opinion 1/91, Opinion 2/13 raises the question of whether the possibility that arbitral tribunals will have to assess the division of powers between the EU and its member states for the purposes of attribution breaches the autonomy of the EU legal order, also because such decisions are not necessarily subject to review under the preliminary ruling procedure. The Court's take on the prior involvement procedure, in turn, reminds that arbitral tribunals may have to interpret EU law provisions, the meaning of which the ECJ has not clarified, and the question is whether this possibility breaches, by analogy, the exclusive jurisdiction of the Court 'over the definitive interpretation of EU law', as it may be excluded from reviewing tribunals' interpretations.

⁴⁷⁹ Ibid., paras. 247-248. For the argument that the Court's approach on the co-respondent mechanism and prior involvement procedure are 'well founded', see Daniel Haberstem, "'It's the Autonomy, Stupid!' A Modest Defense of Opinion 2/13 on the EU Accession to the ECHR, and the Way Forward", 6 *German Law Journal* (2015), pp. 105-146, at 115-117.

⁴⁸⁰ The jurisdiction of the ECJ over the Common Foreign and Security Policy (CFSP) is explicitly limited in the founding treaties, but the Court has not ruled on the scope of that jurisdiction. Yet, for the Court, it was clear that 'certain acts adopted in the context of the CFSP fall outside the ambit of judicial review by the Court of Justice'. As a result of the EU's accession, the ECtHR would have jurisdiction to decide whether certain CFSP acts are compatible with the ECHR, while the Court could not review their legality under EU law for lack of jurisdiction. The ECJ referred to Opinion 1/09 and held that the competence to judicially review particular EU acts 'cannot be conferred exclusively on an international court which is outside the institutional and judicial framework of the EU'. The conclusion was that the draft agreement failed 'to have regard to the specific characteristics of EU law with regards to the judicial review of acts, actions or omission on the part of the EU in CFSP matters'. Although the ECJ had no competence to review certain CFSP acts, the ECtHR could not be placed in a position where from it is authorized to interpret such acts so as to determine their compatibility with the ECHR. See *ibid.*, paras. 249-252, 254, 256-257. On the last finding, Peers argues that this finding means, by analogy, 'that it would also breach EU law for Member States to bring a CFSP dispute to the International Court of Justice, or indeed any other international court or tribunal, although presumably national courts could still have jurisdiction.'. See Steve Peers, 'The EU's Accession to the ECHR: The Dream Becomes a Nightmare', 6 *German Law Journal* (2015), pp. 213-222, at 220.

5.3.5. The MOX Plant Judgment

The underlying dispute in *MOX Plant* concerned the protection and preservation of the marine environment. Ireland had brought an arbitral claim against the UK for alleged breaches of several provisions of the United Nations Convention on the Law of the Sea (UNCLOS/Convention), which led the Commission to start infringement proceedings against Ireland.⁴⁸¹ Both the EU and its member states are parties to UNCLOS and had competences over the subject-matter of UNCLOS. The Commission's first argument was that the provisions of the Convention whose breach Ireland had invoked before the UNCLOS tribunal fell within the competence of the EU.⁴⁸² Hence, Ireland had breached Article 344 TFEU by raising the arbitral claim as the ECJ had exclusive jurisdiction over the dispute as it concerned the interpretation and application of EU law (i.e. the UNCLOS provisions over which the EU had competence). The Court agreed and noted that the Convention forms an integral part of the EU legal order once the Union had become a party and it was binding on the EU institutions and the member states under what is now Article 216(2) TFEU. Similarly, the Convention's provisions on which Ireland relied before the UNCLOS tribunal came within the scope of Community competence, and the Court 'has jurisdiction to deal with disputes relating to the interpretation and application of those provisions and to assess a Member State's compliance with them'.⁴⁸³ The Court also referred to Opinions 1/91 and 1/00 and repeated the point that 'an international agreement cannot affect the allocation of responsibilities defined in the Treaties and, consequently, the autonomy of the Community legal system'.⁴⁸⁴ What allowed preserving autonomy in the UNCLOS context was Article 282 of the Convention which provides that the contracting states can submit a dispute concerning its interpretation and application to another judicial body when they had agreed to do so in a 'general, regional or bilateral agreement or otherwise', and in such cases that other procedure 'shall apply in lieu of the procedures provided' in the Convention. In other words, the Convention authorized other courts and tribunals to settle disputes stemming from UNCLOS, and this allowed the ECJ

⁴⁸¹ *MOX Plant*, supra note 348. Ireland had also raised a claim against the UK under the 1992 Convention for the Protection of the Marine Environment of the North-East Atlantic (OSPAR Convention), but the OSPAR tribunal had decided the case in favor of the UK before the Commission initiated the proceedings before the CJEU. For a discussion of this part of the *MOX Plant* dispute, see Yuval Shany, 'The First MOX Plant Award: The Need to Harmonize Competing Environmental Regimes and Dispute Settlement Procedures', 17 *Leiden Journal of International Law* (2004), pp. 815-827.

⁴⁸² *MOX Plant*, supra note 348, para. 60.

⁴⁸³ *Ibid.*, para. 121.

⁴⁸⁴ *Ibid.*, para. 123.

to hold that 'the system for the resolution of disputes set out in the EC Treaty must in principle take precedence over' the UNCLOS system.⁴⁸⁵

As to the scope of Article 344 TFEU, the Court noted that the dispute was between two member states and concerned 'an alleged failure to comply' with EU law obligations based on UNCLOS provisions, which implied that it was 'clearly covered by one of the methods of dispute settlement established' by the founding treaties 'within the terms' of Article 344 TFEU, namely, the procedure set out in what is now Article 259 TFEU.⁴⁸⁶ Similarly, that the arbitral proceedings were a form of dispute settlement in the meaning of Article 344 TFEU was clear on the basis of Article 296 UNCLOS which provided that decisions of UNCLOS tribunals 'shall be final and shall be complied with by all the parties to the dispute'. BITs also provide that arbitral awards are final and binding on the parties, so it seems evident that investment arbitration qualifies as a method of dispute settlement in the meaning of Article 344 TFEU, on the assumption that it applies to investment arbitration as well. The question of competence was also central to the Court's findings; if the EU had had no competence over the UNCLOS provisions which Ireland had invoked, the dispute between Ireland and the UK would not have fallen under the ECJ's exclusive jurisdiction. The Court acknowledged that some aspects of the dispute between Ireland and the UK might 'fall outside its jurisdiction',⁴⁸⁷ but Article 282 of the Convention allowed it to bypass this dilemma and made it unnecessary to delineate the exact division of competences. But the central question is whether the existence of EU competence was relevant for the Court's brief remarks on the autonomy of EU law? In the *Open Skies* judgments, it was unclear whether the Court's finding of discrimination hinged on the existence of EU competence, whereas in *MOX Plant* the question is whether the issue of autonomy became relevant because of the EU's competence over the UNCLOS provisions that Ireland had invoked before the UNCLOS tribunal.

To answer this question, it is necessary look at the Commission's second head of complaint in *MOX Plant*. Ireland had invoked a number of EU law instruments before the UNCLOS tribunal, and the Commission argued that 'the submission by Ireland of instruments of

⁴⁸⁵ Ibid., para. 125.

⁴⁸⁶ Ibid., para. 128. The first paragraph of Article 259 TFEU provides that a 'Member State which considers that another Member State has failed to fulfil an obligation under the Treaties may bring the matter before the Court of Justice of the European Union'.

⁴⁸⁷ See *ibid.*, para. 135.

Community law for interpretation and application by the Arbitral Tribunal amounts to a breach' of Article 344 TFEU.⁴⁸⁸ The UK Government intervened to support the Commission's case and argued, first, that Ireland's arguments before the UNCLOS tribunal concerned 'the interpretation to be given to specific provisions' of (inter alia) two directives and, second, that Ireland had contended that the UK's conduct 'was incompatible with certain Community-law obligations' that it had under these two directives and other relevant EU law instruments.⁴⁸⁹ There was a clear substantive overlap between the UNCLOS provisions and the EU instruments that Ireland invoked; for example, Ireland had referred to Directive 85/337 before the UNCLOS tribunal to provide a reference point to the interpretation of Article 206 UNCLOS. That directive provided that the member states shall carry out an impact assessment of 'projects likely to have significant effects on the environment', whereas Article 206 UNCLOS provided that when the contracting states 'have reasonable grounds for believing that planned activities under their jurisdiction or control may cause substantial pollution of or significant and harmful changes to the marine environment, they shall, as far as practicable, assess the potential effects of such activities on the marine environment'.⁴⁹⁰

Ireland argued that the relevant instruments of EU law were invoked solely 'as non-binding elements of fact' with the purpose of assisting the interpretation of the relevant UNCLOS provisions 'by indicating how those terms are understood' under EU law.⁴⁹¹ Ireland argued that it was not requesting the UNCLOS tribunal to assess whether the UK had breached the EU law instruments, and claimed that its references to them were an instance of *renvoi*, 'a frequently used juridical technique designed to guarantee the harmonious coexistence of rules deriving from different legal orders'.⁴⁹² In other words, Ireland argued that the UNCLOS provisions which the UK had allegedly breached should be understood in an analogous fashion to the corresponding provisions of the EU law instruments, and in that

⁴⁸⁸ *MOX Plant*, supra note 348, para. 140. These instruments included Council Directive 85/337/EEC of 27 June 1985 on the assessment of the effects of certain public and private projects on the environment, OJ L 175, 5.7.1985, pp. 40-48, and Council Directive 90/313/EEC of 7 June 1990 on the freedom of access to information on the environment, OJ L 158, 23.6.1990, pp. 56-58.

⁴⁸⁹ *Ibid.*, paras. 142-143.

⁴⁹⁰ See Article 2(1) of Council Directive 85/337/EEC of 27 June 1985 on the assessment of the effects of certain public and private projects on the environment, OJ L 175, 5.7.1985, pp. 40-48 (the directive is no longer in force).

⁴⁹¹ *MOX Plant*, supra note 348, para. 144. In other words, the EU law instruments and UNCLOS contained similarly worded provisions and Ireland strove to show how the text of the former are understood under EU law.

⁴⁹² *Ibid.*, para. 145. See also Case C-459/03, *Commission v Ireland*, Opinion of AG Maduro, ECLI:EU:C:2006:42, para. 45.

sense they were part of the factual evidence presented to the tribunal. However, the ECJ concurred with the Commission and the UK. For the Court, it was clear that Ireland invoked the EU law instruments pursuant to Article 293 UNCLOS, which provided that the arbitral tribunal 'shall apply this Convention and other rules of international law not incompatible with this Convention'. In this light, the instruments were raised not only to elucidate the meaning of the relevant UNCLOS provisions, but also 'as rules of international law to be applied by the Arbitral Tribunal pursuant to Article 293 of the Convention'.⁴⁹³ While Ireland expressly denied that it had invited the tribunal to determine whether the UK had breached the EU law instruments, the Court held that Ireland's submissions were made to receive a 'declaration' that the UK had violated the instruments, and such declaration necessarily hinged on the interpretation and application of those instruments by the UNCLOS tribunal.⁴⁹⁴ This breached 'the exclusive nature of the Court's jurisdiction' under Article 344 TFEU as the instruments came within the scope of EU law in the meaning of that article.

The Court did not stop there. It continued by noting that the manner in which Ireland had acted at the UNCLOS proceedings (i.e. by invoking the EU law instruments), 'involve a manifest risk that the jurisdictional order laid down in the Treaties and, consequently, the autonomy of the Community legal system may be adversely affected'.⁴⁹⁵ Ireland's assurance that it was not requesting the UNCLOS tribunal to examine whether the UK had breached EU law did not remove this 'manifest risk', and the existence of such risk rendered 'entirely irrelevant the fact that Ireland may have called on the Arbitral Tribunal to apply Community law by way of *renvoi* or by recourse to any other technique'.⁴⁹⁶ After the Court's judgment, Ireland withdrew its claim and the UNCLOS tribunal terminated the proceedings accordingly.⁴⁹⁷ One important observation is that the question of competence appeared to be irrelevant to the Court's general conclusion on the second head of complaint (including to its remarks on the issue of autonomy), whereas in relation to the other heads of complaint it was central.⁴⁹⁸ Neither did the Court refer to the fact that the EU is an UNCLOS contracting party alongside its member states when making the conclusion that

⁴⁹³ Ibid., para. 149.

⁴⁹⁴ Ibid., para. 151.

⁴⁹⁵ Ibid., para. 154.

⁴⁹⁶ Ibid., paras. 155-156.

⁴⁹⁷ See *MOX Plant Case (Ireland v. United Kingdom)*, PCA Case No. 2002-01, Procedural Order No. 6 (Termination of Proceedings), 6 June 2008.

⁴⁹⁸ There were three heads of complaint, but I will not deal with the third head of complaint because it adds nothing new to the analysis.

Ireland's invocation of the instruments breached Article 344 TFEU and posed a threat to the 'autonomy of the Community legal system'. Generally speaking, this would imply that the Court's findings on the second head of complaint are also relevant in respect of situations where the member states invoke EU law instruments in disputes concerning a treaty to which they alone are parties and which provides that disputes concerning its interpretation and application are to be settled by ad hoc arbitration tribunals (like member state BITs).

The Court's reasoning leaves some questions open. It is uncertain whether the Court indicated that the interpretation and application of EU law by a court or tribunal operating outside the EU legal order threatens the autonomy of the EU legal order as such, or whether such 'manifest risk' exists only when a non-EU court *also* determines whether a member state has breached specific EU law provisions. Arguably, a literal interpretation of the relevant paragraphs imply that it is enough that a non-EU court interprets and/or applies EU law for such 'manifest risk' to appear for three reasons. First, the Court discussed the autonomy issue separately and expressly held that Ireland's argument that it had raised the EU law instruments only as factual elements was 'entirely irrelevant' for the existence of the 'manifest risk'. In other words, the potential interpretation and application of EU law by the UNCLOS tribunal created a 'manifest risk' in itself and it was irrelevant whether or not the tribunal had also examined whether the UK had breached the instruments. Second, in respect of the fact/applicable law distinction, if EU law was only a factual element in the analysis, the tribunal would still need to interpret the instruments to assess their relevance for the dispute, and this is what the Court also implied by noting that it was irrelevant whether the instruments were a fact or part of the applicable law. Third, when a court or tribunal interprets an EU law instrument, that interpretation already entails, in many cases, an implicit declaration on whether a member state has violated its obligations under that instrument. For example, if the UNCLOS tribunal had analysed what the directives required from the member states, that analysis would have entailed an implicit declaration on the UK's compliance with the directive.

The Court's take on Article 293 UNCLOS also merits a few comments. As noted, that article provides that UNCLOS tribunals 'shall apply this Convention and other rules of international law not incompatible with this Convention'. From this text, the Court inferred that the UNCLOS tribunal was bound to interpret and apply the EU law instruments raised

by Ireland, which breached Article 344 TFEU. Generally speaking, the Court's inference that Ireland's invocation of the EU law instruments necessarily leads the tribunal to interpret and apply them is correct, but it fails to specify what the ECJ thought about the status that EU law had in the UNCLOS proceedings; was it only a factual element as Ireland argued or part of the law that applies to the merits of the dispute. The ECJ held that Ireland had requested the tribunal to declare that the UK 'had breached the provisions of those [EU law] instruments'. Arguably, this twin contention - that Ireland was inviting the tribunal to declare a breach of EU law and that the tribunal would have accepted the invitation - is less than plausible. It may be the case that the tribunal's ruling could have been read as implying that the UK either breached or complied with its obligations under the EU law instruments, but an express ruling in this respect would have signalled manifest incompetence on the tribunal's part. The wording of the choice of law clause in Article 293 UNCLOS is highly general, but arbitral tribunals are aware of the fact that their jurisdiction does not extend to give rulings 'on alleged breaches of EU law as such', as the *EURAM* tribunal put it,⁴⁹⁹ which also covers declarations on such breaches. An UNCLOS tribunal's jurisdiction is limited to resolving disputes which concern alleged breaches of the Convention's provisions, and EU law provisions can only act 'as non-binding elements of fact' in such analysis, as Ireland had argued.

Put differently, assuming that the UNCLOS tribunal had declared a breach of EU law, such declaration would entail an assessment of the UK's actions only in light of the EU law instruments, but not an assessment of their compatibility with the relevant UNCLOS provisions, and only the latter was relevant for resolving the dispute between Ireland and the UK. Hence, the argument that those instruments were part of the applicable law is incorrect as the underlying dispute could only be resolved against the relevant UNCLOS provisions.⁵⁰⁰ The ECJ's reasoning in the *Commission v. Slovakia* judgment lends support to this understanding.⁵⁰¹ In that case, Advocate-General Jääskinen had noted that the

⁴⁹⁹ *EURAM* award, supra note 83, para. 190.

⁵⁰⁰ Schmalenbach makes the same argument by noting that although Article 293 UNCLOS 'allows the tribunal to apply – apart from UNCLOS – other rules of international law, this does not extend the tribunal's jurisdiction *ratione materiae* to' the EU founding treaties. Similarly, Article 293 UNCLOS 'neither opens the gate for a direct consultation of EC law in order to fully appreciate the meaning of UNCLOS rules, nor does it extend the tribunal's mandate to the interpretation and application of EC law in a given case'. See Schmalenbach, 'Struggle for Exclusiveness', supra note 389, p. 1051 (footnotes omitted). On the other hand, had Ireland argued that certain UNCLOS provisions conflict with EU law, the tribunal would have needed to assess if the alleged conflict exists and which conflict rule applies, with EU law becoming, potentially, part of the applicable law, but Ireland did not raise such argument.

⁵⁰¹ Case C-264/09, *Commission v Slovak Republic*, ECLI:EU:C:2011:580.

Slovak-Switzerland BIT's interpretation is a task that 'falls exclusively within the competence' of arbitral tribunals established under the BIT, also because of the risk of different conclusions that the EU courts and arbitral tribunals could reach.⁵⁰² Similarly, the Court recognized that it was not competent to interpret the BIT, but it nonetheless proceeded to analyze whether the termination of an investment contract by the Slovak Republic, as requested by the EU Commission, would breach the BIT's expropriation clause. The Commission had started the infringement proceedings on the ground that the investment contract breached EU non-discrimination rules. The Advocate-General pointed out that the BIT's provisions 'appear as *facts* relating to the alleged infringement [of EU law], not as legal norms to be interpreted by the Court'.⁵⁰³ While the BIT was only a factual element in the analysis, the Court not only interpreted the BIT but also declared that the contract's termination would 'have the same effect as expropriation within the meaning of Article 6 of the Investment Protection Agreement'.⁵⁰⁴ In other words, the Court's judgment entails a declaration that the termination of the investment contract would breach the Slovak Republic's obligations under the BIT.

The point is that this is what arbitral tribunals will also necessarily do when the parties invoke EU law instruments in their submissions, while simultaneously recognizing that they are not authorized to rule on alleged breaches of EU law as such. The Advocate-General's distinction between facts and 'legal norms to be interpreted by the Court' also suggests that the Court's finding in *MOX Plant* (that the Community law instruments were part of the applicable law in the UNCLOS proceedings) is analytically incorrect. By analogy to *Commission v Slovakia*, the EU law instruments would have remained mere facts even if the UNCLOS tribunal had interpreted and applied them in a similar way as the ECJ did in *Commission v Slovakia*. More generally, the Court's reasoning in *MOX Plant* implies that when EU law is part of the factual matrix or part of the applicable law in an arbitration, the autonomy of the EU legal order is exposed to a 'manifest risk', because the tribunal may have to interpret and apply EU law.⁵⁰⁵ Admittedly, this would significantly expand the scope of the autonomy doctrine, so the question is whether the

⁵⁰² Ibid., para. 40; Case C-264/09, *Commission v Slovak Republic*, Opinion of AG Jääskinen, ECLI:EU:C:2011:150, para. 79.

⁵⁰³ *Commission v Slovak Republic*, Opinion of AG Jääskinen, supra note 502, para. 80.

⁵⁰⁴ *Commission v Slovak Republic*, supra note 501, para. 48.

⁵⁰⁵ In this context, the word 'apply' refers above all to the situation where the tribunal looks at the meaning of an EU law instrument and thereby provides an implicit assessment of the question of whether a member state's actions comply with that instrument.

different ways in which arbitral tribunals may engage with EU law should be distinguished for the purposes of the analysis. For example, if an arbitral tribunal interprets an EU directive, and the directive is not subject to different interpretations, it would seem clear that the autonomy of EU law is not under threat. A good example is *Maffezini* where the tribunal stated that a directive required the investor to carry out an environmental impact assessment,⁵⁰⁶ but the tribunal's primary focus was on deciding whether the member state had breached its obligations under Argentine-Spain BIT, with the directive being a minor factual element in the analysis.

It seems also plausible to assume that the question of competence is only 'indirectly' relevant to the existence of a manifest risk. When EU law instruments are raised before an arbitral tribunal, the EU has competence over the subject-matter of those instruments (creating a manifest risk), although it may not have competence over the subject-matter of the treaty under which the tribunal was established. What the above discussion implies for member state BITs is discussed in the following section, but already here it is useful to note that a number of arbitral tribunals have expressly noted that they may interpret and apply EU law. In *Electrabel*, the tribunal reasoned that it was 'required...to interpret the European Commission's Final [state aid] Decision...and in that sense, to apply EU law to the Parties' dispute'.⁵⁰⁷ Similarly, the *EURAM* tribunal noted that it 'can consider and apply EU law, if required, both as a matter of international law and as a matter of German law'.⁵⁰⁸ Many BITs lack a choice of law clause in which case the applicable arbitration rules become relevant. Article 42(1) of the ICSID Convention, for example, provides that if the disputing parties cannot agree on the applicable law, tribunals 'shall apply the law of the Contracting State party to the dispute...and such rules of international law as may be applicable'. Article 26 of the Energy Charter Treaty provides that tribunals 'shall decide the issues in dispute in accordance with this Treaty and applicable rules and principles of international law'.⁵⁰⁹

These provisions are quite similar to Article 293 UNCLOS, so if a member state raises EU law instruments as part of its defence in an ICSID arbitration, for example, the ECJ's findings in *MOX Plant* appear to become relevant, as they may become in relation to

⁵⁰⁶ See *Maffezini* award, supra note 162, para. 69.

⁵⁰⁷ *Electrabel* award, supra note 144, para. 4.198.

⁵⁰⁸ *EURAM* award, supra note 83, para. 283. The proceedings took place in Frankfurt.

⁵⁰⁹ See Article 26(6) of the ECT, supra note 95.

investment disputes governed by other arbitration rules. Arbitral awards rendered under BITs are final and binding, and the ability of member state courts and the ECJ to review awards in respect of questions of EU law are limited in three ways: first, the grounds of annulment of arbitral awards are limited, and the ability of the ECJ to review a tribunal's interpretation of EU law is equally limited; second, the disputing parties may comply with the award voluntarily which excludes its review by any court; and, third, the tribunal's seat may be outside the EU in which case member state courts can become involved only if the winning party seeks enforcement within the EU.

5.4. Implications for Member State BITs

The Court's use of language in the above cases is somewhat arcane, but its central concern is to ensure that EU law is interpreted homogeneously and has the same effect in all member states. In this sense, the ECJ's perception of its mandate resembles the mandate of courts of last instance in domestic legal systems. Allowing member states to create courts and tribunals whose jurisdiction extends to questions of EU law threatens the uniform interpretation and application of EU law within the EU, as would the creation of a regional court of general jurisdiction by two provinces in a member state, when that court operates in isolation of the domestic legal system and the provinces have no necessary authority under the national constitution. The question is to what extent the ECJ 'tolerates' situations where courts and tribunals other than member state courts interpret and apply EU law without the Court being in a position to ensure the 'correctness' of those interpretations. As noted, investment disputes raised under member state BITs do not necessarily involve questions of EU law. Such disputes may relate, for example, to national criminal proceedings against an investor or to a reversal of a privatization policy over which member states have exclusive competence, apart from the requirement that the policy complies with the fundamental freedoms and the principle of non-discrimination. Moreover, when the parties raise EU law arguments, the tribunal might conclude, as the *Eureko* tribunal did, that the resolution of the dispute 'has no bearing upon any question of EU law'.⁵¹⁰ One central question is what type of EU law arguments the parties can raise under standard arbitration clauses and what kind of 'techniques' tribunals use when addressing those arguments. In general terms, the disputing parties can invoke EU law related arguments if this is considered a good litigation strategy and if the facts and legal

⁵¹⁰ *Achmea* award, supra note 325, para. 276.

materials facilitate their use, and this holds true irrespective of the wording of the arbitration clause or the content of the arbitration rules that govern the dispute. The choice of law clauses in BITs, when they exist, place no restrictions in this regard either. Another question is, as noted, to what extent member state courts and the ECJ can review the ways in which tribunals have engaged with EU law, in particular how the latter have interpreted EU law in individual cases.

The ways in which arbitral tribunals use EU law also relate to 'regulatory conflicts', to which I alluded in the introduction. Regulatory conflicts refer to the following scenario: a member state takes action to comply with the requirements of EU law; this action affects an investment qualifying for protection under a BIT; the investor decides to raise a claim against the member state, arguing that the measure breaches, for example, the fair and equitable treatment standard. The challenged measure can relate to various types of EU acts - to implementation of the decisions of the Commission, to general legislative changes that relate to the requirements of specific EU directives, or to administrative and legal decisions taken on the basis of an EU regulation. In defending the measure, the member state can make the general argument that EU law mandated the contested action, but also employ more specific arguments related to EU law. First, it can argue that its obligations under EU law take priority over its BIT obligations as matter of international law (and EU law). Second, it can argue that EU law is a factual element which is relevant for analyzing the measure's compatibility with the BIT. Third, the member state can argue that the measure is attributable to the EU under international law and the investor's claim therefore inadmissible. When analyzing such arguments, the tribunal has to determine what role EU law has in the proceedings. Is it part of the applicable law or a factual element?

The following section looks at the dichotomy of applicable law and fact as it relates directly to the ways in which arbitral tribunals will use EU law in individual cases. After that, I discuss arbitrations which involved some variant of the basic regulatory conflict scenario outlined above and where the tribunals addressed questions of EU law. This discussion not only shows the extent to which arbitral tribunals use EU law but also demonstrates the basic approaches that arbitral tribunals take in regulatory conflict scenarios. The final section provides a more general assessment of the relationship of member state BITs and the autonomy of the EU legal order as well as provides some comments on the question of interests and values.

5.4.1. The Question of Applicable Law

The dichotomy of 'applicable law' and 'fact' requires some clarification. It is often invoked in discussions concerning the question of whether arbitrators are obliged, *ex officio*, to know the content of the applicable law or whether the dispute should be decided solely with reference to the arguments of and legal grounds raised by the disputing parties. Some commentators frame this issue by asking whether the '*applicable law is a matter of law to be determined by the decision maker or rather a fact to be proven by the parties*'.⁵¹¹ In this approach, *applicable law* is either a fact or 'a matter of law' depending on the way the tribunal determines its contents. But the dichotomy is used in another way as well. That states may not invoke provisions of domestic law to justify a breach of a treaty obligation is a recognized principle of international law.⁵¹² In other words, national law is only an element of fact when a state is accused of breaching its treaty obligations. Similarly, when an investor raises a claim against an EU member state, the provisions of the BIT *are* the applicable law as the dispute is resolved by assessing the member state's actions against the provisions of the BIT (and not against EU law). The relevant question in the present context is whether EU law can be part of the applicable law in the sense that it is applied to the merits of an investment dispute. The way in which tribunals determine the contents of the applicable law *and* of the law that is considered a fact is a different question, and one which will not be addressed in the following.

The principle of party autonomy is central to the idea of arbitration and entails the freedom of the parties to choose the law that governs their dispute. However, if the BIT under which the claim is raised entails a choice of law clause, the tribunal is to apply that clause although the claimant investor played no role in its construction.⁵¹³ It is not uncommon that

⁵¹¹ Emphasis added. Cezary Wiśniewski and Alicja Zielińska, 'Who Should Know the Law: The Arbitrators or the Parties?', *Kluwer Arbitration Blog*, 3 October 2016. Similarly, Kaufmann-Kohler asks whether the applicable law 'is...a fact to be proven by the parties or...law to be investigated by the arbitrators.' See Gabriele Kaufmann-Kohler, 'The Arbitrator and the Law: Does He/She Know It? Apply It? How? And a Few More Questions', 21 *Arbitration International* (2005), pp. 631-638, at 632.

⁵¹² This principle is enshrined in Article 27 VCLT, the relevant part of which reads as follows: 'A party may not invoke the provisions of its internal law as justification for its failure to perform a treaty.'

⁵¹³ See e.g. Rudolf Dolzer and Christoph Schreuer, *Principles of International Investment Law* (Oxford University Press, 2nd ed. 2012), p. 289; Yas Banifatemi, 'The Law Applicable in Investment Treaty Arbitration', in Katia Yannaca-Small (ed.), *Arbitration Under International Investment Agreements: A Guide to the Key Issues* (Oxford University Press, 2010), pp. 191-210, at 194-195. See also *Antoine Goetz et al. v. Republic of Burundi*, ICSID Case No. ARB/95/03, Award (embodying the parties' settlement agreement), 10 February, 1999, para. 94 ('Sans doute la détermination du droit applicable n'est-elle pas, à proprement parler, faite par les parties au présent arbitrage (Burundi et investisseurs requérants), mais par les parties à la Convention d'investissement (Burundi et Belgique). Comme cela a été le cas pour le consentement des

BITs lack a clause on the applicable law and that the parties have not agreed on the matter either, in which case tribunals resort to the choice of law clauses in the applicable arbitration rules.⁵¹⁴ As noted, the generality of choice of law clauses means that they usually do not determine the formal status of EU law. If a tribunal concludes that EU law is part of the applicable law, this means, in principle, that EU law applies to the merits of the dispute together with the provisions of the BIT and any other applicable rules of international law. Since international law is not a hierarchical legal order, treaty obligations stand on equal footing. If EU law is part of the applicable law and the respondent state argues that its obligations under specific EU acts take priority over its BIT obligations, the priority of one obligation over the other can only be established by applying conflict rules.⁵¹⁵ On the other hand, if EU law is considered a fact, it cannot rise to the same hierarchical level as the relevant BIT, nor invoked to justify a breach of BIT obligations. If EU law is equated with national law, the principle enshrined in Article 27 VCLT applies by analogy: the respondent member state cannot 'invoke the provisions of its internal law [i.e. EU law] as justification for its failure to perform a treaty'.⁵¹⁶ In other words, the designation of EU law as national law is necessarily equivalent to treating it as fact, which cannot override the provisions of the applicable BIT. To understand better regulatory conflict scenarios and to show how arbitral tribunals tackle questions of EU law, it is useful to look at a number of relevant arbitrations.

parties, le Tribunal estime cependant que la République du Burundi s'est prononcée en faveur du droit applicable tel qu'il est déterminé dans la disposition précitée de la Convention belgo-burundaise d'investissement en devenant partie à cette Convention et que les investisseurs requérants ont effectué un choix similaire en déposant leur requête d'arbitrage sur la base de ladite Convention.').

⁵¹⁴ Article 42(1) of the ICSID Convention provides that in the absence of an agreement between the parties, tribunals 'shall apply the law of the Contracting State party to the dispute (including its rules on the conflict of laws and such rules of international law as may be applicable.' Article 35(1) of the UNCITRAL Arbitration Rules provides that the tribunal 'shall apply the rules of law designated by the parties as applicable', and 'failing such designation by the parties, the arbitral tribunal shall apply the law which it determines to be appropriate'. Article 26(6) of the ECT makes no reference to the agreement of the parties on applicable law and it reads as follows: 'A tribunal...shall decide the issues in dispute in accordance with this Treaty and applicable rules and principles of international law.' Article 22(1) of the Stockholm Chamber of Commerce Arbitration Rules state that if the parties have not agreed upon applicable law, the tribunal 'shall apply the law or rules of law which it considers to be most appropriate'.

⁵¹⁵ I am referring here not to primary conflict arguments but to regulatory conflict arguments (i.e. alleged conflicts between BIT protection standards and secondary EU law).

⁵¹⁶ As Crawford notes, this 'position is not in doubt.' See James Crawford, *Brownlie's Principles of Public International Law* (Oxford University Press, 8th ed. 2012), p. 51. The quote in the text is from Article 27 VCLT.

5.4.2. Arbitral Tribunals and EU Law

The rules of thumb are clear. Once a state has acceded to the EU, the primacy of EU law dictates that its obligation to implement EU acts takes priority over its obligations under intra-EU BITs as a matter of EU law. But regulatory conflicts may be 'neutralized' in a number of ways. For example, a tribunal may conclude that EU law is only an element of fact or then hold that the challenged measure was not related to or required by the relevant EU act. Similarly, the parties may agree that EU law and the relevant BIT are compatible, but disagree over the status of the relevant EU law instrument: was the challenged measure mandated by EU law or not, and is it part of the applicable law or merely a fact that either is central to or plays no role in the tribunal's analysis. As to extra-EU BITs, member states have to eliminate treaty obligations that prevent the implementation of EU acts as a matter of EU law, but third state investors can continue to rely on BIT protections also when domestic acts of implementation affect their investments in a negative way. But, again, direct conflict arguments are unlikely to be raised for the same reasons as in intra-EU disputes, with other litigation strategies being more plausible.

In many arbitrations, the claimant investor has relied on the legitimate expectations doctrine and the fair and equitable treatment standard. The doctrine of legitimate expectations exists under EU law and international investment law, but its basic elements are broadly similar under both legal systems.⁵¹⁷ In essence, the doctrine refers to the regulatory framework of the host state (or the EU) and to specific assurances and representations that the host state (or the EU institutions) have made in respect of the stability of that framework. Changes in that framework, which cancel out such assurances and representations, can lead investors to seek redress both under EU law and member state BITs on the ground that the changes breached their legitimate expectations. Put differently, the central question is what kind of expectations a diligent businessman can entertain in respect of the stability of the regulatory framework of the host state (or the internal market). Another central question is whether tribunals should apply the legitimate expectations doctrine as it stands under EU law, or whether their analyses will necessarily

⁵¹⁷ On the legitimate expectations doctrine as it stands under EU law, see Paul Craig, *EU Administrative Law* (Oxford University Press, 2nd ed. 2012), Chapter 18. On its content in the context of investor-state arbitration, see Michele Potesta, 'Legitimate Expectations in Investment Treaty Law: Understanding the Roots and the Limits of a Controversial Concept', 28 *ICSID Review* (2013), pp. 88-122, at 98-121; Elizabeth Snodgrass, 'Protecting Investors' Legitimate Expectations: Recognizing and Delimiting a General Principle', 21 *ICSID Review* (2006), pp. 1-58.

be based on the doctrine as developed by arbitral tribunals. The ECJ has held that economic operators (including investors) 'cannot have a legitimate expectation that an existing situation which is capable of being altered by the Community institutions in the exercise of their discretionary power will be maintained'.⁵¹⁸ In other words, and in general terms, if investors are bound by EU law rules and principles once they have made an investment in a member state, how should this 'binding effect' affect BIT claims that relate to EU law in one or another way.

Many of the arbitrations where EU acts have played a role were raised under the Energy Charter Treaty (ECT), to which both the EU and its member states are parties. While this clearly distinguishes the ECT from member state BITs, it is useful to look at the cases because we are interested in the general question of how arbitral tribunals approach and use EU law and whether this poses a 'manifest risk' to the autonomy of the EU legal order. Similar type of claims could be brought under member state BITs, in which case the tribunals would have to address the relevant EU law questions in one or another way.

5.4.2.1. The Power Purchase Agreement Cases

The *AES Summit*, *EDF* and *Electrabel* arbitrations were raised under the ECT and concerned so called power purchase agreements (PPAs) concluded between Hungary and the claimant companies in the 1990s. In the agreements, Hungary pledged to buy electricity at a given price for a fixed time period, which guaranteed a return on the claimants' investments without commercial risk. The PPAs were not 'processed' under the state aid rules of the EU-Hungary association Agreement (as they should have), and neither did they qualify as existing aid under the rules established in the accession treaty and its annexes,⁵¹⁹ which prompted the Commission to begin the investigation after Hungary had acceded to the EU.⁵²⁰ At the same time, the perception that the PPAs allowed generators to pocket overly high profits generated political debate in Hungary and led

⁵¹⁸ See e.g. Case C-350/88, *Delacre and Others v Commission*, ECLI:EU:C:1990:71, para. 33.

⁵¹⁹ See *Electrabel* award, supra note 144, paras. 4.94-4.97.

⁵²⁰ Hungary's Europe Agreement entailed state aid provisions that were identical with the corresponding EU state aid rules. See Article 8 of Protocol 2 of the Europe Agreement establishing an association between the European Communities and their Member States, of the one part, and the Republic of Hungary, of the other part, OJ L 347, 31.12.1993, pp. 2-266. The PPAs had not been processed under the state aid rules of the Europe Agreement (as they should have), and neither did they qualify as existing aid under the various rules established in the accession treaty and its annexes, which prompted the Commission to begin the investigation. On this, see *Electrabel* award, supra note 144, paras. 4.94-4.97.

(together with the state aid concern) to the introduction of price regulation in 2006, which substantially reduced the profitability of the generators.

A central principle under EU law is that economic operators cannot entertain any legitimate expectations over the lawfulness of state aid they have received unless the aid scheme was notified to and authorized by the Commission before its application.⁵²¹ If there are exceptional circumstances which caused the beneficiary to assume that the aid is lawful, such circumstances can play a role 'only in resisting the possible recovery of that aid'.⁵²² In other words, if a given aid scheme is not authorized by the Commission beforehand, its beneficiaries cannot entertain any legitimate expectations about its continuation or argue that they are entitled to keep the aid they have already received, unless the recovery breaches a principle of EU law. In June 2008, the Commission decided that the PPAs constitute illegal state aid and ordered Hungary to recover the aid which the claimants had received under the PPAs after Hungary's EU accession.⁵²³ In the wake of the Commission's decision, the Hungarian parliament adopted a law authorizing the early termination of the PPAs by the end of 2008.⁵²⁴ The basic argument of the claimants in *AES Summit*, *EDF* and *Electrabel* was that by introducing the price regulation and/or terminating the PPAs, Hungary had breached its obligations under Article 10 ECT, including the investors' legitimate expectations under the fair and equitable treatment standard.⁵²⁵ While the EU is party to the ECT, none of the claimants raised a claim against the EU on the basis of the Commission's state aid decision, but the Hungarian subsidiaries of the claimants, which owned and operated the power plants, brought direct actions against the Commission's decision before the General Court.⁵²⁶ The following analysis focuses on the *AES Summit* and *Electrabel* awards as they are publicly available, and some references are also made to the *Micula* arbitration which was raised under the Romania-Sweden BIT. I will focus on two aspects of the awards; those that are directly relevant to

⁵²¹ See e.g. Case T-179/09, *Dunamenti Erőmű Zrt. v Commission*, ECLI:EU:T:2014:236, para. 104.

⁵²² *Idem*.

⁵²³ Commission decision of 4 June 2008 on the State Aid C 41/05 awarded by Hungary through Power Purchase Agreements, OJ L 225, 27.8.2009, pp. 53-103, at 102.

⁵²⁴ European Commission, *State aid N 691/2009, Hungarian stranded costs compensation scheme*, Brussels (27 April, 2010), C(2010)2532 final, p. 2.

⁵²⁵ *Electrabel* award, supra note 144, para. 1.47; *AES Summit Generation Limited and AES-TISZA Erőmű Kft. v. Hungary*, ICSID Case No. ARB/07/22, Award (hereinafter *AES Summit* award), 23 September 2010, paras. 4.1 and 5.1.

⁵²⁶ Article 256 TFEU establishes the jurisdiction of the General Court to 'hear and determine at first instance actions or proceedings referred to' e.g. in Article 263 TFEU. Article 263(4) TFEU authorizes natural and legal persons to 'institute proceedings against an act addressed to that person or which is of direct and individual concern to them'.

the question of autonomy of the EU legal order as well as to aspects that relate to the general approaches that arbitral tribunals take in respect of regulatory conflicts.

Electrabel

In all three cases (*AES Summit*, *EDF* and *Electrabel*) the tribunals were to apply the provisions of the ECT and 'applicable rules and principles of international law', as provided by Article 26(6) ECT. On the role of EU law, the *Electrabel* tribunal noticed that it could operate in three different ways. As international law, as a legal order distinct both from international law and legal orders of member states, or as part of Hungary's national law.⁵²⁷ The claimant argued that EU law was part of Hungary's domestic law and should be considered as 'a matter of fact or evidence', which implied that Hungary could not invoke EU law to justify a breach of its ECT obligations.⁵²⁸ Hungary agreed that EU law is relevant as an element of fact, but added that EU law also qualifies as international law because it originates in international treaties.⁵²⁹ Neither party raised conflict arguments but argued that EU law and the ECT should be read as constituting a harmonious set of obligations.⁵³⁰ As a first step, the tribunal concurred with Hungary and classified EU law as international law, 'because it is rooted in international treaties'.⁵³¹ Both primary and secondary EU law were 'part of a regional system of international law'.⁵³² More specifically, since the Commission's state aid decision was central to the termination of the PPA, it 'would be artificial' to classify Article 107 TFEU as international law and assign a different status to the implementation of that article by an organ created under the same international treaty.⁵³³

The claimant argued that the PPA's termination breached the ECT's fair and equitable treatment standard, but the act of termination was detached from the state aid decision in two ways. First, the claimant was not requesting the tribunal 'to make any decision

⁵²⁷ *Electrabel* award, supra note 144, para. 4.20.

⁵²⁸ *Ibid.*, paras. 4.24.-4.25.

⁵²⁹ *Ibid.*, paras. 4.57-4.58. For more detailed arguments of Hungary in this regard, see paras. 4.65-4.74. The Commission submitted a lengthy brief to the tribunal and claimed, in essence, that Article 26(6) ECT 'requires the application of EU law because EU law is international law' (see para. 4.102).

⁵³⁰ *Ibid.*, paras. 4.43, 4.59 and 4.75.

⁵³¹ *Ibid.*, para. 4.120.

⁵³² *Ibid.*, para. 4.122. With reference to *Van Gend & Loos*, supra note 360, p. 12 ('The Community constitutes a new legal order of international law for the benefit of which the states have limited their sovereign rights.').

⁵³³ *Ibid.*, paras. 4.122-4.123.

concerning the correctness' of the state aid decision 'as a matter of EU law'.⁵³⁴ Second, the claimant argued that the decision did not require Hungary to terminate the PPA.⁵³⁵ This isolated the PPA's termination from the state aid decision. As the tribunal put it, the claimant 'does not seek to impugn, in these arbitration proceedings, the legal validity' of the state aid decision under EU law, 'nor Hungary's legal obligation under EU law to implement that Decision in accordance with its terms'.⁵³⁶ The relationship of EU law and the ECT played an important role in the tribunal's analysis, and similarly to the disputing parties, the tribunal held that there is a presumption that the ECT's provisions are 'in conformity with EU law'.⁵³⁷ This presumption was based on a number of factors: on the EU's central role in the conclusion of the ECT; on the similar objectives of EU law and the ECT; on Article 207(3) TFEU, which provides that the Council and the Commission have to ensure that treaties falling under the Common Commercial Policy, such as the ECT, 'are compatible with internal Union policies and rules'; and on Article 1(3) ECT which recognizes that the EU has the authority to take binding decisions over EU member states, including in matters covered by the ECT.⁵³⁸ A logical corollary of the presumption of compatibility was that 'the ECT does not protect the Claimant, as against the Respondent, from the enforcement by the Respondent of a binding decision of the European Commission under EU law'.⁵³⁹ Put differently, if ECT and EU law obligations form a harmonious set of obligations, investors cannot invoke the ECT when member states implement EU law.

Since the tribunal held that the ECT does not protect the claimant from the consequences of the enforcement of the state aid decision, the crucial question was whether that decision required Hungary to terminate the PPA. A negative answer would denote that Hungary could not rely on the state aid decision as part of its defense, and the tribunal's dictum on the relationship of the ECT and the state aid decision would not apply either. Rather, Hungary's termination of the PPA would be assessed solely against the ECT's fair and

⁵³⁴ Ibid., para. 6.20.

⁵³⁵ Ibid., paras. 6.22.-6.26.

⁵³⁶ Ibid., para. 6.77.

⁵³⁷ Ibid., para. 4.134. can have had no legitimate expectations [under the ECT] in regard to the consequences of the implementation by an EU member state' of decisions taken by the Commission (see para. 4.142).

⁵³⁸ See *ibid.*, paras. 4.134-4.135, 4.137-4.138 and 4.142. As to Article 1(3) ECT, the tribunal held that this provision indicated that 'investors can have had no legitimate expectations [under the ECT] in regard to the consequences of the implementation by an EU member state' of decisions taken by the Commission (see para. 4.142).

⁵³⁹ Ibid., para. 4.169.

equitable treatment standard, with the state aid decision becoming an (inconsequential) part of the factual evidence. A positive answer, in turn, would denote that the tribunal's dictum applied fully and the termination was compatible with the ECT. The tribunal provided a detailed analysis of the state aid decision and concluded that it had required Hungary to terminate the PPA.⁵⁴⁰ Under the tribunal's approach, this finding alone was enough to lead to the dismissal of the claimant's PPA termination claim, but the tribunal also carried out a short discussion on the attribution of the termination as between Hungary and the EU. It held that the state aid decision had obligated Hungary to terminate the PPA, which meant that Hungary was 'not legally responsible for acts by the European Commission...under the ECT or under international law'.⁵⁴¹ The tribunal argued that binding decisions of the EU institutions, 'recognized as such under the ECT', could not create responsibility for Hungary, because Hungary can only be responsible for its own wrongful acts under international law.⁵⁴²

In sum, the *Electrabel* tribunal assessed the division of competences between the EU and its member states (in the context of attribution) and rejected the claimant's PPA termination claim on the basis of the Commission's state aid decision. It is noteworthy that the tribunal's finding on attribution was based on the application of international law rules governing attribution, and not on the application of EU law. Yet, as a matter of EU law attributing responsibility for the implementation of EU acts falls under the exclusive jurisdiction of the ECJ. Clearly, and again, this appears to be problematic in particular in light of the Court's findings in Opinions 1/91 and 2/13. As to the potential conflict between the ECT and the Commission's state aid decision, the disputing parties agreed that there was no conflict, and the claimant disconnected the two by claiming that it was not challenging the state aid decision and that in any case the decision did not require Hungary to terminate the PPA. By and large, the tribunal followed suit and also attributed the termination to the EU, which rendered the PPA termination claim inadmissible.

⁵⁴⁰ Ibid., paras. 6.78-6.91.

⁵⁴¹ Ibid., para. 6.70.

⁵⁴² Ibid., para. 6.72.

AES Summit

AES Summit differs from *Electrabel* in that the case commenced prior to Hungary's termination of the PPAs and prior to the Commission's state aid decision. The claimants were challenging only the 2006 and 2007 price regulations, which had reduced their profitability and allegedly breached a number of ECT protection standards.⁵⁴³ On the applicable law, Hungary argued that as the ECT and EU competition law have similar objectives, its respective obligations under them should 'be read in harmony and be interpreted to minimize conflict'.⁵⁴⁴ Since the price regulations were partly motivated by the Commission's preliminary view that the PPAs constituted illegal state aid, the claimants could not legitimately expect that Hungary does not address such concerns by regulating electricity prices.⁵⁴⁵ As to the status of EU law, Hungary acknowledged that it is a factual element which should influence the tribunal's assessment of the price regulations. The claimants equated EU law with Hungarian national law, which meant that EU law could not justify the alleged breaches of the ECT.⁵⁴⁶ In contrast to Hungary, the claimants saw that the price regulations had to be assessed against the ECT's standards alone, with the state aid concerns being entirely irrelevant to deciding the dispute, even if part of its factual matrix.⁵⁴⁷

The tribunal first noted that it was mandated (under Article 26(6) ECT) to decide the dispute on the basis of the ECT and 'applicable rules and principles of international law'.⁵⁴⁸ EU competition law was both an 'international law regime' and part of the national law of EU member states, but the tribunal held that it should be considered as fact on the ground that the parties had so agreed.⁵⁴⁹ As to conflicts between EU law and the ECT, the tribunal held that the dispute was 'about the conformity or non-conformity of Hungary's acts and measures with the ECT', and the relationship of the price regulations to the dictates of EU

⁵⁴³ See *AES Summit* award, supra note 525, para. 5.1 (Hungary's actions constituted a breach of its obligation to provide fair and equitable treatment; impairment of the claimants' investment by unreasonable and discriminatory measures; breach of its obligation to provide national treatment; breach of its obligation to provide most favored nation treatment; breach of its obligation to provide constant protection and security; and expropriation).

⁵⁴⁴ *Ibid.*, para. 7.2.3.

⁵⁴⁵ *Ibid.*, para. 7.2.5.

⁵⁴⁶ *Ibid.*, paras. 7.3.4 and 7.3.8. In the oral proceedings, Hungary agreed that EC law is relevant as fact (see para. 7.5.2).

⁵⁴⁷ *Ibid.*, para. 7.3.2.

⁵⁴⁸ *Ibid.*, paras. 7.6.1-7.6.4.

⁵⁴⁹ *Ibid.*, para. 7.6.6.

law was 'only an element to be considered...when determining the "rationality," "reasonableness," "arbitrariness" and "transparency"' of the regulations.⁵⁵⁰ Unlike the *Electrabel* tribunal, the *AES Summit* tribunal did not analyze the EU's central role in the conclusion of the ECT, nor provided a general analysis of the relationship of the ECT and EU law.

The claimants asserted that fair and equitable treatment requires that states honor agreements they have entered into. Hence, the introduction of the price regulations breached their legitimate expectations as it altered Hungary's commitments under the PPA.⁵⁵¹ Likewise, some of the legislative changes introduced in connection with the price regulations 'eviscerated the legal framework' upon which the claimants 'had legitimately relied' when making their investment.⁵⁵² Hungary replied by noting that the existence of legitimate expectations requires that the investor has received express 'representations and assurances' on which the investor relies when making the decision to invest. Since the claimants had not received any such assurances, their case failed to meet the test.⁵⁵³ The only reference to EU law in the arguments of the parties on the issue of legitimate expectations was Hungary's observation that the price regulations were partly motivated by the Commission's demands that its state aid programs are brought in line with EU law.⁵⁵⁴

The tribunal concurred with Hungary on the criteria against which the existence of legitimate expectations should be assessed. Legitimate expectations can only arise in relation to assurances given at the time the investment was made and the tribunal referred to a string of investment arbitrations where this rule was applied.⁵⁵⁵ The claimants had made investments on two separate occasions in 1996 and 2001, and the question was if Hungarian authorities had given assurances upon which the claimants could rely on either occasion. Having analyzed the facts before it, the tribunal concluded that Hungary gave no such assurances and the claimants could not entertain any legitimate expectations that 'a regime of administrative pricing would not be reintroduced'.⁵⁵⁶ The tribunal also made the general point that 'any reasonably informed business person or investor knows that laws

⁵⁵⁰ *Ibid.*, para. 7.6.9.

⁵⁵¹ *Ibid.*, paras. 9.1.2-9.1.4.

⁵⁵² *Ibid.*, para. 9.1.5.

⁵⁵³ *Ibid.*, para. 9.2.5-9.2.8.

⁵⁵⁴ *Ibid.*, para. 9.2.13.

⁵⁵⁵ *Ibid.*, para. 9.3.8-9.3.12.

⁵⁵⁶ *Ibid.*, paras. 9.3.15-9.3.26 (the quote is from para. 9.3.26).

can evolve in accordance with the perceived political policy dictates of the times',⁵⁵⁷ but the role of Hungary's EU accession was not expressly referred to in this context.

However, the state aid concerns that (in part) motivated the price regulations were discussed in the context of the claim that the regulations were unreasonable and discriminatory in the meaning of Article 10(1) ECT. Hungary had justified the price regulations on three main grounds, one of them being the Commission's investigation on the compatibility of the PPAs with EU state aid rules.⁵⁵⁸ The tribunal saw that measures taken to comply with EU state aid obligations constitutes 'a rational public policy measure', but since the Commission had not yet decided that the PPAs constitute illegal state aid when the price regulations were introduced, Hungary could not justify them with reference to EU competition law.⁵⁵⁹ However, the tribunal was split on this with the majority concluding that the price regulations were 'not motivated by pressure from the EC Commission',⁵⁶⁰ whereas the dissenting arbitrator saw that the communications between the Commission and Hungary proved that there were good reasons to presume that the PPAs constituted illegal state aid, which implied that the question of the PPAs could not be disconnected from the 'motivation that was behind' the price regulations. Hence, arbitrator Stern concluded that 'the evidence is overwhelming' that the price regulations were 'a rational, non-arbitrary response to a complex set of legitimate policy concerns', one of which was the state aid concern.⁵⁶¹ It is noteworthy that although the majority held that the price regulations were not causally related to EU competition law, the claimant's claim about unreasonable and discriminatory treatment was rejected on the ground that the regulations were a 'reasonable, proportionate and consistent' policy response to the 'luxury profits' of the power generators.⁵⁶² Generally speaking, also the majority approached EU law as fact that would have affected the analysis of the 'rationality' and 'reasonableness' of the price regulations, *if* the two arbitrators had found a connection between the regulations and the state aid concerns.

⁵⁵⁷ Ibid., para. 9.3.34.

⁵⁵⁸ Ibid., para. 10.2.3.

⁵⁵⁹ Ibid., para. 10.3.16.

⁵⁶⁰ Ibid., para. 10.3.18.

⁵⁶¹ Ibid., para. 10.3.19. In *Electrabel*, the claimant had also challenged the price regulations, but the tribunal rejected the claim e.g. on the basis that the regulations were motivated by the state aid concerns that the Commission had repeatedly expressed to Hungarian authorities. See *Electrabel* award, *supra* note 144, paras. 8.24-8.27.

⁵⁶² Ibid., paras. 10.3.34 and 10.3.36.

In parallel with the arbitral proceedings, the Hungarian subsidiaries of *Electrabel* and *AES Summit* sought the annulment of the Commission's state aid decision before the General Court (GC), which dismissed both actions in 2014.⁵⁶³ *Electrabel* and its subsidiary appealed to the ECJ, which dismissed the plea in 2015, but the grounds of appeal are not relevant for the present discussion.⁵⁶⁴ The two judgments of the GC outline the basic elements of the legitimate expectations doctrine under EU law and provide a pathway into analyzing the different approaches that EU courts and investment tribunals take in state aid cases and on the relationship of the ECT and EU law. The judgments demonstrate that conflict arguments tend to play the second fiddle also before EU courts in regulatory conflict scenarios. The relevant arguments of the applicants were broadly similar in both cases and centered on the principles of legal certainty and legitimate expectations as well as Article 10 ECT, which contains the fair and equitable treatment standard and the prohibition of unreasonable and discriminatory measures.⁵⁶⁵

As to the legitimate expectations principle under EU law, the GC referred to its previous case law according to which three conditions 'must be satisfied in order for a claim to entitlement to the protection of legitimate expectations to be well founded'.⁵⁶⁶ First, EU or national authorities must have given 'precise, unconditional and consistent assurances... to the person concerned'; second, the assurances must be of such nature 'as to give rise to a legitimate expectation on the part of the person to whom they are addressed'; and third, the assurances 'must comply with the applicable rules'.⁵⁶⁷ The principle of legal certainty, in turn, requires that EU law rules 'be clear and precise' so that 'interested parties can

⁵⁶³ Case T-468/08, *Tisza Erőmű v Commission*, ECLI:EU:T:2014:235 (hereinafter *AES Summit GC*); Case T-179/09, *Dunamenti Erőmű Zrt. v Commission*, ECLI:EU:T:2014:236 (hereinafter *Electrabel GC*).

⁵⁶⁴ See Case C-357/14, *Electrabel SA and Dunamenti Erőmű Zrt. v Commission*, ECLI:EU:C:2015:642.

⁵⁶⁵ *AES Summit GC*, supra note 563, para. 219; *Electrabel GC*, supra note 563, para. 99. Article 10(1) ECT reads as follows: 'Each Contracting Party shall, in accordance with the provisions of this Treaty, encourage and create stable, equitable, favorable and transparent conditions for Investors of other Contracting Parties to make Investments in its Area. Such conditions shall include a commitment to accord at all times to Investments of Investors of other Contracting Parties fair and equitable treatment. Such Investments shall also enjoy the most constant protection and security and no Contracting Party shall in any way impair by unreasonable or discriminatory measures their management, maintenance, use, enjoyment or disposal. In no case shall such Investments be accorded treatment less favorable than that required by international law, including treaty obligations. Each Contracting Party shall observe any obligations it has entered into with an Investor or an Investment of an Investor of any other Contracting Party.'

⁵⁶⁶ *AES Summit GC*, supra note 563, para. 220; *Electrabel GC*, supra note 563, para. 100.

⁵⁶⁷ *Idem*. With reference e.g. to Case T-347/03, *Branco v Commission*, ECLI:EU:T:2005:265, para. 102; Case T-282/02, *Cementbouw Handel & Industrie v Commission*, ECLI:EU:T:2006:64, para. 77.

ascertain their position in situations and legal relationships governed by EU law'.⁵⁶⁸ In both judgments, the GC held that the applicants had not received any assurances over the compatibility of the PPAs with EU law, meaning that no legitimate expectations had arisen.⁵⁶⁹ Further, the state aid rules in Hungary's association agreement, in the Accession Treaty and in the Act of Accession, 'regarding both the substantive and the procedural rules of EU law on State aid', were clear and precise.⁵⁷⁰ In other words, the applicants had to know, first, that the compatibility of the PPAs with the state aid rules was not assessed prior to the Commission's decision and, second, that the PPAs did not qualify as existing aid under any of the relevant state aid provisions.⁵⁷¹ Another principle to which the GC referred to provides that a beneficiary of illegally granted aid, 'implemented without prior notification to the Commission', cannot entertain a legitimate expectation that the 'grant of the aid is lawful'.⁵⁷² If there are exceptional circumstances, which caused the beneficiary to assume that the aid is lawful, such circumstances can play a role 'only in resisting the possible recovery of that aid'.⁵⁷³ Likewise, and as noted, the Commission does not 'require recovery of the aid if this would be contrary to a general principle of Union law', such as the principle of legitimate expectations.⁵⁷⁴ No such circumstances were present and neither

⁵⁶⁸ *AES Summit GC*, supra note 563, para. 221; *Electrabel GC*, supra note 563, para. 101. See also Case C-63/93, *Duff and Others*, ECLI:EU:C:1996:51, paras. 19-20 (where the ECJ held that the principle of the protection of legitimate expectations 'is the corollary of the principle of legal certainty').

⁵⁶⁹ *AES Summit GC*, supra note 563, para. 222; *Electrabel GC*, supra note 563, para. 102.

⁵⁷⁰ *AES Summit GC*, supra note 563, para. 223; *Electrabel GC*, supra note 563, para. 105. The relevant provisions in the 2003 Act of Accession read as follows: 'The following aid schemes and individual aid put into effect in a new Member State before the date of accession and still applicable after that date shall be regarded upon accession as existing aid within the meaning of Article 88(1) of the EC Treaty: (a) aid measures put into effect before 10 December 1994; (b) aid measures listed in the Appendix to this Annex; (c) aid measures which prior to the date of accession were assessed by the State aid monitoring authority of the new Member State and found to be compatible with the *acquis*, and to which the Commission did not raise an objection on the ground of serious doubts as to the compatibility of the measure with the common market, pursuant to the procedure set out in paragraph 2. All measures still applicable after the date of accession which constitute State aid and which do not fulfil the conditions set out above shall be considered as new aid upon accession for the purpose of the application of Article 88(3) of the EC Treaty.' See Part 3 of Annex IV to the Act concerning the conditions of accession of the Czech Republic, the Republic of Estonia, the Republic of Cyprus, the Republic of Latvia, the Republic of Lithuania, the Republic of Hungary, the Republic of Malta, the Republic of Poland, the Republic of Slovenia and the Slovak Republic and the adjustments to the Treaties on which the European Union is founded, OJ L 236, 23.9.2003, pp. 33-988, pp. 797-802.

⁵⁷¹ See *Electrabel GC*, supra note 563, paras. 50-72, for a discussion on the rules governing Hungary's aid schemes during the association and accession process.

⁵⁷² *Ibid.*, para. 104. With reference to Case 223/85, *RSV v Commission*, ECLI:EU:C:1987:502, para. 17; Case C-183/91, *Commission v Greece*, ECLI:EU:C:1993:233, para. 18; and Joined Cases C-183/02 P and C-187/02 P, *Demesa and Territorio Histórico de Álava v Commission*, ECLI:EU:C:2004:701, para. 51.

⁵⁷³ *Idem.*

⁵⁷⁴ See Article 16 of Council Regulation (EU) 2015/1589 of 13 July 2015 laying down detailed rules for the application of Article 108 of the Treaty on the Functioning of the European Union (codification), OJ L 248, 24.9.2015, pp. 9-29, at 20.

did the recovery breach a general principle of EU law.⁵⁷⁵ Finally, the GC also made the more general observation that EU accession entails 'a major change in legal and economic features of a market', which entails the possibility that a measure may transform into illegal state aid upon EU accession 'without that undermining the legitimate expectations of the interested party or the principle of legal certainty'.⁵⁷⁶

One observation is that the GC's take on the clarity and precision of the state aid rules under Hungary's association agreement is quite different from the *Micula* tribunal's analysis. *Micula* concerned a pre-accession aid scheme and its premature revocation by Romania in 2004, some three years before its EU accession. The *Micula* tribunal emphasized much more the difficulties Romanian authorities had had in understanding, implementing and operating the pre-accession state aid rules, and the consequences this had on the investors' legitimate expectations,⁵⁷⁷ whereas the GC simply looked at the 'abstract' clarity of those rules and then held that the applicants had to know their contents and requirements. This is quite interesting because the GC also acknowledged that Hungarian authorities had completely neglected the implementation of the pre-accession state aid mechanism; apparently, Hungary had not established any national competition agency to which its existing aid schemes (including the PPAs) could have been notified at the pre-accession stage.⁵⁷⁸ The Commission's reasoning in the *Micula* state aid decision is also interesting as it by and large follows the reasoning of the GC. The *Micula* claimants had become eligible to benefit from the revoked aid scheme only *after* the Romanian Competition Council had decided in May 2000 that it constitutes illegal state aid under the association agreement. While the date of eligibility was not relevant for the Commission's state aid decision, this fact still meant that the claimants 'must have been fully aware' of the Competition Council's decision and of the state aid provisions of the association agreement and Romanian national law, both of which prohibited state aid and designated the Competition Council as the competent national authority on state aid matters.⁵⁷⁹ Since the ECJ's case law on state aid applied vis-à-vis Romania under Article 64 of the association agreement (including the legitimate expectations doctrine), and since the Competition

⁵⁷⁵ *AES Summit GC*, supra note 563, paras. 161-164; *Electrabel GC*, supra note 563, paras. 281ff.

⁵⁷⁶ *AES Summit GC*, supra note 563, para. 223; *Electrabel GC*, supra note 563, para. 105.

⁵⁷⁷ For a scathing critique of the *Micula* tribunal's reasoning on the claimants' legitimate expectations, see Maja Stanivuković, 'Legitimate Expectations: A Commentary of *Micula v. Romania*, 14 *Transnational Dispute Management* (2017, Issue 1).

⁵⁷⁸ *Electrabel GC*, supra note 563, para. 52.

⁵⁷⁹ *Ibid.*, para. 159.

Council had not authorized the aid scheme at the pre-accession stage, the claimants 'could never have entertained a legitimate expectation' that the aid scheme constitutes lawful state aid, 'regardless of the subsequent actions of the Romanian Government' after the decision of the Competition Council in May 2000.⁵⁸⁰⁵⁸¹ Similarly to the two judgments of the GC, the Commission relied on the abstract clarity of the state aid rules and ignored the difficulties Romanian authorities had in respect of the application and enforcement of the pre-accession state aid rules (and in understanding whether or not the entire scheme had to be revoked), which difficulties were an important element in the *Micula* tribunal's analysis.

The GC's judgments and the Commission's state aid decision in *Micula* demonstrate that the legitimate expectations doctrine has a high threshold of application under EU law. The relevant assurances of domestic or EU authorities have to be 'precise, unconditional and consistent', and addressed directly to the person relying on them; the content of the assurances have to give 'rise to a legitimate expectation on the part of the person to whom they are addressed'; and the assurances must also be compatible 'with the applicable rules'. Further, as noted, the ECJ has consistently held that economic operators 'cannot have a legitimate expectation that an existing situation which is capable of being altered by the Community institutions in the exercise of their discretionary power will be maintained'.⁵⁸² In the area of state aid the rules are equally strict: economic operators have to know whether an aid scheme was notified to and approved by the Commission prior to its application; they also have to know whether a pre-accession aid scheme qualifies as 'existing aid' (i.e. as legal state aid under EU law) under the provisions governing the host state's EU accession. Had the *Electrabel* and *Micula* tribunals applied the above EU law principles, the PPA termination claim and the legitimate expectations claim in *Micula* would have been rejected in a heartbeat, given that those principles assume that the claimants knew that the aid schemes were not authorized by the competent national authorities at the pre-accession stage.

Generally speaking, these cases suggest that arbitral tribunals *may* use different standards than the EU institutions to determine whether an investor's legitimate expectations were breached in the context of state aid, although the cases related to pre-accession aid

⁵⁸⁰ *Idem*.

⁵⁸¹ This last point referred to the decision of Romania to implement the aid scheme in a modified form, despite the Competition Council's finding that it violates the Europe Agreement.

⁵⁸² See *Delacre and others*, supra note 518, para. 33.

schemes. Admittedly, once a state has acceded to the EU, it is unlikely that investors can successfully challenge measures taken to comply with EU state aid rules, because the rules of the game should be clear to all stakeholders, including arbitral tribunals.⁵⁸³ However, disputes that relate to pre-accession regulatory changes may arise in the future. According to the UNCTAD investment treaty database, current candidate states and potential candidate states have 243 BITs.⁵⁸⁴ Out of these, 116 are concluded with current EU member states, with Serbia and Turkey respectively having 23 and 25 extra-EU BITs.⁵⁸⁵ Under the association agreements,⁵⁸⁶ candidate states (and potential candidate states) pledge to take sweeping political and economic reforms. For example, the EU-Serbia association agreement, which entered into force in September 2013, provides that the 'Parties recognize the importance of the approximation of the existing legislation in Serbia to that of the Community and of its effective implementation. Serbia shall endeavor to ensure that its existing laws and future legislation will be gradually made compatible with the Community acquis'.⁵⁸⁷ The association agreements also contain rules on competition policy that correspond to EU competition rules. These rules impose requirements on the candidate states and economic operators by proscribing the same practices as EU competition rules: practices which distort competition between the Community and the candidate state; abuses of a dominant market position; and granting of state aid 'which distorts or threatens to distort competition by favoring certain undertakings or certain

⁵⁸³ *Micula* is an outlier in this respect. In the Commission's view, it is Romania's compliance with the award that breaches EU state aid rules, rather than the 2004 revocation of the aid scheme.

⁵⁸⁴ Albania, Macedonia, Montenegro, Serbia and Turkey are candidate states, whereas Bosnia and Herzegovina and Kosovo are potential candidate states.

⁵⁸⁵ See at <http://investmentpolicyhub.unctad.org/IIA> (last visited 23 April 2016).

⁵⁸⁶ Officially Stabilization and Association Agreements (SAAs). These agreements were previously called Europe Agreements, but all existing agreements have the title of Stabilization and Association Agreement.

⁵⁸⁷ See Article 72(1) of the Stabilization and Association Agreement between the European Communities and their Member States of the one part, and the Republic of Serbia, of the other part, OJ L 278, 18.10.2013, pp. 16-473. For a similarly worded provision, see e.g. Article 70(1) of the Stabilization and Association Agreement between the European Communities and their Member States, of the one part, and the Republic of Albania, of the other part - Protocols - Declarations, OJ L 107, 28.4.2009, pp. 166-502; Article 70(1) of the Stabilization and Association Agreement between the European Communities and their Member States, of the one part, and Bosnia and Herzegovina, of the other part, OJ L 164, 30.6.2015, pp. 2-547. The agreements identify priority areas for the approximation of laws which relate to the fundamental elements of the internal market. Article 72(3) of the EU-Montenegro association agreement contains a standard provision in this regard as it provides that the approximation 'will, at an early stage, focus on fundamental elements of the Internal Market acquis, including financial sector legislation, Justice, Freedom and Security as well as on trade-related areas. At a further stage, Montenegro shall focus of the remaining parts of the acquis'. See Article 72(3) of the Stabilization and Association Agreement between the European Communities and their Member States, of the one part, and the Republic of Montenegro, of the other part, OJ L 108, 29.4.2010, pp. 3-354. Similar provisions are found in the other agreements as well (see e.g. Article 72(3) of the EU-Serbia agreement).

products'.⁵⁸⁸ While general changes in the regulatory framework that relate to the approximation of laws should not lead to successful BIT claims, it is not foreclosed that investors challenge changes in aid schemes they are entitled to, because the state aid rules are highly complex and their implementation at the pre-accession stage has proven to be a challenge.⁵⁸⁹

As to regulatory conflicts, in each case the parties agreed that there was no conflict between EU law and the relevant investment treaty. Apart from *Electrabel* where the Commission's state aid decision was part of the applicable law in the context of the PPA termination claim, EU law constituted a fact that was taken account of in different ways by the tribunals so as to assess whether the challenged measure was a rational public policy measure. Similarly, apart from *Electrabel*, the tribunals did not need to interpret and apply

⁵⁸⁸ See e.g. Article 71(1) of the EU-Albania agreement, supra note 588. The agreements also require that the candidate state establishes a national monitoring agency to carry out the application and enforcement of the competition rules. For example, Article 71(4) of the EU-Albania association agreement requires Albania to create 'an operationally independent authority which is entrusted with the powers necessary for the full application' of the state aid provision 'within four years from the date of entry into force' of the agreement. The general purpose of this and similar provisions is to ensure that the interpretation and application of the competition rules is aligned with EU competition rules and with the attendant practice of the EU institutions. For a useful discussion on these mechanisms and the role of the EU Commission, see Marise Cremona, 'State Aid Control: Substance and Procedure in the Europe Agreements and the Stabilization and Association Agreements', 9 *European Law Journal* (2003), pp. 265-287.

⁵⁸⁹ While much of the above discussion has focused on competition policy, state aid in particular, the SAAs also contain provisions on free movement of goods and capital, freedom to provide services and freedom of establishment, which follow, by and large, the logic of the internal market freedoms and the principle of equal treatment. These provisions are subject to numerous exceptions and often contain timelines for their gradual implementation, but it is not foreclosed that their implementation compels candidate states to take measures that affect aid schemes granted or assurances given to specific investors, leading the latter to take action under BITs. One example would be the withdrawal of the promise to renew public procurement contracts without inviting competing tenders - such promise clearly violates the non-discrimination principle in the context of freedom to provide services. The above general considerations apply to these situations as well. In principle, these remarks are also relevant in respect of association agreements concluded with third states that are not yet potential future member states or cannot become member states. While there is clear variance in the content of such agreements in comparison to those concluded with candidate states, these agreements usually contain rules on the fundamental market freedoms and competition policy as well as provisions under which the associate state commits to approximate its laws to specific areas of Union law. For example, Chapter VI of the Georgia-EU association agreement, which entered into force in July 2016, deals with establishment, trade in services and electronic commerce, and contains a number of articles under which Georgia commits to align its laws with those of the EU within specific timeframes, in particular with EU rules dealing with the provision of different types of services. Article 81 provides that Chapter VI provisions 'shall not affect the rights of entrepreneurs of the Parties arising from any existing or future international agreement relating to investment, to which a Member State of the EU and Georgia are parties.' The wording of Article 81 suggests that when Georgia implements the association agreement and an investor raises a claim under a BIT concluded between Georgia and an EU member state, the BIT takes priority in case of conflict. See Association Agreement between the European Union and the European Atomic Energy Community and their Member States, of the one part, and Georgia of the other part, OJ L 261, 30.8.2014, pp. 4-743. Most of the other association agreements in this category do not contain similar rules, but the point is that when investors challenge policy measures of associate states, those claims are evaluated according to similar principles as claims raised under the association agreements of candidate states if EU law related arguments are raised in the proceedings.

EU law to the merits, which begs the question of whether EU-law-as-fact poses a threat to the autonomy of the EU legal order. In *Electrabel*, the termination of the PPAs was attributed to the EU on the ground that the state aid decision had mandated that measure. If the ability of the EEA court and EctHR to assess the division of competences between the EU and its member states posed a threat to the autonomy of EU law, the question is whether the same principle applies in respect of arbitral tribunals, regardless of the fact that such assessments are not binding on the EU institutions.

5.4.2.2. The Spanish Solar Energy Cases

EU investors have lodged more than thirty claims against Spain under the ECT. These cases stem from the scaling back of certain solar energy subsidies between 2008 and 2014, and in the *Charanne* arbitration Spain referred to the Commission's 2015 decision to start a preliminary investigation over the compatibility of the original subsidy scheme with EU state aid rules.⁵⁹⁰ That scheme, adopted in 2007, was in part motivated by the 2001 renewable energy directive,⁵⁹¹ but Spain did not invoke the directive in the *Charanne* proceedings as a ground for the scheme or the subsequent amendments. However, the directive did provide that any subsidies which member states provide to investors so as to reach their renewable energy goals were without prejudice to the application of EU state aid rules.⁵⁹² It is also noteworthy that the 2001 directive did not contain any mandatory national targets as regards the production of renewable energy, whereas its successor, the 2009 directive, sets such targets which member states have to achieve by 2020.⁵⁹³ However, it is safe to assume that the latter directive is not directly relevant for the ECT cases, because member states retain much latitude in determining how to reach their national targets. It is also interesting that the Commission has expressly stated that the legislative changes that scaled back the subsidies did not breach the 2009 directive. The Commission reasoned that member states 'retain full discretion over whether they use

⁵⁹⁰ *Charanne B.V. & Construction Investments S.A.R.L. v. Spain*, SCC Case No. 062/2012, Award (hereinafter *Charanne* award, 21 January 2016).

⁵⁹¹ See Directive 2001/77/EC of the European Parliament and of the Council of 27 September 2001 on the promotion of electricity produced from renewable energy sources in the internal electricity market, OJ L 283, 27.10.2001, pp. 33-40.

⁵⁹² *Ibid.*, Article 4(1). This article provides that without '*prejudice to Articles 87 and 88 of the Treaty* [now Article 107 and 108 TFEU], the Commission shall evaluate the application of mechanisms used in Member States according to which a producer of electricity, on the basis of regulations issued by the public authorities, receives direct or indirect support, and which could have the effect of restricting trade, on the basis that these contribute to the objectives set out in Articles 6 and 174 of the Treaty' (emphasis added).

⁵⁹³ Directive 2009/28/EC of the European Parliament and of the Council of 23 April 2009 on the promotion of the use of energy from renewable sources and amending and subsequently repealing Directives 2001/77/EC and 2003/30/EC, OJ L 140, 5.6.2009, pp. 16-62 (see annex I for the national targets).

support schemes or not and, should they use them, over their design, including both the structure and the level of support'. This discretion includes the right to 'enact changes to their support schemes, for example to avoid overcompensation or to address unforeseen developments such as a particularly rapid expansion of a precise renewables technology in a given sector'. The Commission concluded that the 2009 directive provides no grounds 'to take legal action against Spain with regard to the legislative changes which affected the level of support given to investors in renewable energy projects', and the affected investors were advised to seek judicial review before national courts if they considered that the scaling back breached their legitimate expectations.⁵⁹⁴

But the Commission also remarked that 'support schemes' for the production of renewable energy 'need to be compatible with the Guidelines on State aid for environmental protection and energy in as far as they constitute state aid'.⁵⁹⁵ Pending state aid investigations are confidential, but it is known that the Commission's investigation includes the Spanish law which introduced the generous feed-in-tariff system for solar energy production and quickly led to an investment boom.⁵⁹⁶ It appears that Spain had not notified the aid scheme to the Commission, most likely because it assumed that the feed-in-tariff system fulfills the criteria of lawful state aid established both in numerous Commission guideline documents, which exempt certain categories of aid from the notification obligation, as well as in the case law of the ECJ. Be that as it may, if the Commission finds that the aid scheme constitutes unlawful state aid, the question is what implications it has for the pending arbitrations. Should the above principles apply, it would mean that under EU law the affected investors could not entertain any legitimate expectations that the scheme is compatible with EU law if the Commission had not expressly authorized it. Without the Commission's approval, there would be appear to be no exceptional circumstances either that enabled investors to legitimately assume that the scheme is compatible with EU law. Likewise, explicit assurances of Spanish authorities that the scheme is lawful state aid would be materially irrelevant. To paraphrase the ECJ, diligent solar energy producers should normally be able to determine whether Spain had followed the state aid procedure prior to implementing the aid scheme.

⁵⁹⁴ The Commission expressed these remarks in the context of a petition submitted to the European Parliament on behalf of a Spanish renewable energy association. See European Parliament, Committee on Petitions, *Notice to Members, Petition No 2520/2014, on the situation of the photovoltaic sector and the legality of the changes made to the law by the Spanish government*, 29 February 2016.

⁵⁹⁵ *Idem*.

⁵⁹⁶ See *Charanne* award, *supra* note 590, para. 449.

Both Spain and the Commission argue that the 2001 and 2009 directives are materially unconnected to the scaling back of the subsidies, implying that the directives play no role in the pending arbitrations. But the Commission's state aid investigation may complicate matters to *Micula* like proportions. In May 2017, the *Eiser* tribunal held that Spain had breached the ECT's fair and equitable treatment by one of the relevant measures (adopted in 2014) and awarded the claimants €128 million in damages.⁵⁹⁷ In principle, the enforcement of the *Eiser* award could breach EU state aid rules,⁵⁹⁸ but this hinges on the Commission's findings: the implications are different depending on which version(s) of the aid schemes constitute illegal state aid. It is also uncertain whether the Commission would obligate Spain to recover the incompatible aid in full or whether countervailing considerations could exempt recovery, although this should only be possible if the recovery breaches a general principle of EU law. Any finding of incompatibility would probably be appealed to the ECJ, which may eventually come to a different conclusion than the Commission. I have worked on the assumption that arbitral tribunals will defer to the Commission's state aid decision, as the *Electrabel* tribunal did, but it is not guaranteed that tribunals go along this path. The *Charanne* tribunal referred to the Commission's state aid investigation, but since it was pending it had no bearing on the merits.⁵⁹⁹ Regardless of the outcome of the Commission's investigation, Spain could also invoke the Commission's position that the amendments to the aid scheme did not violate the 2009 directive or other EU law provisions, and provide no ground for infringement proceedings under EU law, even if this would only be a factual element in the analyses of tribunals (on the assumption that the 2009 directive cannot be invoked as a ground for the amendments). Here, the EU law compatibility of the amendments would support the argument that the scaling back was a reasonable policy based on sound public interest considerations. Arguably, these types of references to EU law constitute only a 'light touch' to EU law, and it would seem

⁵⁹⁷ See *Eiser Infrastructure Limited and Energia Solar Luxembourg S.À R.L. v. Spain*, ICSID Case No. ARB/13/36, Award, 4 May 2017. In the other two arbitrations that have concluded at the time of writing, the tribunals rejected the claimants' claims based on the scaling back of the subsidies. In the *Isolux* arbitration, the tribunal assessed the same measures as the *Eiser* tribunal, but saw that these did not constitute a breach of the claimant's legitimate expectations. See *Isolux Netherlands, BV v. Kingdom of Spain*, SCC Case V2013/153, Award, 12 July 2016. The *Charanne* arbitration concerned earlier modifications to the aid scheme, but again the tribunal rejected the claimant's claims.

⁵⁹⁸ Spain had argued that 'European authorities might regard any monetary award by the Tribunal in favor of the Claimants as impermissible state aid, implying that payment of such an award by Spain would be contrary to European law'. See *Eiser* award, supra note 597, para. 173.

⁵⁹⁹ *Idem*. Spain argued (see at para. 224) that if the Commission finds that the subsidy program constitutes illegal state aid and the tribunal decides the dispute in favor of the claimants, it is probable that the award is unenforceable due to its compatibility with EU state aid rules.

plausible to argue that such light touches do not pose a threat to the autonomy of EU law, because the directive grants broad discretionary powers to the member states.

A final observation is that the more than 30 claims brought against Spain are somewhat paradoxical, as they are challenging Spain's failure to uphold pro-environmental legislation, which is one of the central general concerns of the critics.

5.4.2.3. The Vattenfall v. Germany (No. 1) Case

Vattenfall started to plan the construction of a coal-fired power plant on the bank of Elbe in 2004. The power plant's site was situated on the outskirts of Hamburg, and at first local politicians not only gave the go-ahead to the project, but suggested that Vattenfall build a larger plant than originally planned. The company agreed, approved the €2.2 billion investment, and received a preliminary permit to start the construction as well as assurances on the conditions under which the plant was to be operated, including the amount of water it could abstract from and release back to the Elbe. Around the same time, the political climate in Hamburg and elsewhere in Germany started to shift, with anxieties over the implications of climate change becoming a more urgent political concern, in particular in the wake of the 2006 Stern report on the economics of climate change. In 2008, Hamburg city-state elections brought to power a CDU-Green alliance, which led to a review of the project and the imposition of more stringent conditions on the plant's operation. As a result, Vattenfall filed a claim against Germany under the ECT, claiming that the delays in the authorization of the final permit and the stricter environmental conditions would render the plant economically unviable. The case was settled in 2010, and while the details of the settlement remain confidential, media reports implicated that Germany thinned the water-use limitations imposed on Vattenfall in the final permit.⁶⁰⁰

The power plant started to operate in February 2015, but already before this the Commission had started infringement proceedings against Germany on the ground that it had failed to 'apply the requirements of the Habitats Directive in relation to the authorization of a coal power plant in Hamburg/Moorburg'. The operation of the power plant risked 'having a negative impact on a number of protected fish species', and since

⁶⁰⁰ These facts are derived from Sebastian Knauer, 'Vattenfall vs. Deutschland: Machtkampf um Moorburg', *Der Spiegel*, 11 July 2009; IAREporter, 'Parties announce settlement of dispute over German power plant', *IAREporter News*, 28 August 2010.

Germany had repeatedly refused to perform an assessment of alternatives to the planned operating process, as the directive required, the Commission referred the matter to the ECJ in March 2015,⁶⁰¹ which rendered its judgment in April 2017. Germany's original 2008 environmental impact assessment (EIA) had shown that the plant's operation would adversely affect certain fish species protected under the Habitats Directive. Germany had taken certain precautionary measures to protect those species, but since there was no 'definitive data' as to the effectiveness of those measures at the time the plant's construction was authorized, it had failed to fulfil its obligations under Article 6(3) of the Habitats Directive. Article 6(3) requires that such authorization is given only after it is certain that the plant's operation 'will not adversely affect the integrity of the site concerned' (i.e. the site through which the fish species migrate).⁶⁰² Such finding implies, in principle, that Germany is obligated to carry out a new EIA to determine whether the precautionary measures prevent the negative effects on 'the integrity of the site'. What complicates matters, however, is the fact that the settlement between Vattenfall and Germany loosened the environmental requirements in comparison to the 2008 permit. For example, the fish monitoring standards became less strict under the terms of the settlement.⁶⁰³

Depending on the conclusions of the new EIA, Germany might have to impose new requirements on the plant's operation, with Vattenfall potentially reopening the arbitration proceedings under the ICSID Convention. Arguably, since this is an intra-EU dispute (Swedish investor v. Germany), the Habitats Directive should take priority over the ECT as a matter of EU law, and the principle that treaties concluded by the EU take priority over secondary EU law is materially irrelevant. If the *Electrabel* tribunal's finding that EU law and the ECT are compatible is applied (by analogy), the implementation of the directive cannot be successfully challenged under the ECT, also because Article 1(3) ECT recognizes the power of the EU to take binding decisions in matters governed by the ECT, which decisions bind the member states. If the directive is an element of fact in our hypothetical case, Germany could argue that it is uncontested that the Habitats Directive is a rational and non-discriminatory response to a legitimate policy concern, which cannot

⁶⁰¹ European Commission press release, 'Environment: Commission refers Germany to Court over coal power plant in Moorburg', IP/15/4669, Brussels, 26 March 2015. See also Council Directive 92/43/EEC of 21 May 1992 on the conservation of natural habitats and of wild fauna and flora (Habitats Directive), OJ L 206, 22.7.1992, pp. 7-50.

⁶⁰² Case C-142/16, *Commission v Germany*, ECLI:EU:C:2017:301, paras. 37 and 45.

⁶⁰³ Laurens Ankersmit, 'Case C-142/16 Commission v Germany: The Habitats Directive Meets ISDS?', *European Law Blog*, 6 September 2017.

constitute a breach of the ECT protection standards. Further, since the environmental requirements would be based on the Habitats Directive, Germany could argue that the tribunal lacks jurisdiction, because its actions are attributable to the EU as a matter of international law.

The *Vattenfall* case is indicative of the fact that conflicts between EU acts and member state BITs and the ECT may arise outside competition law as well. If the Commission has monopoly over the authorization of state aid schemes under EU law, national authorities play a central role in other subject areas over which the EU has competences, including other areas of competition policy. If regulatory conflict arguments are often less compelling than 'EU law as fact' arguments, the general question is under which conditions investors can entertain legitimate expectations over the stability of the EU regulatory framework, and whether arbitral tribunals should apply the legitimate expectations doctrine as it stands under EU law. In state aid matters the basic EU law principles are well established, but it is difficult to assess what type of principles should apply in other policy areas. From the perspective of arbitral tribunals, much will depend on the clarity and precision of the relevant EU legislation, on the attendant practice of the EU institutions, on the assurances and representations given to the claimant investor, and on the linkage that the challenged domestic act has to the requirements of specific EU law instruments. Generally speaking, once a state has acceded to the EU, investors are subject to the requirements of the legitimate expectations doctrine as it stands under EU law and they should not be able to (successfully) resort to BIT protections when they cannot obtain redress for a regulatory change under EU law. The same principle should apply in respect of state aid matters. As to the distinction between intra-EU and extra-EU BITs, it seems plausible to argue that nationality should play no role in assessing whether the investor could entertain legitimate expectations. As to the autonomy of the EU legal order, given the broad range of EU acts and the differences in the discretion they leave to the member states, the autonomy concerns will vary in accordance with the underlying circumstances. The central question is whether the interpretation of EU law by an arbitral tribunal, as such, may pose a threat to the autonomy of EU law or whether those interpretations need to have some sort of binding effects within the EU legal order before a 'manifest risk' arises.

5.5. General Assessment and Arguments Supporting the Compatibility of BIT Arbitration Clauses with the Autonomy of the EU Legal Order

The previous section showed that regulatory conflict arguments are rarely invoked in practice. The legitimate expectations doctrine played a central role in determining whether the claimant's treatment was fair and equitable, with the parties having different views over the role and weight that EU law should have in the resolution of the dispute. As to the autonomy of the EU legal order, the *Electrabel* tribunal's use of EU law 'went furthest', but in most cases EU law was a factual element that played a relatively modest role in the tribunals' analyses. It is relatively easy to imagine multiple scenarios where arbitral tribunals *may* have to engage with EU law similarly to the *Electrabel* tribunal. For example, a member state may implement the National Emissions Ceiling Directive by imposing more stringent environmental conditions on power generators.⁶⁰⁴ An affected investor could bring a claim under a relevant BIT, arguing that the new requirements constitute unfair and inequitable treatment as they place an unreasonable burden on power generators in comparison to other business sectors and economic operators. As to the directive, the investor could argue that it is only a factual element that cannot override the member state's BIT obligations, and that in any case the directive did not require that power generators are overburdened to meet the relevant emission targets. In such case, the arbitral tribunal would not only have to determine to what extent the directive is relevant when the domestic act of implementation is assessed in light of the BIT standards, but also interpret the directive to understand what it requires from the member states. Likewise, the member state could argue that the domestic act of implementation is attributable to the EU under international law as it was based solely on the requirements of the directive. Depending on the circumstances of the underlying dispute, these and analogous arguments will have varying degrees of plausibility, but the point is that when addressing such arguments, arbitral tribunals will have to interpret the EU law instrument and, if the issue of attribution is raised, assess the division of competences between the EU and its member states.⁶⁰⁵

⁶⁰⁴ See Directive (EU) 2016/2284 of the European Parliament and of the Council of 14 December 2016 on the reduction of national emissions of certain atmospheric pollutants, amending Directive 2003/35/EC and repealing Directive 2001/81/EC, OJ L 344, 17.12.2016, pp. 1-31.

⁶⁰⁵ The content of the invoked EU law provisions may not require any interpretation on the tribunal's part, for example, when the EU courts have provided a conclusive interpretation, and this could be raised to argue that the *acte clair* doctrine applies similarly in respect of arbitral tribunals. In other words, when there is no doubt

In Opinions 1/91 and 2/13, the agreements under scrutiny enabled the EEA court and the EctHR to assess the division of competences between the EU and its member states for the purposes of attributing responsibility for a specific act or omission. This was 'likely adversely to affect the allocation of responsibilities defined in the Treaties and, hence, the autonomy of the Community legal order'.⁶⁰⁶ Importantly, it appeared that the ability of the two courts to address the question of competence alone led to a finding of incompatibility. In other words, it was irrelevant whether or not (e.g.) the EEA court's assessment of competences bound the ECJ. If an arbitral tribunal determines the question of competence directly, or indirectly by attributing a measure either to the EU or the respondent state, it would appear that this is equally problematic from the perspective of autonomy. Such determination is final and binding and will determine the outcome of (at least some aspect) of the dispute. The ECJ could become involved and review the tribunal's assessment under certain conditions and therewith safeguard the autonomy of EU law.⁶⁰⁷ However, these conditions entail limitations on the ECJ's review powers, and I will address them below.

The BGH made a number of interesting points on the scope of Article 344 TFEU in its referral to the ECJ, with *MOX Plant* playing a central role. The wording of Article 344 TFEU does not provide conclusive answer to the question of whether it applies to disputes between member states and private parties.⁶⁰⁸ In Opinion 2/13, the ECJ held that Article 344 TFEU applies to disputes between the EU and its member states,⁶⁰⁹ and the General Court has held that a pre-accession arbitration clause in an agreement between the EU Commission and the Czech Republic came within the article's scope.⁶¹⁰ In Opinion 1/09,

about the meaning of specific EU law provisions, the autonomy of the EU legal order is not threatened. But even if this argument is plausible as such, it does not remove the possibility that under any given arbitration clause disputes can arise in which the parties raise EU law instruments, the meaning of which is unclear.

⁶⁰⁶ *Opinion 1/91*, supra note 362, para. 35. In *Opinion 2/13*, supra note 439, para. 235, the ECJ held that 'the arrangements for the operation of the co-respondent mechanism laid down by the agreement envisaged do not ensure that the specific characteristics of the EU and EU law are preserved.' While the Court used different phrases to make a finding of incompatibility, the basis of the conclusion was similar in both opinions.

⁶⁰⁷ Of course, member state BITs are binding on the contracting states alone and the EU cannot be a respondent in a dispute raised under them. Similarly, the EU was to become party to the EEA agreement and the ECHR, whereas it is not and will not be a party to member state BITs. However, and arguably, the Court's take on the question of competence was not based on the possibility of the EU being a respondent in disputes brought under the EEA agreement and the ECHR or on the EU's status as a contracting party.

⁶⁰⁸ As the BGH put it, 'Der Wortlaut des Art. 344 AEUV lässt allerdings keinen eindeutigen Schluss darauf zu, ob die Bestimmung auch für Streitigkeiten zwischen einer Person des Privatrechts und einem Mitgliedstaat gilt.' See *Eureka* referral, supra note 150, para. 27. Another issue is whether Article 344 TFEU applies to disputes between member states and third state private parties or only to disputes between member states and private parties having an EU nationality.

⁶⁰⁹ *Opinion 2/13*, supra note 439, para. 202 ff.

⁶¹⁰ See Case T-465/08, *Czech Republic v European Commission*, ECLI:EU:T:2011:186, paras. 95-102.

disputes between two private parties in the field of patents were outside the sweep of Article 344 TFEU, but none of these findings shed light on the relationship of BIT arbitration clauses and Article 344 TFEU. Academic commentators remain divided over the issue, but the majority concur with arbitral tribunals and hold that the article's scope is limited to disputes between member states.⁶¹¹ The BGH noted that Article 344 TFEU refers expressly to disputes 'concerning the interpretation or application of the Treaties'. When analyzing this phrase, the BGH referred to *MOX Plant* and inferred that Article 344 TFEU is not necessarily breached when non-EU courts use EU law as an interpretative aid so as to determine whether a provision in a non-EU treaty is breached.⁶¹² The BGH then held, crucially, that *MOX Plant* suggests that Article 344 TFEU is breached only when the non-EU court's decision is based on the interpretation and application of EU law, and the BGH made an express reference to the ECJ's finding that Ireland submitted the EU law instruments to the UNCLOS 'tribunal for purposes of their interpretation and application in the context of proceedings seeking a declaration that the United Kingdom had breached the provisions of those instruments'.⁶¹³ Further, and as noted, the BGH's referral stemmed from the *Eureko* arbitration, and the compensation that the claimant investor had received was based solely on a breach of the Dutch-Slovak BIT. As the award entailed no declaration that the Slovak Republic had breached its obligations under EU law, the BGH reasoned that the dispute fell outside the scope of Article 344 TFEU.⁶¹⁴ This would imply that if a tribunal declares that a member state has breached EU law, investment disputes come within the scope of Article 344 TFEU, but as noted such declarations are unlikely to occur in practice because in most arbitrations EU law is a factual element rather than part of the applicable law. As to *Electrabel*, the tribunal's finding on attribution did not entail any

⁶¹¹ See e.g. Dimopoulos, 'The Validity and Applicability of International Investment Agreements', supra note 26, at 86-87; Christer Söderlund, 'Intra-EU Investment Protection and the EC Treaty', 24 *Journal of International Arbitration* (2007), pp. 455-468, at 459-460; Eilmansberger, 'Bilateral Investment Treaties and EU Law', supra note 26, at 404; Wehland, 'Intra-EU Investment Agreements and Arbitration', supra note 280, at 318-319. For the opposing view, see Hindelang, 'Circumventing Primacy of EU Law', supra note 26, at 199 (footnote 82). For the view that the scope of Article 344 is uncertain, see Konstanze von Papp, 'Clash of "Autonomous Legal Orders": Can EU Member State Courts bridge the Jurisdictional Divide between Investment Tribunals and the ECJ? A Plea for Direct Referral from Investment Tribunals to the ECJ', 50 *Common Market Law Review* (2013), pp. 1039-1082, at 1052-1054.

⁶¹² See *Eureko* referral, supra note 150, para. 32 (in the BGH's words, the *MOX Plant* judgment suggests that 'für einen Verstoß gegen Art. 344 AEUV wohl nicht ausreichen, dass ein Schiedsgericht Unionsrecht als Auslegungskriterium für eine nicht dem Unionsrecht angehörende Bestimmung berücksichtigt').

⁶¹³ Idem. ('Vielmehr könnte ein Verstoß gegen Art. 344 AEUV erst vorliegen, wenn Gegenstand der Entscheidung des Schiedsgerichts die Auslegung und Anwendung unionsrechtlicher Vorschriften selbst ist'), with reference to paras. 140, 149 and 151 of *MOX Plant*, supra note 348 (the quote is from para. 151).

⁶¹⁴ Ibid., paras. 32-33.

assessment of whether Hungary had breached its EU law obligations, but the finding nonetheless creates autonomy concerns.

The above discussion suggested that *MOX Plant* could be understood in another way for two main reasons. First, I argued that the ECJ's finding on the 'manifest risk' to the autonomy of the EU legal order was based solely on Ireland's invocation of the EU law instruments at the UNCLOS proceedings, and the question of how the tribunal was to use those instruments (either as facts or applicable law) was, to quote the Court, 'entirely irrelevant' to the existence of that risk. Second, I pointed out that arbitral tribunals assess the respondent member state's actions against the treaty under which they were established (e.g. a BIT or the UNCLOS) and not against the provisions of EU law, just as the ECJ did in *Commission v Slovakia*. Unless the parties raise regulatory conflict arguments or argue that EU law takes priority over the BIT, EU law is only a factual element and not part of the law that applies to the merits. Hence, the BGH's implicit suggestion that the decision of the UNCLOS tribunal could be based on the interpretation and application of EU law is incorrect to the extent that the material dispute between Ireland and the UK could only be resolved by applying the provisions of the UNCLOS to the merits of the dispute. While the ECJ's own analysis blurred the fact/applicable law dichotomy, the *MOX Plant* judgment could still be read as implying that Article 344 TFEU is breached, in disputes between member states, when a non-EU court interprets and applies EU law to ascertain its meaning as fact, because the Court held that the autonomy of the EU legal order was under threat regardless of whether the EU law instruments were raised as facts or as applicable law.

This finding was not connected to the twin-fact that the UNCLOS was part of EU law and that many of its provisions fell under EU competence. Further, the UNCLOS provisions that Ireland had invoked came within the scope of EU competence, which meant that the Court had exclusive jurisdiction to settle disputes between member states concerning those provisions, but again this point was not tied to the finding that Ireland's invocation of the (non-UNCLOS) EU law instruments posed a manifest risk to the autonomy of the EU legal order. In other words, it appears that the autonomy doctrine was raised independently of Article 344 TFEU. Interestingly, the BGH made a connection between Articles 259 and 344 TFEU to support the argument about the latter's inapplicability to investment arbitration. Article 259 TFEU allows a member state to raise a claim against another

member state before the ECJ for an alleged failure 'to fulfil an obligation under the Treaties'. The BGH saw that Article 344 TFEU obligates member states to use the procedure under Article 259 TFEU when their dispute concerns EU law.⁶¹⁵ The BGH then referred to *MOX Plant* where the Court held that the dispute between Ireland and the UK was covered by a method of settlement in the meaning of Article 344 TFEU, and that method of settlement was found in what is now Article 259 TFEU.⁶¹⁶ The BGH argued that there is no equivalent provision under EU law allowing investors to bring actions for damages against member states. In other words, disputes between member states were covered by Article 344 TFEU, because Article 259 TFEU provided a method for their settlement, whereas the founding treaties contained no 'method of settlement' for disputes between EU investors and member states. The preliminary ruling procedure under Article 267 TFEU was not such a method of settlement either. When investors bring actions for damages against member states before domestic courts, these courts can submit preliminary questions to the ECJ, but this was not a 'method of settlement' in the meaning of Article 344 TFEU, but an interim procedure for resolving a question of EU law in a national '*Streitbeilegungsverfahren*'.⁶¹⁷ It is noteworthy that in *MOX Plant* the ECJ held that the UNCLOS arbitration was a 'method of settlement other than those provided for' under EU law, as the tribunal's decision was to be final and binding on the disputing parties.⁶¹⁸ By analogy, investment arbitration qualifies as such 'method of settlement' in the meaning of Article 344 TFEU, as awards of tribunals are final and binding, but this analogy is relevant only if investment disputes fall under the article's scope in the first place.

I argued that the Court misunderstood the jurisdiction of the UNCLOS tribunal, because arbitral tribunals will not make formal declarations on alleged breaches of EU law. EU law can be part of the applicable law only if a member state argues that its obligation to implement an EU act takes priority over its BIT (or UNCLOS) obligations, which assumes

⁶¹⁵ *Ibid.*, para. 34

⁶¹⁶ *MOX Plant*, supra note 348, para. 128.

⁶¹⁷ *Eureko* referral, supra note 150, para. 35.

⁶¹⁸ *MOX Plant*, supra note 348, para. 129. Here, Article 296 UNCLOS is relevant and reads as follows: '1. Any decision rendered by a court or tribunal having jurisdiction under this section shall be final and shall be complied with by all the parties to the dispute. 2. Any such decision shall have no binding force except between the parties and in respect of that particular dispute.'

the existence of conflict,⁶¹⁹ but even in this scenario the tribunal would not rule on breaches of EU law, as the conflict could only be resolved by applying a conflict rule of international law. Or, alternatively, the member state could argue that its relevant EU law and BIT obligations constitute a harmonious set of obligations which implies that the challenged measure is compatible with the BIT as it was mandated by EU law. However, arbitral tribunals assess the challenged measure only against the relevant BIT standards, so in the latter scenario EU law cannot rise to the level of applicable law in the sense that the tribunal would apply EU law to the merits. The point of this quibbling is that unless conflict arguments are raised, EU law is necessarily a factual element in the tribunal's analysis, although it may constitute a direct (and only) basis for the finding that the challenged measure was (or was not) a rational public interest measure which does not breach the BIT. Another scenario is one where the member state argues that the challenged measure is attributable to the EU, which would render the claim inadmissible as a matter of international law, but here too EU law would not be part of the applicable law as the question of attribution is decided on the basis of the relevant rules of international law.

This suggests that *MOX Plant* and the four opinions could be read in two ways. First, as implying that member states are not allowed to refer disputes to a court or a tribunal if the dispute raises questions of EU law. Even if the presiding body's jurisdiction extends only to the treaty (e.g. UNCLOS, BIT) under which it was created, the invocation of EU law instruments by a member state creates a manifest risk to the autonomy of EU law. This would suggest that each arbitration clause in member state BITs creates such a risk, because of the *possibility* that member states invoke EU law instruments in given cases. Second, the Court's approach could indicate that whatever the status of EU law is in an arbitration, the crucial question is whether the tribunal's interpretation (and/or application) of EU law produces binding effects in one or another way. Arbitral awards are final and binding, but only on the disputing parties, and the Court alluded to this when it held that UNCLOS arbitrations are a form of dispute settlement in the meaning of Article 344 TFEU. The first reading would broaden the scope of the autonomy doctrine but also set relatively clear limits to it, whereas the second reading raises the difficult question of whether or not arbitral awards have 'binding effects' within the EU legal order. The first

⁶¹⁹ Clearly, if there is no conflict, and the member state argues that EU law is part of the applicable law, the argument is based on a flawed logic; in such cases EU law can only be a fact because the tribunal assesses the challenged measure against the applicable BIT.

reading would also raise the question of whether autonomy is safeguarded adequately if member state courts and the ECJ can review the EU law engagements of arbitral tribunals. The following tackles these two questions, as well as addresses the question about the scope of Article 344 TFEU.

Many of the Court's opinions emphasize the centrality of the preliminary ruling procedure for the uniform interpretation of EU law and for ensuring that EU law has the same effect in all member states.⁶²⁰ In Opinion 2/13, the Court alluded to this by noting that the 'interpretation of a provision of EU law, including of secondary law, requires, in principle, a decision of the Court of Justice where that provision is open to more than one plausible interpretation'.⁶²¹ In most of the arbitral cases discussed above, the seat of the tribunals was in an EU member state. This meant that the disputing parties could turn to national courts during and after the arbitral process, with the ECJ (potentially) becoming involved through the preliminary ruling procedure. This is of course what happened in *Eureko*. The Slovak Republic challenged the final award before German courts, but already during the arbitral proceedings the Slovak Republic requested the tribunal to submit preliminary questions to the ECJ on the compatibility of the BIT's arbitration clause with EU law.⁶²² In *Eastern Sugar*, the Czech Republic made a similar request,⁶²³ but in both cases the tribunals rejected the requests. Three questions arise: first, can arbitral tribunals submit preliminary questions; second, to what extent can member state courts and the ECJ review the decisions of arbitral tribunals, in particular their interpretations of EU law; and third, what implications do the answers to the two previous questions have for the relationship of BIT arbitration clauses and the autonomy of the EU legal order.

Generally speaking, each state has its own rules of procedure which determine the ways in which arbitral tribunals and the parties can resort to national courts at different stages of the arbitral process. In its referral, the BGH noted that the German *Zivilprozessordnung* (ZPO) contained a provision allowing arbitral tribunals to request German courts, for

⁶²⁰ For example, in *Opinion 2/13*, supra note 439, para. 176, the ECJ held that the preliminary ruling procedure is the 'keystone' of the EU legal order and 'has the object of securing uniform interpretation of EU law...thereby serving to ensure its consistency, its full effect and its autonomy as well as, ultimately, the particular nature of the law established by the Treaties.' Similarly, in *Opinion 1/09*, supra note 354, para. 83, the preliminary ruling procedure was described as guaranteeing that EU law 'has the same effect' in the member states and as aiming to 'avoid divergences in the interpretation' of EU law.

⁶²¹ *Opinion 2/13*, para. 440.

⁶²² See *Eureko* award, supra note 74, para. 148.

⁶²³ *Eastern Sugar* award, supra note 98, para. 130.

example, to carry out judicial acts which the former are not authorized to do under German law.⁶²⁴ The BGH referred to the *überwiegend* view of German commentators that Article 1050 ZPO allows German courts to submit preliminary questions to the ECJ on the interpretation of an EU law provision on the request of an arbitral tribunal.⁶²⁵ However, since Article 8(5) of the Dutch-Slovak BIT provided that the 'tribunal shall determine its own procedure applying the arbitration rules of the United Nations Commission for International Trade Law (UNCITRAL)', the BGH saw that the tribunal could not invoke the ZPO provision to make a request concerning the preliminary ruling procedure.⁶²⁶ National rules of procedure do not necessarily allow arbitral tribunals to use national courts to obtain the ECJ's interpretation on a relevant EU law question, and even when they accommodate such requests, tribunals are not obligated to make one. Two commentators have also argued that the wording of Article 267 TFEU and the Court's judgment in *Roda Golf* suggest that a member state court can refer preliminary questions 'only if there is a case pending before it and if it is called upon to give judgment in proceedings intended to lead to a decision of a judicial nature.'⁶²⁷ Arguably, a request to a member state court by an arbitral tribunal to submit preliminary questions on its behalf does not fulfil this requirement, with the ECJ potentially rejecting such requests.⁶²⁸ Likewise, the seat of arbitral tribunals may be outside the EU, in which case the proceedings are subject to the procedural law of the seat state, with member state courts and the preliminary ruling procedure being excluded from the process at all stages of the arbitration.⁶²⁹

National rules of procedure may provide an indirect access to the ECJ, but can arbitral tribunals submit preliminary questions directly to the Court, without an intermediary? Arguably, *if* arbitral tribunals were authorized *and* obligated to submit preliminary

⁶²⁴ See Article 1050 of the Zivilprozessordnung (the relevant part reads as follows: 'Das Schiedsgericht oder eine Partei mit Zustimmung des Schiedsgerichts kann bei Gericht Unterstützung bei der Beweisaufnahme oder die Vornahme sonstiger richterlicher Handlungen, zu denen das Schiedsgericht nicht befugt ist, beantragen.'

⁶²⁵ *Eureka* referral, *supra* note 150, para. 51. For one such view in German legal commentary, see Bernhard Wieczorek, Rolf A. Schütze et al. (eds.), *Zivilprozessordnung und Nebengesetze Großkommentar*, Band 11 (De Gruyter, 4th ed. 2014), p. 602.

⁶²⁶ *Ibid.*, para. 52.

⁶²⁷ Case C-14/08, *Roda Golf & Beach Resort SL*, ECLI:EU:C:2009:395, para. 34

⁶²⁸ This is the argument in Miloš Olik and David Fyrbach, 'The Competence of Investment Arbitration Tribunals to Seek Preliminary Rulings from European Courts', 2 *Czech Yearbook of International Law* (2011), pp. 191-205, at 202-203.

⁶²⁹ Apart from situations where the winning party seeks the award's enforcement in a member state, but given the narrow grounds under which an award's enforcement can be challenged, it is unlikely that a member state court can submit a preliminary question concerning the tribunal's interpretation of particular EU law provisions.

questions to the ECJ whenever questions of EU law arise to which there is no clear answer, this could eliminate any and all autonomy concerns. The ECJ has not ruled on this specific issue and its case law on commercial arbitration provides support for opposing arguments on whether arbitral tribunals qualify as 'ordinary courts' for the purposes of Article 267 TFEU.⁶³⁰ Academic commentators disagree over the matter,⁶³¹ but it seems unnecessary to address this question in detail. Assuming that the ECJ authorizes arbitral tribunals to submit preliminary questions, the latter would not have a legal obligation to do so unless the relevant treaty articles are amended accordingly.⁶³² As tribunals have thus far rejected requests to use the preliminary ruling procedure, it is unlikely that they will change course unless obligated to do so under law. Hence, on the assumption that tribunals are authorized to use the preliminary ruling procedure, it does not, at present, ensure that member state courts and the ECJ become involved so as to review the way in which tribunals have interpreted EU law in particular cases.

Arbitral tribunals have referred to the *Eco Swiss* and *Nordsee* cases to support the thesis that BIT arbitration clauses are compatible with EU law.⁶³³ In both cases, the ECJ emphasized that when questions of EU law are raised in a commercial arbitration, member state courts 'may be called upon to examine them either in the context of their collaboration with arbitration tribunals, in particular in order to assist them in certain procedural matters

⁶³⁰ In *Nordsee* the ECJ held that the referring arbitral tribunal was not a court or tribunal of a member state in the meaning of Article 267 TFEU and could not submit preliminary questions to the Court. See Case C-102/81, *Nordsee Deutsche Hochseefischerei GmbH v. Reederei Mond Hockseefischerei Nordstern AG* ECLI:EU:C:1982:107, paras. 11-13. The Court made a similar finding in the *Denuit and Cordenier* case, indicating that commercial arbitration tribunals do not, as a rule, qualify as courts of member state for the purposes of Article 267 TFEU. See Case C-125/04, *Guy Denuit und Betty Cordenier v. Transorient – Mosaique Voyages und Culture SA*, ECLI:EU:C:2005:69, paras. 11-17. However, the Court has also ruled that under certain conditions an arbitral tribunal can qualify as a court or tribunal of a member state. See Case 109/88, *Dansk Arbejdsgiverforening*, ECLI:EU:C:1989:383, paras 7-8. For a useful discussion on the criteria of an 'ordinary court' established in the relevant ECJ case law, see von Papp, 'A Plea for Direct Referral from Investment Tribunals to the ECJ', supra note 611, at 1066-1079.

⁶³¹ For the argument that investor-state tribunals cannot use the preliminary ruling procedure, see Dimopoulos, 'The Validity and Applicability of International Investment Agreements', supra note 26, p. 91 (footnote 98). For the opposing argument, see Hindelang, 'Circumventing Primacy of EU Law', supra note 26, pp. 201-203; Jürgen Basedow, 'EU Law in International Arbitration: Referrals to the European Court of Justice', 32 *Journal of International Arbitration* (2015), pp. 367-386, at 378-381. See also Case C-567/14, *Genentech*, Opinion of Advocate General Wathelet, ECLI:EU:C:2016:177, para. 59 (footnote 34, where the Advocate General supports the idea that ICSID tribunals could qualify as 'ordinary courts' and submit preliminary questions).

⁶³² This would at least require the inclusion in member state BITs of a clause providing that arbitral tribunals qualify as courts and tribunals in the meaning of Article 267 TFEU, and are thus bound by its contents. It is unclear whether the EU founding treaties would have to be amended. It is equally uncertain whether tribunals whose seat is in a third state could be authorized to use the preliminary ruling procedure.

⁶³³ *Eco Swiss*, supra note 145; *Nordsee*, supra note 630.

or to interpret the law applicable, or in the course of a review of an arbitration award'.⁶³⁴ Likewise, it is the task of member state courts to 'ascertain whether it is necessary for them to make a reference' to the ECJ 'in order to obtain an interpretation or assessment of the validity of provisions of Community law which they may need to apply when reviewing an arbitration award'.⁶³⁵ In *Eco Swiss*, the Court also recognized that 'it is in the interest of efficient arbitration proceedings that review of arbitration awards should be limited in scope and that annulment of or refusal to recognise an award should be possible only in exceptional circumstances'.⁶³⁶ Arbitral tribunals have inferred that *Eco Swiss* and *Nordsee* indicate that since the ECJ has sanctioned commercial arbitration, the same principle should apply, by analogy, in respect of investment arbitration. The BGH also argued that the Court's reference in *Eco Swiss* to the 'interest of an efficient arbitration proceedings' applies equally to investment arbitration, with the consequence that national courts can review awards only in exceptional circumstances without this causing any autonomy concerns.⁶³⁷

These arguments refer to two scenarios. First, to the scenario where the ECJ becomes involved *during* the arbitral proceedings to clarify the meaning of specific EU law provisions, and, second, to the scenario where the losing party challenges the enforcement of an award before a member state court on the grounds provided in national rules of procedure. The grounds of challenge under national rules of procedure are purposely narrow and reflect the basic idea of arbitration, namely, that it provides a fast, final and binding settlement of the underlying disputes and is an alternative to national courts. To schematize matters, arbitral awards (and other decisions of tribunals) can only be challenged on similar grounds as domestic judgments which have obtained *res judicata* effect. Manifest violations of due process, lack of jurisdiction, and decisions breaching a state's public policy are typical examples of such grounds, which imply that the grounds rarely accommodate arguments based on a mistaken interpretation of the law, including EU law. The BGH argued that this does not mean that BIT arbitration clauses are incompatible with EU law, because the ECJ has expressly acknowledged that member state courts are to review commercial arbitration awards only to the extent that they can be certain that the award does not breach 'a fundamental provision [of EU law] which is

⁶³⁴ *Nordsee*, supra note 630, para. 14. See also *Eco Swiss*, supra note 145, para. 32.

⁶³⁵ *Eco Swiss*, supra note 145, para. 33. See also *Nordsee*, supra note 630, para. 15.

⁶³⁶ *Eco Swiss*, supra note 145, para. 35.

⁶³⁷ *Eureka* referral, supra note 150, paras. 62-63.

essential for the accomplishment of the tasks entrusted to the Community and, in particular, for the functioning of the internal market'.⁶³⁸ In other words, if arbitral tribunals have interpreted and applied 'ordinary' EU law provisions, there is no need to review those interpretations, because the 'efficiency' of arbitration proceedings requires this.

However, and clearly, the ECJ can provide an interpretation of such ordinary provisions during the arbitral proceedings if the national rules of procedure allow tribunals to ask national courts to send preliminary questions on their behalf. Equally clearly, however, if such requests are not possible or if the tribunal refuses to make such request, the tribunal's misinterpretation is final, because it does not constitute a ground of challenge of the final award. Only if the award's *enforcement* would breach a 'fundamental' EU law provision can the presiding court annul the award, and in *Eco Swiss* the Court held that the award breached such fundamental provision, namely Article 101 TFEU, and the Dutch Supreme Court then annulled the award on the ground that it was equivalent to a breach of Dutch public policy in the meaning of its national rules of procedure.⁶³⁹

Generally speaking, whether investment arbitration is akin to commercial arbitration is in the eye of the beholder.⁶⁴⁰ Government officials, politicians, NGOs, arbitrators and academic commentators take different approaches to investment arbitration because their interests and objectives as regards the investment treaty regime are different. As Roberts argues, different stakeholders employ different analogies between commercial and investment arbitration so as to compel other stakeholders to accept a particular interpretation of either a specific BIT provision or the investment treaty regime as a whole.⁶⁴¹ In our case, the purpose of the commercial arbitration analogy is to provide support to the argument that investment arbitration is equally compatible with EU law. The analogy strives to ensure that public law institutions keep a similarly polite distance to the work of investment and commercial arbitrators, and the idea is that the requirements of the autonomy doctrine should be loosened to a similar extent in relation to both. In the above

⁶³⁸ *Eco Swiss*, supra note 145, para. 36. See also *Eureko* referral, supra note 150, paras. 55-63.

⁶³⁹ *Ibid.*, para. 37.

⁶⁴⁰ For an insightful critique of the widely accepted argument that investor-state arbitration is 'public' and commercial arbitration 'private' in nature, see José E. Alvarez, 'Is Investor-State Arbitration 'Public'?', *Institute for International Law and Justice Working Paper* 2016/6 (Global Administrative Law Series).

⁶⁴¹ Anthea Roberts, 'Clash of Paradigms: Actors and Analogies Shaping the Investment Treaty System', 107 *American Journal of International Law* (2013), pp. 45-94.

cases, the tribunals simply assumed that the two types of arbitration are alike, without providing arguments that support its use.⁶⁴²

It is important to note that the underlying arbitrations in *Eco Swiss* and *Nordsee* did not involve member states. Both were contractual disputes between two private parties and in both cases the basic argument was that the relevant contracts breached EU law. In *Eco Swiss* the arbitral tribunal had ordered one of the companies to pay damages to the other party on the basis of a licensing agreement, which was automatically void under Article 101 TFEU, as it constituted a market sharing arrangement. In *Nordsee* the Commission had informed a group of shipping companies that a pooling agreement concerning the allocation of EU aid as between them breached the regulations under which the aid was granted and could not be enforced, but one of the shipping companies still sought compensation from another shipping company for breach of the agreement. In *Nordsee* the Court held that 'Community law must be observed in its entirety throughout the territory' of the member states, and the disputing parties in the arbitration were not 'free to create exceptions to it'.⁶⁴³ In *Eco Swiss* the tribunal's seat was in the Netherlands and in *Nordsee* in Germany, and the ECJ held, as noted, that when a tribunal or one of the parties resort to member state courts during or after the arbitral proceedings, it is the task of those courts to determine whether to submit preliminary questions to acquire 'the interpretation or assessment of the validity of provisions of Community law'.⁶⁴⁴ In *Eco Swiss* the losing party resorted to Dutch courts *after* the arbitral tribunal had rendered its final award, while in *Nordsee* the sole arbitrator submitted preliminary questions directly to the ECJ *during* the arbitral proceedings, with the Court finding that it had no jurisdiction to give a ruling on the ground that the arbitrator did not qualify as a court or tribunal of a member state under Article 267 TFEU. It is unknown how the arbitral process progressed from thereon and whether the sole arbitrator resorted to German courts.

This suggests two things. First, the ECJ acknowledged that once a tribunal has rendered the final award, member state courts have limited possibilities to annul them in light of EU law, but this was not a problem for the Court. On the other hand, in *Nordsee*, the ECJ held

⁶⁴² As Dworkin once put it, '...analogy without theory is blind. An analogy is a way of stating a conclusion, not a way of reaching one, and theory must do the real work.' See Ronald Dworkin, 'In Praise of Theory', 29 *Arizona State Law Journal* (1997), pp. 353-376, at 371.

⁶⁴³ *Nordsee*, supra note 630, para. 14.

⁶⁴⁴ *Ibid.*, para. 15.

that parties to an arbitration cannot contract out of the requirements of EU law, as 'Community law must be observed in its entirety' throughout the EU. Without taking a stand on the ability of the sole arbitrator to seize the ECJ through German courts, the Court then made a general reference to the cooperation of arbitral tribunals and member state courts. The Court's findings in *Eco Swiss* and *Nordsee* appear to be somewhat illogical in respect of each other, but there is no point in placing too much emphasis on this. In both cases, the Court was addressing preliminary questions submitted by member state courts, and none of those questions related to the general issue of compatibility of commercial arbitration with EU law or to the situation where a member state is a party to a commercial arbitration. Neither did the questions concern situations where arbitral tribunals have to address questions of EU law in ways that might breach the autonomy of the EU legal order under the Court's case law. As argued above, BIT arbitration clauses may lead, for example, to claims where the tribunal is required to assess the respective competences of the EU and its member states and to analyze the question of attribution in relation to a domestic measure which implements an EU act. Likewise, BIT arbitration clauses may lead to cases where a member state invokes various types of EU law instruments, which the tribunal has to interpret to understand what the instruments required from the member state, and this holds true both when EU law is considered a factual component in the tribunal's analysis and (in the odd case) where it is part of the applicable law.

The third scenario that fell outside the sweep of *Eco Swiss* and *Nordsee* is the one where the tribunal's seat is in a third state. In such cases, as noted, member state courts and the ECJ can only become involved if the winning party seeks the award's enforcement within the EU, but their involvement has its limits given the narrow grounds under which awards may be challenged. It is also noteworthy that ICISD arbitrations are governed solely by the ICSID convention and ICSID arbitration rules, which prevent tribunals and the parties to seize member state courts during the arbitral process. Likewise, once an ICSID tribunal has rendered its final award, the award can only be annulled by an ICSID annulment committee but not by national courts. If the annulment committee upholds the award, ICSID contracting states are obligated to 'recognize an award rendered pursuant to...[ICSID] Convention as binding and enforce the pecuniary obligations imposed by that award within its territories *as if it were a final judgment of a court in that State*'.⁶⁴⁵ This

⁶⁴⁵ See Article 54(1) ICSID Convention, *supra* note 8 (emphasis added).

implies that challenges to ICSID awards are possible on extraordinary grounds of appeal under which final judgments of domestic courts can be challenged. Whether such grounds accommodate a challenge based on a tribunal's misinterpretation of EU law is an open question, but it seems clear that the misinterpretation would at least have to concern a fundamental EU law provision.

The Court's statement, that it is in 'the interest of interest of efficient arbitration proceedings that review of arbitration awards should be limited in scope and that annulment of or refusal to recognise an award should be possible only in exceptional circumstances', should be seen in the light of its context. The *Eco Swiss* tribunal had rendered its final award and the Court was in a position to ensure that the Dutch *Hoge Raad* annuls the award on the ground that its enforcement would have amounted to enforcing a market sharing arrangement, which would have breached Article 101 TFEU. Moreover, the Court's statement is descriptive and not a categorical acceptance of the many implications that the 'efficiency' of arbitration proceedings may have on the uniform interpretation and full effect of EU law. In other words, 'efficiency' is clearly one of the reasons why the disputing parties choose arbitration over national courts, but this does not mean that the parties are 'free to create exceptions to' EU law, as the Court put it in *Nordsee*. Hence, again, it seems that the two cases provide no conclusive answer to the compatibility of BIT arbitration clauses with the autonomy of the EU legal order.

The analysis suggests that in many situations the EU law interpretations of arbitral tribunals are outside the reach of member state courts and the ECJ. If the above broad reading of the Court's case law is accepted, the implication is that BIT arbitration clauses pose a manifest risk to the autonomy of EU law, and the fact that the ECJ cannot control tribunals' EU law interpretations only strengthens the conclusion. On the other hand, if the second, more narrow reading is accepted, the question is in which situations do decisions of arbitral tribunals have binding effects within the EU legal order.⁶⁴⁶ The legal opinion of the European Parliament's Legal Service on the relationship of investment dispute settlement provisions in EU trade agreements and EU law contains an interesting analysis

⁶⁴⁶ The Electrabel tribunal's finding of attribution between the EU and its member states was 'binding' in the sense that it formed the basis for the rejection of the PPA termination claim. While the ECJ might have concurred with the tribunal on the issue of attribution, it could not review that finding because the proceedings were governed by the ICSID Convention under which awards can only be challenged before an ad hoc tribunal established in accordance with the Convention's provisions. No such challenge was made, so the member state courts or the ECJ did not become involved.

in this regard.⁶⁴⁷ The opinion discussed the topic through the proposed investment protection provisions of CETA. Article 8.31 CETA provides that tribunals shall not have jurisdiction to determine the legality of a [challenged] measure...under the domestic law of the disputing party', with the domestic law of the disputing party considered 'as a matter of fact'. Likewise, tribunals will 'follow the prevailing interpretation given to the domestic law by the courts or authorities' of the disputing party, and 'any meaning given to domestic law by the Tribunal shall not be binding upon the courts or the authorities of that Party'. These points led the Legal Service to conclude that when CETA tribunals 'make assessments of EU law' in their rulings, 'this would have no effect on the jurisdiction...[or] on the interpretive powers' of the ECJ, because CETA tribunals, and investment tribunals more generally, can only award damages to investors, and the disputes concern 'the interpretation and application of the CETA Investment Chapter' and not the interpretation and application of EU law.⁶⁴⁸ In other words, the challenged EU law instruments would remain in force and applicable, and the Court's exclusive jurisdiction would not be under threat, because CETA tribunals' EU law interpretations have no normative reverberations within the EU legal order.

By analogy, arbitral tribunals established under member state BITs only award damages, and the disputes concern the interpretation and application of the BIT rather than of EU law. Clearly, member state BITs leave the ECJ's exclusive jurisdiction over the 'definitive interpretation' of EU law intact. It is noteworthy that Article 8.21 CETA provides that when it is unclear whether the EU or its member state is the correct respondent in an investment dispute, the EU is competent to determine that question and that determination binds the tribunal. This provision was included so as to address the Court's concern in Opinions 1/91 and 2/13 that the EEA court and the EctHR would have addressed the division of competences between the EU and its member states in the context of attributing a measure between them. This would suggest that the Court's exclusive jurisdiction under Article 344 TFEU and the autonomy of EU law are breached when an arbitral tribunal established under a member state BIT has to address the question of competence. While

⁶⁴⁷ Legal Service of the European Parliament, *Legal Opinion: Compatibility with the Treaties of investment dispute settlement provisions in EU trade agreements*, 1 June 2016, SJ-0259/16 AAM/hwo D(2016)16759. It should be noted that the relationship of investment dispute settlement provisions in EU trade agreements and EU law is clearly different from the question of the compatibility of BIT arbitration clauses with EU law, given that the EU is party to such agreements.

⁶⁴⁸ *Ibid.*, paras. 51-52. Schill makes a similar argument, see Stephan W. Schill, 'Editorial: Opinion 2/13 - The End for Dispute Settlement in EU Trade and Investment Agreements?', 16 *Journal of World Investment & Trade* (2015), pp. 379-388, at 385.

the *Electrabel* arbitration appears to be the only case where this has happened thus far, similar cases may arise, and the above discussion suggested that tribunals may engage with EU law in a number of other ways as well. One of the arguments of tribunals was that the EU Commission can always start infringement proceedings against a member state that complies with an award that breaches EU law, therewith ensuring that EU law is ultimately complied with.⁶⁴⁹ Against this, Hindelang argues that BIT arbitration clauses create a situation of 'structural incompatibility'⁶⁵⁰ as they create a legal space outside the EU legal order where arbitral tribunals can engage with EU law in ways that undermine the ECJ's exclusive jurisdiction and the uniform interpretation of EU law. Be that as it may, what is clear is that infringement proceedings have no impact on the validity of arbitral awards or on the interpretations of EU law that tribunals have provided.

The relevant preliminary questions of the BGH focused on Articles 267 and 344 TFEU.⁶⁵¹ I have argued that BIT arbitration clauses could breach the autonomy of the EU legal order, and that this finding is not necessarily based on direct breaches of Articles 267 and 344 TFEU, as the Court's construction of the autonomy of the EU legal order is in part detached from specific primary law provisions. Yet the Commission's argument that Article 344 TFEU reflects 'a more general principle' under which member states are obligated not to create 'methods of settlement' for disputes involving questions of EU law, is plausible. That those disputes involve private parties in case of investment arbitration

⁶⁴⁹ See e.g. *EURAM* award, supra note 83, para. 264.

⁶⁵⁰ Hindelang, 'Circumventing Primacy of EU Law', supra note 26, p. 198. For a similar type of argument, see Teis Tonsgaard Andersen and Steffen Hindelang, 'The Day after: Alternatives to Intra-EU BITs', 17 *The Journal of World Investment & Trade* (2016), pp. 984-1014 (footnote 13). The *EURAM* tribunal also argued that since member state courts retain discretion as to whether to submit preliminary questions to the ECJ, there was 'no automatic or *ex officio* seizure of the ECJ as soon as EU law is at stake, which leaves open... the possibility of divergent interpretations of EU law'. *EURAM* award, supra note 83, para. 252. This argument is subject to the critique that, unlike arbitral tribunals, member state courts are obligated to interpret and apply EU law and to give priority to it over conflicting rules of national law. The latter are also obligated to submit preliminary questions on certain conditions, while arbitral tribunals have no possibility or obligation to submit preliminary questions.

⁶⁵¹ Hindelang argues that *intra-EU BITs* may also breach Article 259 TFEU which deals with disputes between member states concerning an alleged breach of EU law by one of them. The logic is that 'litigation between investor and host Member State can arguably be perceived as litigating a conflict over substantive rights contained in the BIT between the home state of the investor and the host state'. In this view, 'the material rights and obligations resulting from the BIT primarily concern only... [the two] Member States and procedural rights are granted to an investor in a BIT only in order to effectively enforce the substantive ones, the latter still belonging to the state parties to the treaty'. Hence, Hindelang concludes, 'what the individual investor fights out before the arbitral tribunal can ultimately still be considered as a dispute of his home Member State with the host Member State regarding the violation of material protection standards in the BIT'. In other words, when an intra-EU investment dispute involves questions of EU law, the 'initiation of arbitral proceedings would have to be considered as a violation of Article 259 TFEU'. See Hindelang, 'Circumventing Primacy of EU Law', supra note 26, pp. 199-200.

does not necessarily undermine the Commission's argument. First, Article 344 TFEU is located in Part Seven of the TFEU, which is titled 'General and Final Provisions', whereas provisions dealing with the jurisdiction and powers of the ECJ are located in Part Six (Chapter I, Section five), titled 'Institutional and Final Provisions'. This indicates that Article 344 TFEU has to be understood as reflecting a 'more general principle',⁶⁵² and not simply as relating to the provisions dealing with the ECJ. In other words, the BGH's argument that Article 344 TFEU has to be read in connection with Article 259 TFEU, which provides for a method of settlement for disputes between two member states, and that Article 344 TFEU therefore only covers disputes between two member states, is problematic given the more general nature of the latter. It is much more plausible to understand Article 344 TFEU as a general provision that safeguards the autonomy of the EU legal order and the Court's central position within it. As the mandate of the ECJ resembles the mandate of domestic courts of last instance, the member states cannot contract out of their obligation to bring disputes involving questions of EU law before EU courts, regardless of the identity of the other disputing party. However, as noted, it is not entirely clear where the outer boundaries of the autonomy doctrine lie, but it would seem that the possibility that tribunals rule on the twin-issue of competence and attribution constitutes a problem in light of the Court's case law (see following paragraph). This would also indicate that if BIT arbitration clauses breach the autonomy of the EU legal order, both intra- and extra-EU BITs are problematic. The autonomy of EU law can be exposed to a similar 'manifest risk' in disputes between a member state and a third state investor, because tribunals may have to assess similar EU law questions as in intra-EU disputes.

The BGH's finding that Article 267 TFEU was not breached in the circumstances of the *Eureko* arbitration stemmed in part from the fact that the *Eureko* tribunal had not ruled on any question of EU law in its final award.⁶⁵³ In other words, and more generally speaking, when an arbitration under a member state BIT has no connection to EU law, the preliminary ruling procedure is entirely irrelevant to the arbitration. But the same argument could be made in relation to Article 344 TFEU. If the parties raise no EU law arguments in the proceedings, then the dispute's settlement by an arbitral tribunal cannot breach Article

⁶⁵² EU Commission, *amicus curiae* brief in *US Steel*, supra note 124, para. 37. For a similar argument, see Hindelang, 'Circumventing Primacy of EU Law', supra note 26, at 199 (footnote 82).

⁶⁵³ *Eureko* referral, supra note 150, paras. 60-61.

344 TFEU. The point is, as noted above, that particular investment disputes may well be 'compatible' with EU law when they relate to purely national measures, but each arbitration clause has the potential of breaching the autonomy of the EU legal order given the broad range of circumstances from which investment disputes stem. A good analogy is found in the three extra-EU BIT cases.⁶⁵⁴ Those cases related to a *potential* conflict between the free transfer of payments provisions in the BITs and primary EU law provisions allowing the EU Council to restrict capital movements between member states and third states. The EU Council had not adopted any such restrictions vis-à-vis the third states with which Austria, Finland and Sweden had concluded the BITs, but the Court held that the BIT provisions were incompatible with the primary law provisions, and the respondent states had failed to fulfill their obligation to eliminate that conflict as required by Article 351(2) TFEU.⁶⁵⁵ By analogy, one could argue that each BIT arbitration clause may lead to disputes between investors and member states where a broad range of EU law questions are raised, indicating that the clauses have the potential of adversely affecting the autonomy of the EU legal order.

The EU is also party to the founding agreements of the World Trade Organization (WTO). In a number of judgments, the Dispute Settlement Body (DSB) has declared that specific EU law instruments breach one or more of the WTO agreements.⁶⁵⁶ Prima facie, this appears to pose a threat to the autonomy of the EU legal order, given that the ECJ has no powers to review DSB decisions that interpret EU measures, nor is there any formal institutional relationship between the WTO dispute settlement mechanism and the ECJ. Moreover, the decisions of the DSB are binding upon the disputing parties, including the EU. The ECJ has never addressed the question of the relationship of WTO dispute settlement and autonomy of EU law. The Court has issued a number of judgments in which it has 'accepted' that the DSB interprets EU law and also defined what consequences its decisions have as a matter of EU law. As many commentators have noted, the Court has thus far 'evaded the question of whether such [DSB] decisions have legal force within the

⁶⁵⁴ Case C-205/06, *Commission v Austria*, ECLI:EU:C:2009:118; Case C-249/06, *Commission v Sweden*, ECLI:EU:C:2009:119; Case C-118/07, *Commission v Finland*, ECLI:EU:C:2009:715.

⁶⁵⁵ *Ibid.*, para. 1 of the declarative parts of the three judgments.

⁶⁵⁶ See e.g. Appellate Body Report, *European Communities - Regime for the Importation, Sale and Distribution of Bananas*, WT/DS27/AB/R (9 September 1997); Appellate Body Report, *European Communities - Measures Concerning Meat and Meat Products (Hormones)*, WT/DS48/AB/R (16 January 1998).

EC legal order',⁶⁵⁷ but it has provided a clear set of principles on the effects that DSB decisions have as a matter of EU law. In a nutshell, the ECJ has held that the WTO is based on the 'principle of negotiations' between the contracting states, through which they strive to achieve 'reciprocal and mutually advantageous arrangements', and WTO law is characterized by 'the great flexibility of its provisions, in particular those conferring the possibility of derogation' from them.⁶⁵⁸ Similarly, WTO law and DSB decisions have no direct effect under EU law, that is to say, the GC and ECJ do not review the legality of EU acts in light of WTO law as this would deprive WTO members of the necessary 'flexibility and discretion in devising solutions' to DSB decisions which establish violations of WTO law.⁶⁵⁹ Generally speaking, these findings allow the EU institutions to interpret and apply EU law as before internally, despite the fact that this may breach a DSB ruling.

The ECJ's position pays respect to the political sensitivities inherent in trade disputes as well as to the fact that DSB rulings are not addressed to individuals but to the disputing parties of the WTO agreements. The Court does not want to tread on the toes of the Commission and the member states in the sense that it allows them to decide how to react to a DSB ruling, also because the other WTO parties give no direct effect to DSB rulings in their domestic legal orders either. This indicates that the EU's participation in WTO dispute settlement is not relevant, by analogy, in the member state BIT context. While the DSB interprets EU acts in light of the WTO agreements, the implications of those interpretations are a political matter to be decided by the relevant political organs.⁶⁶⁰ Again, given the broad range of EU law related questions that arbitral tribunals may have

⁶⁵⁷ Schmalenbach, 'Struggle for Exclusiveness', supra note 389, p. 1059.

⁶⁵⁸ Joined Cases C-21-24/72, *International Fruit Company*, ECLI:EU:C:1972:115, para. 21.

⁶⁵⁹ See John Errico, 'The WTO in the EU: Unwinding the Knot', 44 *Cornell International Law Journal* (2011), pp. 179-208, at 194. As the ECJ put it: 'To accept that the role of ensuring that Community law complies with those rules [i.e. WTO rules] devolves directly on the Community judicature would deprive the legislative or executive organs of the Community of the scope for manoeuvre enjoyed by their counterparts in the Community's trading partners'. See Case C-149/96, *Portuguese Republic v Council*, ECLI:EU:C:1999:574, paras. 40-47 (the quote is from para. 46). For a general analysis of this matter, see Hélène Ruiz Fabri, 'Is There a Case - Legally and Politically - for Direct Effect of WTO Obligations?', 25 *European Journal of International Law* (2014), pp. 151-173. However, the Court has shown some acceptance of WTO rulings. After the AB had ruled that the so called 'zeroing' method breached WTO law, the ECJ held that the method violated EU law as well, but the judgment made no references to the AB ruling, as the violation was based solely on a relevant EU regulation. See Case C-351/04, *Ikea Wholesale Ltd v Commissioners of Customs & Excise*, ECLI:EU:C:2007:547. Similarly, the ECJ has held that a DSB decision may in certain circumstances be used to interpret EU law. See Joined Cases C-319/10 and C-320/10, *X and Y & X BV*, ECLI:EU:C:2011:720.

⁶⁶⁰ Individual applicants can only ask the EU courts whether certain EU measures comply with WTO rules in light of a DSB ruling *after* the EU organs have implemented the obligations flowing from a DSB decision. See Case C-377/02, *Leon Van Parys*, Case C-377/02, ECLI:EU:C:2005:121, para. 40.

to address, the relationship of member state BITs and EU law should be decided on the basis of the implications that such 'addressing' may have within the EU legal order, rather than by relying on the peculiarities of the WTO system.

Finally, the EU member states are parties to the ECHR and the Strasbourg court has faced a number of applications that concern the domestic implementation of EU acts. In essence, in all scenarios the EctHR has attributed domestic implementing measures to the member states, but the way in which a measure's compatibility with the ECHR is assessed depends on the discretion that the EU act leaves to domestic institutions. For example, in *Bosphorus*, the EctHR held that a regulation left no discretion to Ireland as it 'was "generally applicable" and "binding in its entirety"...so that it applied to all member States, none of which could lawfully depart from any of its provisions', and it became part of Irish law 'when it was published in the Official Journal...without the need for implementing legislation'. Further, Irish authorities had no discretion over the aircraft's seizure and the measure 'amounted to compliance by the Irish State with its legal obligations' under Article 8 of the regulation.⁶⁶¹ When the EU act leaves no discretionary powers to the member states, there is a presumption that EU law provides equivalent protections to the applicant, but the ECtHR still examines whether the presumption holds water in an individual case.⁶⁶² On the other hand, if the EU act provides discretion over its implementation, the presumption of 'equivalent protection' does not apply, and the EctHR reviews the implementing measure in full to understand whether it complies with the ECHR.⁶⁶³ This means that not only does the ECtHR interpret EU law instruments on a

⁶⁶¹ Application no. 45036/98, *Bosphorus Hava Yollari Turizm ve Ticaret Anonim Şirketi v. Ireland*, Judgment of 30 June 2005 (hereinafter *Bosphorus* judgment), para. 145. In contrast, the underlying Security Council resolution, which was implemented within the EU via the regulation, was not part of Irish law and did not provide a 'legal basis for the impoundment of the aircraft.' The judgment had previously (at para. 83) recognized that regulations take effect in member state legal orders 'without the need for domestic implementation.'

⁶⁶² In *Bosphorus* the EctHR concluded that 'it cannot be said that the protection [under EU law] of the applicant company's Convention rights was manifestly deficient, with the consequence that the relevant presumption of Convention compliance by the respondent State has not been rebutted. Ibid., para. 166. The applicant had also challenged the regulation before the ECJ. Demonstrating that the wheels of justice may grind slowly, the ECJ had rendered its decision on the aircraft's seizure some nine years before the EctHR gave its judgment, with the ECJ finding that the seizure did not violate the applicant's fundamental rights and was an appropriate and proportionate measure given the importance of the undergirding aim of the regulation. See Case C-84/95, *Bosphorus*, ECLI:EU:C:1996:312, paras. 19-27.

⁶⁶³ See e.g. Application no. 17862/91, *Cantoni v. France*, Judgment of 11 November 1996. The French implementing legislation of a directive reproduced the directive's text almost literally and the applicant claimed that the legislation's wording 'lacked sufficient clarity and precision to satisfy the requirements of Article 7(1) of the Convention'. Rather than examining whether the implementing measure was attributable to France, the Court simply noted (at para. 30) that although the relevant article in the French public health

regular basis but also assesses the division of competences between the EU and its member states by attributing implementing measures to the latter. Clearly, in light of the above, this appears to be problematic from the perspective of the autonomy of EU law.

Given the knockout delivered in Opinion 2/13, it will take considerable time before EU acts can be directly challenged before the ECtHR. However, since all EU member states are parties to the Convention, its provisions have sneaked into the EU legal order through the backdoor. The Convention does not formally bind the EU, but Article 6(3) TEU provides that fundamental rights, as guaranteed by the Convention and 'as they result from the constitutional traditions common to the Member States, shall constitute general principles of the Union's law'. Accordingly, the ECJ has applied the Convention's provisions and the attendant case law 'indirectly' as part of those general principles.⁶⁶⁴ Likewise, Article 52(3) of the Fundamental Rights Charter provides that '[i]n so far as this Charter contains rights which correspond to rights guaranteed by the Convention for the Protection of Human Rights and Fundamental Freedoms, the meaning and scope of those rights shall be the same as those laid down by the said Convention'.⁶⁶⁵ As Advocate General Jacobs put it, 'for practical purposes the Convention can be regarded as part of Community law and can be invoked as such both in this Court and in national courts where Community law is in issue. That is so particularly where, as in this case, it is the implementation of Community law by Member States which is in issue. *Community law cannot release Member States from their obligations under the Convention*'.⁶⁶⁶ Similarly, in its submissions in *Bosphorus* before the ECtHR, the EU Commission endorsed the 'equivalent protection' doctrine and urged the ECtHR to apply it 'pending accession to the Convention by the European Union'.⁶⁶⁷

code was almost identical to the directive's text, this 'does not remove it from the ambit of Article 7 of the Convention', and no further relevant analysis followed.

⁶⁶⁴ The first case where the ECJ held that fundamental rights are part of the general principles of EU law was Case 29/69, *Erich Stauder v City of Ulm - Sozialamt*, ECLI:EU:C:1969:57, para. 7. For an example of the ECJ relying on the Convention's articles, see e.g. Case C-413/99, *Baumbast and R v Secretary of State for the Home Department*, ECLI:EU:C:2002:493, para. 72 ('Moreover, in accordance with the case-law of the Court, Regulation No 1612/68 must be interpreted in the light of the requirement of respect for family life laid down in Article 8 of the European Convention. That requirement is one of the fundamental rights which, according to settled case-law, are recognized by Community law.').

⁶⁶⁵ Fundamental Rights Charter, supra note 69. The ECJ has also showed willingness to change its case law in accordance with the case law of the ECtHR. See Case C-94/00, *Roquette Frères SA v Directeur général de la concurrence*, ECLI:EU:C:2002:603, para. 29.

⁶⁶⁶ See Case C-84/95, *Bosphorus*, Opinion of Advocate General Jacobs, ECLI:EU:C:1996:179, para. 53 (emphasis added).

⁶⁶⁷ See *Bosphorus* judgment, supra note 661, para. 122.

Clearly, the judgments of the ECtHR are not binding on the EU institutions, and one could also characterize the judgments as concerning not the question of competence but member states' compliance with the Convention provisions. It is also evident that the ECJ will not get a chance to address the question whether the ECtHR's findings are problematic from the perspective of autonomy, because the status quo appeases all concerned parties (witness the Commission's statement). Generally speaking, the equivalent protection doctrine protects the autonomy of EU law indirectly, and I am unaware as to the number of cases where the ECtHR might have found that a member state implementing measure breaches the Convention and what practical consequences such findings have had on the implementation of the underlying EU act. What is more, it appears that a typical ECtHR judgment makes a declaration of breach, rather than obligates the losing state to repeal or amend the challenged measure. This would suggest that the judgments have no binding effects within the EU legal order, even if the ECtHR were to find that an implementing measure breaches the Convention. In sum, it is difficult to make clear conclusions as to what implications the ECtHR's case law could have in the context of investment arbitration, because the EU institutions have accepted its authority to review domestic implementing measures.

As it appears to be somewhat uncertain whether arbitration clauses in member state BITs pose a threat to the autonomy of EU law, the question is which way should the scales tip? Here, arguably, the question of values and interests should play a central role. Many commentators have argued that the ECJ should focus on 'the facilitation of interaction with other international legal regimes [i.e. the investment treaty regime], rather than concentrating strictly on the delimitation of an autonomous EU legal order'.⁶⁶⁸ In this perception, investment arbitration serves an important purpose and the Court should facilitate its inclusion in EU investment agreements in one or another way. Similarly, the relationship of autonomy and arbitration under member state BITs should be resolved with reference to the fact that EU law is only an incidental visitor to arbitral proceedings and remains a mere (often insignificant) fact in most arbitrations, and only the *Electrabel* tribunal's finding on attribution looks problematic, although that finding was clearly in line with the division of competences between the Commission and the member states in the area of state aid. In this light, investment arbitration is not a *real* problem for the autonomy

⁶⁶⁸ Hannes Lenk, 'Investment Arbitration under EU Investment Agreements: Is There a Role for an Autonomous EU Legal Order?', 28 *European Business Law Review* (2017), pp. 135-162, at 162.

or uniform of interpretation of EU law, and the decisions of arbitral tribunals do not, in principle, have any binding effects within the EU legal order, apart from the extremely rare situation where the *enforcement* of an award breaches particular EU law rules, although in such situations the Commission could intervene and start infringement proceedings to ensure compliance.

Second, as commentators have noted, EU law does not provide equally broad and effective protection to investors, and many arbitrations concern situations where EU law either plays no role and where the remedies under EU law and national law are less generous, and where compensation is not forthcoming given the more stringent liability criteria that apply under EU law and national law. Generally speaking, Article 53 of the Fundamental Rights Charter could be invoked in this context. It provides that the Charter does not restrict or adversely affect 'human rights and fundamental freedoms as recognised, in their respective fields of application, by Union law and international law and by international agreements to which the Union, the Community or all the Member States are party, including the European Convention for the Protection of Human Rights and Fundamental Freedoms, and by the Member States' constitutions'. Read literally, investment treaties do not fall under any of the categories listed in Article 53, but if member states are allowed to provide better protection of human rights and fundamental freedoms under domestic constitutions when they implement EU law, clearly the same principle should apply in respect of bilateral treaties to which they are party and regardless of whether or not the treaty protections relate to the implementation of EU law. The *Melloni* case implies that when the EU has harmonized the protection of fundamental rights in a certain area, Article 53 does not apply (in such cases member states have to apply the EU standard),⁶⁶⁹ but the EU has not harmonized the area of investment protection which leaves the member states free to provide better protection in the form of BITs.⁶⁷⁰ This argument may seem a bit stretched, but the point is that the question of values and interests could play a role when the relationship of autonomy and investment arbitration is addressed, also because the Court's case law is less than clear on where the limits of the doctrine lie in respect of dispute settlement mechanisms established in treaties concluded by the member states.

⁶⁶⁹ Case C-399/11, *Melloni*, ECLI:EU:C:2013:107.

⁶⁷⁰ However, Chapter 4 argued that member state BITs violate the principle of non-discrimination, and the application of Article 53 cannot override the requirement of equal treatment, which suggests that all EU investors should be able to rely on BIT protections, but Chapter 4 also showed that this option is highly unlikely for a number of reasons.

The question of values and interests should also be taken account of *if* BIT arbitration clauses pose a threat to the autonomy of the EU legal order. Generally speaking, the proponents of investment treaties could argue that in relation to intra-EU BITs the member states have an obligation to ensure that investors cannot invoke the clauses in relation to disputes that lead tribunals to interpret and apply EU law in ways that breach the autonomy of EU law. For example, the member states could amend intra-EU BITs so as to ensure that disputes related to EU law no longer fall within the sweep of the arbitration clause, but the clauses could continue to apply in relation to disputes concerning purely domestic measures. This solution would respect the argument that investment treaties and arbitration protect the fundamental rights of investors as well as the fact that many investment disputes have no relation to EU law. In relation to extra-EU BITs, member states are under a general obligation to 'take the necessary measures to eliminate incompatibilities' from extra-EU BITs as a matter of EU law.⁶⁷¹ In principle, the contracting states could amend the treaties similarly to intra-EU BITs, but this is a purely hypothetical scenario to begin with, given the broader political context outlined above.

To return to intra-EU BITs, much will depend on the ECJ's findings in the pending *Achmea* case, although those findings are confined to that clause and have no direct relevance for other intra-EU BITs. The relevant part of that clause provides that the 'arbitration tribunal shall determine its own procedure applying the arbitration rules of the United Nations Commission for International Trade Law (UNCITRAL)',⁶⁷² and unlike many other clauses, it does not allow investors to choose between different arbitration venues and arbitration rules. This will prevent the ECJ from addressing, for example, specific questions that relate to arbitrations carried out under the ICSID Convention. It is also unclear to what extent the circumstances in the underlying *Eureko* arbitration will affect the Court's reasoning (for example the fact that the tribunal concluded that the dispute had no bearing on any question of EU law). Assuming that the Court makes a finding of incompatibility, those member states that oppose to the Commission's intra-EU BIT policy could argue that other intra-EU BITs remain valid and continue to apply as a

⁶⁷¹ The Grandfathering Regulation, *supra* note 58, recital, para. 11.

⁶⁷² See Article 8(5) of the Dutch-Slovak BIT, quoted in *Eureko* award, *supra* note 74, para. 11.

matter of international law,⁶⁷³ which would compel the Commission to continue the ongoing infringement proceedings.⁶⁷⁴

The final issue that needs to be addressed is the relationship between the Court's autonomy doctrine and the division of competences between the EU and its member states over matters regulated in BITs.⁶⁷⁵ The internal market is an area of shared competence, so the question could be raised as to whether this means that *intra-EU* BITs could somehow stay outside the reach of the autonomy doctrine. The question is premised on the assumption that the EU has not used its competence in matters governed by intra-EU BITs, which would mean that member states remain competent to act in areas covered by them. This approach misunderstands the relationship between autonomy and competence. As Cremona argues in another context, the issue is not to what extent the EU has exercised a shared competence in a given area but whether a dispute in relation to a non-EU agreement, to which one or more member states are parties, raises issues that come within the scope of EU law. If such disputes are submitted to a method of settlement other than those provided in the founding treaties, the autonomy of the EU legal order may be adversely affected in light of the Court's case law.⁶⁷⁶ As should be clear by now, disputes raised under member state BITs may raise issues that come within the scope of EU law,⁶⁷⁷ even if many BIT claims have no connection to EU law.

This discussion on the autonomy of the EU legal order has been long, relatively complex and technical, in part because the Court's case law is written in language that leaves many questions open. However, the analysis highlights that the ECJ has some latitude in deciding how to answer the BGH's preliminary questions, which suggests that its chosen

⁶⁷³ Given that all BIT arbitration clauses have the potential of leading to disputes where tribunals have to interpret and apply EU law in ways that threaten the autonomy of the EU legal order, it is not convincing to argue that an ECJ judgment declaring that a BIT arbitration clause is incompatible with EU law would not apply, by analogy, in respect of other arbitration clauses. According to Article 260(1) TFEU, member states are 'required to take the necessary measures to comply with the judgment of the Court', and non-compliance may lead to the imposition of a 'lump sum or penalty payment under Article 260(2) TFEU.

⁶⁷⁴ Yet, and this is not an entirely implausible scenario, a member state could refuse to comply with the ECJ's judgment, which could lead to the imposition of a lump sum fine and/or a penalty payment against the member state, but even in that case the relevant treaty would remain in force as a matter of international law.

⁶⁷⁵ Generally speaking, when the EU has competence over a given policy area, that competence includes dispute settlement related to that area.

⁶⁷⁶ Marise Cremona, 'Defending the Community interest: The Duties of Cooperation and Compliance', in Marise Cremona and Bruno De Witte (eds.), *EU Foreign Relations Law: Constitutional Fundamentals* (Hart Publishing, 2008), pp. 125-170, at 151.

⁶⁷⁷ Dimopoulos makes the same conclusion, but qualifies it in some respect. See his 'The Validity and Applicability of International Investment Agreements', *supra* note 26, pp. 86-90.

course of action should be based on a proper understanding of the broader implications of investment treaties and arbitration. Chapters 6 and 7 strive to establish such understanding as the discussion centers on the alleged pros and cons of the investment treaty regime.

6. Arguments for Investment Treaties and Arbitration

6.1. Introduction

Chapter 3 showed how arbitral tribunals have rejected the conflict arguments of the Commission and a number of member states. For the tribunals, the ability of investors to bring claims against the host state without exhausting local remedies distinguished the subject-matter of BITs from that of EU law. Investment arbitration was described as a guarantee against undue interferences by the host state, with the tribunals emphasizing en masse that neither EU law or domestic laws of the member states provide an equally effective remedy. As two commentators put it, the clauses transform BITs from 'mere political declarations' to an effective 'set of rules enforceable against states'.⁶⁷⁸ Chapter 3 also noted that the argumentation of the tribunals carried ethical connotations in the sense that investment treaties were perceived as providing a necessary check on the opportunistic behavior of the host state as they provide access to a neutral and depoliticized venue for the settlement of investment disputes.⁶⁷⁹ In this vein, Brower and Blanchard argue that arbitral tribunals 'contribute to international and domestic *rule of law* by relying on and developing human rights jurisprudence when interpreting treaties', with BIT rights overlapping 'substantially with the rights protected in human rights treaties'.⁶⁸⁰

As noted in the introduction, it is important to go to the roots of the critique of investment arbitration as well as of the arguments with which the regime is defended. The

⁶⁷⁸ Brower and Schill, 'The Legitimacy of International Investment Law?', supra note 18, at 477.

⁶⁷⁹ 'Neutral' and 'depoliticized' are value-laden terms, but as has been noted investment arbitration is neutral at least in the sense that it proceeds 'outside the *direct* control of both host states and foreign investors'. See Jonathan Bonnitcha, Lauge N. Skovgaard Poulsen and Michael Waibel, *The Political Economy of the Investment Treaty Regime* (Oxford University Press, 2017), p. 87.

⁶⁸⁰ Brower and Blanchard, 'The Truth about Investor-State Arbitration', supra note 19, at 757-758 (emphasis added). See also Christoph Schreuer and Ursula Kriebaum, 'From Individual to Community Interest in International Investment Law', in Ulrich Fastenrath et al. (eds.), *From Bilateralism to Community Interest. Essays in Honour of Judge Bruno Simma* (Oxford University Press, 2011), pp. 1079-1096, at 1088 (arguing more cautiously that 'investment law has certain similarities with human rights law in that it protects an individual or corporate investor against infringements' by the host state.). Typically, the relationship of investment protection and human rights is approached from a perspective where the central question is whether arbitral tribunals accommodate human rights in their analysis, which, of course, is entirely different from the approach where investors are understood as the bearers of human rights. For two contributions adopting the former approach, see Pierre-Marie Dupuy et al. (eds.), *Human Rights in International Investment Law and Arbitration* (Oxford University Press, 2009), Lone Wandahl Mouyal, *International Investment Law and the Right to Regulate: a Human Rights Perspective* (Routledge, 2016).

understanding that investment treaties serve an ethical purpose is one such argument and without an appreciation of this and other relevant arguments it is difficult to take sides in the debate on how the relationship of EU law and investment treaties should be resolved.

The investment treaty regime is a moving target. New developments emerge on a weekly basis, with each new award potentially supporting or undermining the critique or fading quickly out depending on the outcome and the identity of the disputing parties. Scholarship is burgeoning and it is becoming increasingly difficult to keep track of the results and conclusions it brings. Similarly, a high number of states continue to conclude new investment treaties, whereas others are terminating or amending their existing treaties as a reaction to their hitherto experiences.⁶⁸¹ That it is impossible to keep track of all these changes and developments is not necessarily a problem. Whether the Commission's proposal for an investment court system will gain traction in the years to come is uncertain, but what is certain is that an overwhelming majority of member state BITs will remain in force for the foreseeable future, with investors continuing to bring new claims under them. As this thesis is going to press, for example, ICSID alone has registered 38 new claims during 2017, many of which were raised under BITs concluded in the 1990s, including member state BITs.⁶⁸² Most of these treaties contain vaguely formulated protection standards, with no reference made, for example, to the host state's right to regulate. Hence, although the policy and academic debate is focusing more and more on how to reform the 'old system', the old system is very much in place and provides an additional motive for the following discussion.

In the introduction, I also noted that the critics and proponents employ economic arguments to support their respective cases. These arguments are highly general and relate either to the economic benefits that investment treaties are understood to bring about, or to the ways in which they reinforce the position and interests of the most dominant players in the global economy at the expense of other stakeholders and interest groups. But the economics of foreign investment and investment treaties is a complex and multi-dimensional topic and one that requires expertise in (or at least familiarity with) the attendant theoretical frameworks and models. One could look at the dynamics of foreign

⁶⁸¹ At the time of writing, around 2700 investment treaties are in force and investors have initiated over 800 known arbitrations. The most up-to-date statistics are available at <http://investmentpolicyhub.unctad.org> (accessed 28 August 2017).

⁶⁸² See at <https://icsid.worldbank.org/en/Pages/cases/AdvancedSearch.aspx> (accessed 19 September 2017).

investment (whether direct or portfolio) from the perspective of investors or home and host states, and then choose between a microeconomic and a macroeconomic perspective. The microeconomics of investment treaties refers to their effects on the decision-making of individual firms and governments, whereas the macroeconomic perspective looks at the 'aggregate economic effects of investment treaties, which depend on the cumulative impact of decisions of individual firms and states'.⁶⁸³ In the following, I will focus on two intertwined macroeconomic arguments: that investment treaties increase investment flows, and that an increase in investment flows contributes to economic growth and development. The point of the discussion is to understand whether or not (or to what extent) the arguments are plausible. This chapter proceeds as follows. The following sections look at the building blocks of the case for investment treaties and arbitration. At first I look more closely at the human rights analogy to which I referred in Chapter 3, and then focus on the argument that investment treaties promote the rule of law domestically and internationally. After this, I address the two economic arguments that enjoy considerable vogue in political rhetoric. I will provide a critical analysis of each argument to pave the way for the discussion on the critique of investment arbitration, which is addressed in Chapter 7.

6.2. The Human Rights Analogy

Chapter 3 provided some remarks on the broad idea that investment treaties bear similarities to human rights treaties. This idea was based on a number of features of investment treaties and arbitration,⁶⁸⁴ as well as on cases where the factual record supported the argument that the host state's treatment violated an investor's core human right, such as the right to a fair trial.⁶⁸⁵ The underlying contention was that investors are more or less at the mercy of host states, with investment arbitration providing an important counterbalance against arbitrary exercises of public power. In this regard, one argument was that small- and medium-sized investors 'make up a large part of the claimants in contemporary investment-treaty arbitration'.⁶⁸⁶ Arguably, this was meant to provide emotive support to the human rights analogy as it draws a parallel between persecuted

⁶⁸³ The quote is from Bonnitza, Poulsen and Waibel, *The Political Economy*, supra note 679, p. 127.

⁶⁸⁴ E.g. in addition to BITs, property rights are protected under a number of human rights conventions such as the ECHR and the Fundamental Rights Charter, and similarly to human rights courts, the state is always the respondent (and never the claimant) in investment arbitration, and state behavior is assessed only in light of international standards.

⁶⁸⁵ See e.g. *Hesham v. Indonesia*, supra note 192.

⁶⁸⁶ Brower and Schill, 'The Legitimacy of International Investment Law?', supra note 18, p. 481.

minorities and foreign investors whose negotiating position vis-à-vis host states is much weaker than that of large multinationals. More generally, some proponents associate the rise of the investment treaty regime with the rise of international human rights. As Judge Schwebel put it,

'entitlement to international arbitration is one of the most progressive developments in the procedure of international law of the last fifty years, indeed in the whole history of international law. It is consistent with the development of international human rights, including the right to own property, and with the dethroning of the State from its status as the sole subject of international law.'⁶⁸⁷

Similarly, Robers refers to commentators who argue that similarly to human rights law, 'investment treaties...regulate a state's treatment of nonstate actors within its territory and permit those actors to challenge governmental conduct before an international body'.⁶⁸⁸ Some arbitral awards have also used the analogy. In *Tecmed*, for example, the tribunal referred to an EctHR judgment to give weight to the argument that since the claimant company had no political rights in the host state, it was in a more vulnerable position vis-à-vis domestic policy-making than domestic investors,⁶⁸⁹ whereas in *Thunderbird* one arbitrator held that the 'judicial practice most comparable to treaty-based investor-state arbitration is the judicial recourse available to individuals against states under the European Convention on Human Rights' under which 'states have to defray their own legal representation expenditures, even if they prevail'.⁶⁹⁰ This meant that the same principle should apply in the investment arbitration context as well. Generally speaking, the *formal*

⁶⁸⁷ Stephen M. Schwebel, 'Keynote Address: In Defence of Bilateral Investment Treaties', in Jan van den Berg (ed.), *Legitimacy: Myths, Realities, Challenges*, ICCA Congress Series, Vol. 18 (Kluwer, 2015), pp. 1-11, at 4.

⁶⁸⁸ Roberts, 'Clash of Paradigms', supra note 641, p. 46. See also Zachary Douglas, 'The Hybrid Foundations of Investment Treaty Arbitration', 74 *British Yearbook of International Law* (2004), pp. 151-289, at 153-154 (arguing that in 'the sphere of legal relationships between private entities and sovereign states, there are many parallels between the legal regime created by investment treaties on the one hand and those regimes established by the European Convention of Human Rights and the Algiers Accords (creating the Iran/US Claims Tribunal) on the other', footnotes omitted); Karl-Heinz Böckstiegel, 'Enterprise v. State: the New David and Goliath?', 23 *Arbitration International* (2007), pp. 93-104, at 93 (arguing that similarly 'to the situation of private persons claiming international protection of human rights such as the European Convention on Human Rights, private enterprises are today accepted as subjects and holders individual procedural and substantive rights in international law').

⁶⁸⁹ *Tecmed v. Mexico*, ICSID Case No. ARB(AF)/00/2, Award (hereinafter *Tecmed* award), 29 May 2003, para. 122 (with reference to Application no. 8793/79, *James and Others*, Judgment of 21 February 1986).

⁶⁹⁰ *Thunderbird v. Mexico*, UNCITRAL, Separate Opinion of Thomas Wälde, 1 December 2005, para. 141. See also *Mondev Int'l Ltd. v. United States*, ICSID Case No. ARB(AF)/99/2, Award, 11 October 2002, para. 144.

plausibility of the analogy depends on how we define human rights, and it seems unnecessary to engage in such pedantry, but there are a number of general factors that undermine the credibility of the analogy. Firstly, the critics could point out that it is implausible to draw a parallel between foreign investors and ethnic groups facing violent persecution from their governments, because there is no conclusive evidence that foreign investors are the target of systematic abuse anywhere in the world. On the contrary, one recent empirical study concluded that foreign investors 'often tend to be treated the same, or better, than domestic firms, even after robustly controlling for size, sector, and other relevant factors that may distinguish foreign firms'.⁶⁹¹ Another empirical study found that foreign investors often 'derive substantial fiscal and regulatory advantages from their political influence and from their ability to negotiate superior entry conditions' in developing countries in particular.⁶⁹²

These findings, of course, do not mean that foreign investors always receive better treatment than domestic investors or that foreign investors are never mistreated or oppressed. There will always be cases where a host state behaves arbitrarily, and if such cases are used as the (only) reference point for the analogy, its refutation will be a difficult task. But the existing evidence does undermine rather than supports the argument that foreign investors are subject to systematic mistreatment, although the empirical literature is still 'in its infancy'.⁶⁹³ Second, the critics could also point out that 'small- and medium-sized' investors are de facto either extremely wealthy individuals or corporations running multi-million businesses in a foreign country, and they usually have the wherewithal to defend themselves against government excess and are never in as vulnerable a position as private individuals. This suggests that violations of human rights 'proper' and violations of investor rights are not in the same ballpark as the relative position of foreign investors and oppressed individuals and groups is fundamentally different.⁶⁹⁴

However, these general remarks do not refute the human rights analogy, as they focus on the extent to which foreign investors are (or are not) mistreated and on their relatively privileged position. Arguably, the persuasive force of the analogy will depend on the

⁶⁹¹ Bonnitcha, Poulsen and Waibel, *The Political Economy*, supra note 679, p. 150 (referring to an unpublished manuscript 'Are Aliens Mistreated' by Emma Aisbet and Lauge Poulsen).

⁶⁹² The quote is from Rodolphe Desbordes and Julien Vauday, 'The Political Influence of Foreign Firms in Developing Countries', 19 *Economics & Politics* (2007), pp. 421-451, at 421.

⁶⁹³ Bonnitcha, Poulsen and Waibel, *The Political Economy*, supra note 679, p. 150.

⁶⁹⁴ For a critical discussion of the analogy, see Roberts, 'Clash of Paradigms', supra note 641, esp. at 69-74.

general perception one has of the purposes and implications of investment treaties and arbitration. If the investment treaty regime is understood to provide valuable protection to foreign investors, and to contribute to economic growth and development, the analogy will seem plausible regardless of the 'size' of and influence that foreign investors may have in host states, as the purpose of the regime is to ensure that host states refrain from arbitrary treatment in *all* circumstances. Arguably, this basic perception also dictates the way in which the proponents approach the relationship of investment arbitration and domestic policy-making. Gus van Harten has argued that, in comparison to domestic courts, arbitral tribunals exercise much less 'judicial restraint' in respect of host states' legislative and executive acts as well as in relation to parallel litigation before other adjudicative bodies.⁶⁹⁵ For example, domestic courts often defer to legislative and executive acts on democratic grounds, which includes situations where an elected body makes policy 'in areas of decision-making that are considered sensitive or complex, such as social and economic policy, national security, or public health'.⁶⁹⁶ Van Harten's analysis covers more than two hundred awards and he notes that the 'pervasive lack of evidence of [judicial] restraint highlights that arbitrators are, to a significant extent, agents of their own role'.⁶⁹⁷

Arguably, this 'role' is another word for the perception that the proponents have about the purposes of investment treaties and arbitration, which also explains the reluctance of arbitral tribunals to defer to domestic policy-making. Brower and Schill provide a useful description of this basic perception. They argue that BITs 'prevent governments from sacrificing foreign investors for the public good by protecting them against expropriations without compensation and [against] *measures that exceed what is reasonably acceptable in a market economy*'.⁶⁹⁸ The perceived proclivity of state authorities to make policy on grounds that go beyond what is 'reasonably acceptable' in a market economy necessitates an impartial and independent dispute-settlement mechanism which elevates the dispute to the (depoliticized) international level and away from the 'shop floor' of domestic institutions where parochial priorities and concerns are likely to intervene in the enactment of policy. If human rights activists and lawyers claim to represent the 'global standard' and speak in the name of the international community, the proponents of investment arbitration

⁶⁹⁵ This is one of the central arguments in Gus Van Harten, *Sovereign Choices and Sovereign Constraints: Judicial Restraint in Investment Treaty Arbitration* (Oxford University Press, 2013).

⁶⁹⁶ *Ibid.*, p. 4.

⁶⁹⁷ *Ibid.*, p. 17.

⁶⁹⁸ Brower and Schill, 'The Legitimacy of International Investment Law', *supra* note 18, at 489 (emphasis added).

assume that investment treaties and arbitration represent the 'global standard' in a globalized economy. As Wälde once noted, the conclusion of BITs 'expresses a formal decision to accept a rules and value system characteristic of developed market economies. The host state signals to investors - and to the global markets - that its intention is to behave as developed market economies do or are expected to do'.⁶⁹⁹ This mentality is also reflected in how Wälde characterizes BITs as setting a 'benchmark against which national legislative action is measured and by which it is inspired'. For him, legislative acts which fail to meet the benchmark are 'deviations' stemming from 'nationalist, socialist or protectionist tendencies'.⁷⁰⁰ The tone of these remarks is very similar to that of human rights organizations which name and shame governments that 'deviate' from international human rights standards.

If this is the understanding that the proponents (and arbitrators) have of investment treaties and arbitration, its natural corollary is the lack of restraint that Van Harten identifies. In such view, the critique that arbitral tribunals fail to defer to measures adopted in sensitive policy areas misunderstands the basic idea of investment arbitration, which is to provide an assessment of all domestic policy in light of international protection standards.⁷⁰¹ Another way to understand the role of arbitrators stems from research that analyzes 'interpretive' or 'epistemic' communities. The latter concept refers to a 'network of professionals with recognized expertise and competence in a particular domain and an authoritative claim to policy-relevant knowledge within that domain or issue-area'.⁷⁰² The expertise and knowledge of an epistemic community is unified in the sense that its members share a particular way of looking at social reality, which is based on 'a set of shared symbols and references, mutual expectations and a mutual predictability of intention'.⁷⁰³ In other words, epistemic communities 'delimit, for their members, *the* proper construction of social reality'.⁷⁰⁴ Stanley Fish invented the concept of 'interpretive community',⁷⁰⁵ and the term is

⁶⁹⁹ Thomas Wälde, 'Law, Contract and Reputation in International Business: What Works?', 2 *Business Law International* (2002), pp. 190-210, at 196.

⁷⁰⁰ *Ibid.*, p. 197.

⁷⁰¹ This is of course in line with the maxim (found in Article 27 VCLT) that a state 'may not invoke the provisions of its internal law as justification for its failure to perform a treaty'.

⁷⁰² Peter Haas, 'Introduction: Epistemic Communities and International Policy Coordination', 46 *International Organization* (1992), pp. 1-35, at 3.

⁷⁰³ John Ruggie, 'International Responses to Technology', 29 *International Organization* (1975), pp. 557-583, at 569-570.

⁷⁰⁴ *Ibid.*, p. 570.

⁷⁰⁵ See Stanley Fish, *Is There a Text in this Class? The Authority of Interpretive Communities* (Harvard University Press, 1980).

relatively vague, but in the present context it simply refers to a 'social group whose shared comprehension of a context makes possible the common interpretation of socially relevant texts'.⁷⁰⁶ Schematically speaking, the proponents of the investment treaty regime form an epistemic and interpretive community which shares a set of beliefs about the purpose of the regime as well as about what should be the *starting-point* of investment treaty interpretation, namely, that investment treaties provide a benchmark for what is reasonably acceptable government conduct in a market economy.

This understanding ties in with the perception that the proponents have on the role of arbitrators in deciding individual investment disputes. Some argue that 'an arbitrator is not the guardian of public policy, that his duties are towards the parties only, and that he must confine himself to the determination of disputes involving private interests'.⁷⁰⁷ Such view implies that arbitral tribunals should refrain from considering the 'governance implications of their decisions (including the interests of third parties) because the outcome of the dispute is only relevant to the disputing parties themselves'.⁷⁰⁸ What supports this view indirectly is that most BITs (including member state BITs) contain no references to host states' right to regulate but solely emphasize the investment protection function. Finland's BIT stock provides a good example of this. Out of the around 70 BITs, a lion's share was concluded before 2005 and the treaties follow by and large the European template as they focus on post-establishment treatment (and not on liberalization) with the protection standards being highly general in content. In the preamble of the Finland-Dominican Republic BIT, for example, the contracting states recognize the need to protect investments and to promote greater economic co-operation, as well as agree that 'a stable framework for investment will contribute to maximising the effective utilisation of economic resources'. The public interest receives no mention in the preamble and Article 2(2) provides that each contracting state 'shall... accord to investments... fair and equitable treatment and full and constant protection and security', with no further description given as to the standards' contents.⁷⁰⁹ Since the provisions of the relevant BIT constitute the applicable law in most arbitrations, it is not surprising that the investment protection function usurps other

⁷⁰⁶ Eben Moglen and Richard J. Jr. Pierce, 'Sunstein's New Canons: Choosing the Fictions of Statutory Interpretation', 57 *University of Chicago Law Review* (1990), pp. 1203-1245, at 1207.

⁷⁰⁷ Pierre Mayer, 'Reflections on the International Arbitrator's Duty to Apply the Law', 17 *Arbitration International* (2001), pp. 235-248, at 246-247.

⁷⁰⁸ Bonnitcha, Poulsen and Waibel, *The Political Economy*, supra note 679, p. 246.

⁷⁰⁹ Agreement between the Government of the Republic of Finland and the Government of the Dominican Republic on the Promotion and Protection of Investments (SopS 36/2007).

functions in practice, even if the countervailing public interests are recognized in one or another way in the tribunals' reasoning.

Admittedly, the investment arbitration community does not constitute a homogenous epistemic or interpretive community. Its membership holds different views about the past, present and future of the investment treaty regime, which reflect its members' work affiliations as well as the institutional and political leanings of the academic traditions in which they were fostered into professional maturity. For example, in contrast to the narrow function just described, many argue that arbitral tribunals exercise law-making and governance functions and 'therefore require democratic legitimacy'.⁷¹⁰ These arguments recognize that investment disputes may necessitate a review of host state legislative and other acts related to sensitive areas of public policy, which should place requirements both on the applicable law and the rules that govern the arbitral process (e.g. on rules related to transparency and third party intervention). Similarly, any sample of arbitral awards will contain references to the host state's right to regulate in one or another way: for example, the *S.D. Myers* tribunal held that determining whether an investor's treatment is unjust or arbitrary 'must be made in light of the high measure of deference that international law generally extends to the right of domestic authorities to regulate matters within their own borders',⁷¹¹ whereas the *Unglaube* tribunal noted that when state action relates to its 'responsibility to protect public health, safety, morals or welfare, ... such measures are accorded a considerable measure of deference in recognition of' the state's right to regulate such matters inside its borders.⁷¹² This is not to say that such deference is invariably the starting-point of interpretation, but that in most cases arbitral tribunals take account of the public interest that motivated the challenged measure, although they may 'adopt different interpretive paradigms depending on who the arbitrators are'.⁷¹³

The purpose of these remarks is two-fold. First, they attempt to show that the view one has of the purpose of investment treaties and arbitration will influence the view one has of the

⁷¹⁰ See Ingo Venzke, 'Investor-State Dispute Settlement in TTIP from the Perspective of a Public Law Theory of International Adjudication', 17 *Journal of World Investment & Trade* (2015), pp. 374-400, at 374. See also José E. Alvarez, 'What are International Judges for? The Main Functions of International Adjudication', in Cesare P.R. Romano et al. (eds.), *The Oxford Handbook of International Adjudication* (Oxford University Press, 2014), pp. 158-178.

⁷¹¹ *S.D. Myers, Inc. v. Government of Canada*, UNCITRAL, Partial Award, 13 November 2000, para. 263.

⁷¹² *Marion Unglaube v. Republic of Costa Rica*, ICSID Case No. ARB/08/1, Award, 16 May 2012, para. 246.

⁷¹³ Michael Waibel, 'Interpretive Communities in International Law', in Andrea Bianchi et al., *Interpretation in International Law* (Oxford University Press, 2015), pp. 147-165, at 159.

authority of arbitral tribunals to review domestic policy. If the purpose of investment treaties and arbitration is to set and enforce international protection standards, then any and all public measures adopted by the three branches of government are subject to review by arbitral tribunals. In one way, the human rights analogy is a useful sidekick to the paternalistic assertion that arbitral tribunals discipline states for making policy that exceeds what is reasonably acceptable in a market economy, as the analogy and the examples used divert attention away from who is doing the disciplining; not the tribunals, but host states which engage in opportunistic and arbitrary behavior toward 'small- and medium-sized' investors. The second purpose was to undermine the perception that arbitral tribunals show no deference to domestic policy-making and are only concerned with promoting narrow investor interests. Clearly, the investment arbitration community is diverse and holds different views about the extent to which arbitral tribunals should take account of the public interest in individual cases, as well as about the role that arbitral tribunals should have in respect of broader governance questions. But regardless of the position one holds in respect of these questions, the critique that investment treaties and arbitration undermine the right to regulate will seem more or less misplaced, because this is what states consented to when ratifying investment treaties.⁷¹⁴

The above discussion has said nothing about the reasons that drove states to conclude investment treaties or about the implications that investment treaties and arbitration have had for domestic policy-making. Both issues are complex, and while the reasons that compelled states to sign investment treaties may be more generic, there still is variation in this regard as well. The next section looks at one general argument that relates to the alleged implications of investment treaties and arbitration, namely, that they promote the rule of law.

6.3. The Rule of Law Argument

BITs emerged as a solution to the anxiety of developed states over the investment climate of developing and newly decolonized states, although similar type of treaties were

⁷¹⁴ See e.g. Brower and Schill, 'The Legitimacy of International Investment Law, supra note 18, p. 477 (arguing that 'the investor's right to initiate arbitration enables the host state to make credible the commitments it made under its investment treaties').

concluded already much earlier.⁷¹⁵ A central object and purpose of early BITs was to ensure that western investors receive compensation for large-scale nationalizations, particularly in the extractive industries sector. However, this original assumption - that protecting western investments was not a priority for developing states in the absence of BITs - has transformed into a much broader and largely untested assumption about the necessity of investment treaties and arbitration in promoting economic globalization. The previous section already touched on two aspects of this assumption, namely, on the twin-argument that investment treaties resemble human rights treaties and set international standards for what is acceptable government conduct in a globalized economy. The third aspect of the assumption relates to the idea that the enforcement of those standards through investment arbitration promotes the rule of law. The descriptive part of the argument is premised on the view that 'in many developing and transitioning countries' there are no 'independent courts' that would resolve cases 'in accordance with pre-established rules of law in a timely fashion'.⁷¹⁶ As arbitral tribunals have interpreted the fair and equitable treatment standard to entail basic due process requirements,⁷¹⁷ the assumption is that host states are bound to 'improve the rule of law and governance generally in order to avoid liability' under investment treaties,⁷¹⁸ or, as another commentator put it, investment treaty obligations create a spillover effect 'that benefits national citizens and residents as the host country gradually develops better administrative practices to comply with international investment best practices'.⁷¹⁹ In other words, investment treaties, through the medium of

⁷¹⁵ For a history of BITs that is situated in a more general economic and political context, see Chapter 2 of Kenneth J. Vandeveld, *Bilateral Investment Treaties: History, Policy, and Interpretation* (Oxford University Press, 2010). See also Chapter 1 of Andrew Newcombe and Lluís Paradel, *Law and Practice of Investment Treaties. Standards of Treatment* (Kluwer Law International, 2009).

⁷¹⁶ Brower and Schill, 'The Legitimacy of International Investment Law, supra note 18, p. 479. For a similar argument, see Christoph Scheuer, 'Do We Need Investment Arbitration?', in Jean E. Kalicki and Anna Joubin-Bred (eds.), *Reshaping the Investor-State Dispute Settlement System* (Brill, 2015), pp. 879-890, at 883.

⁷¹⁷ See e.g. *The Loewen Group, Inc. and Raymond L. Loewen v. United States of America*, ICSID Case No. ARB(AF)/98/3, Award, 26 June 2003, para. 137 (the tribunal noted that the trial in a Mississippi court and the 'resultant verdict were clearly improper and discreditable and cannot be squared with minimum standards of international law and fair and equitable treatment'); *Azinian et al. V. Mexico*, ICSID Case No. ARB(AF)/97/2, Award, 1 November 1999, para. 102 (noting that a 'denial of justice could be pleaded if the relevant courts refuse to entertain a suit, if they subject it to undue delay, or if they administer justice in a seriously inadequate way'). More generally, tribunals have also emphasized that the rule of law requires that host states have legislation to recognize and enforce property and contractual rights, the quality of which 'meets minimum international standards'. The quote is from *AMTO v. Ukraine*, SCC Case No. 080/2005, Final Award, 26 March 2008, para. 87.

⁷¹⁸ Robert Howse, 'International Investment Law and Arbitration', *IILJ Working Paper 2017/1* (MegaReg Series), p. 34.

⁷¹⁹ See Roberto Echandi, 'What Do Developing Countries Expect from the International Investment Regime?', in Jose E. Alvarez and Karl P. Sauvant, *The Evolving International Investment Regime. Expectations, Realities, Options* (Oxford University Press, 2011), pp. 3-21, at 13-14. See also UNCTAD, *Investor-State*

arbitral tribunals, may slowly transform domestic governance structures as host states realize the high cost of not complying with basic principles of procedural fairness and access to justice.

Generally speaking, the rule of law concept suffers from overuse and is for many a 'self-congratulatory rhetorical device',⁷²⁰ which means little more than 'Hooray for our side!'⁷²¹

Rule of law projects and indicators abound, with a standard definition being that it is

'a principle of governance in which all persons, institutions and entities, public and private, including the State itself, are accountable to laws that are publicly promulgated, equally enforced and independently adjudicated, and which are consistent with international human rights norms and standards. It requires, as well, measures to ensure adherence to the principles of supremacy of law, equality before the law, accountability to the law, fairness in the application of the law, separation of powers, participation in decision-making, legal certainty, avoidance of arbitrariness and procedural and legal transparency.'⁷²²

It seems commonsensical that institutional reform toward the rule of law is both time-consuming and difficult and requires a multitude of human and financial resources. The following discussion will only point to the general problems that relate to the proponents' rule of law arguments as well as provides an overview of empirical studies dealing with the relationship of investment treaties and the rule of law.

In their lengthy defense of investment arbitration, Brower and Blanchard demonstrate how vaguely the concept is often used to make a general argument for the investment treaty regime. They argue that 'investment treaties and arbitration are in fact powerful tools for

Dispute Settlement and Impact on Investment Rulemaking (United Nations, 2007), at ix (noting that 'the increased number of [investment] arbitrations may...motivate developing host countries to improve domestic administrative practices and laws in order to avoid future disputes'). Similarly, Vandevelde concludes that 'BITs help establish the institutional framework necessary for a modern, developed economy able to benefit from economic globalization'. See Vandevelde, *Bilateral Investment Treaties*, supra note 715, p. 114.

⁷²⁰ Judith Shklar, 'Political Theory and the Rule of Law', in Allan Hutchinson and Patrick Monahan (eds.), *The Rule of Law: Ideal or Ideology* (Carswell, 1987), p. 1.

⁷²¹ Jeremy Waldron, 'Is the Rule of Law an Essentially Contested Concept (in Florida?)', 21 *Law and Philosophy* (2002), pp. 137-164, at 139.

⁷²² See Report of the Secretary-General, *The rule of law and transitional justice in conflict and post-conflict societies*, UN Doc. S/2004/616, 23 August 2004, para. 6.

advancing the rule of law, both internationally and domestically'.⁷²³ To support this bold argument, they refer to circumstances where domestic authorities have extracted rents from foreign investors under false pretenses; they suggest that investment treaties have 'replaced gunboat diplomacy' and stabilized the international order; they draw a parallel between foreign investors and 'ethnic minorities' to argue that without investment treaties foreign investors would be in a similarly vulnerable position as the latter; and, finally, they refer to cases where the investor's cause of action 'could just as fittingly be heard by a human rights tribunal'.⁷²⁴ Clearly, these arguments are either based on sweeping generalizations about the virtues of investment arbitration or on implausible correlations between conclusion of investment treaties and broader political developments (is there really a correlation between BITs and a more stable international order?). As noted, the proponents can always refer to cases where foreign investors are the target of arbitrary treatment, with investment arbitration providing the only effective remedy to which the affected investor can resort. But surely this does not support the argument that investment treaties promote the rule of law 'domestically and internationally'.

It is easy to create the *impression* that the investment treaty regime contributes to the rule of law by referring to cases where tribunals have referred to the concept. Similarly, as the rule of law is weak in many parts of the world, it seems plausible to *assume* that investment treaties are a step in the right direction. But impressionistic evidence is quite different from actual empirical evidence. State officials *may* change their view on policy-making if and when an investor is awarded compensation, but whether this can lead to a broader governance reform is an entirely different matter. An UNCTAD study noted that many investment disputes relate to measures adopted by provincial or local authorities who are not necessarily aware of the international obligations that the upper levels of government have committed to.⁷²⁵ This institutional distance has led a small number of countries to adopt mechanisms to inform 'various stakeholders at various levels of government' about the relevant investment treaty obligations to prevent future disputes.⁷²⁶

⁷²³ Brower and Blanchard, 'The Truth about Investor-State Arbitration', supra note 19, p. 755. For additional rule of law arguments, see e.g. Stephan W. Schill, 'In Defense of International Investment Law', in Mark Bungenberg et al. (eds.), *European Yearbook of International Economic Law* (Springer, 2016), pp. 309-341, at 313-318; Judd Kessler, 'Investment Arbitration, Legitimacy and National Law in Latin America: An Arbitrator's Perspective', 27 *The American Review of International Arbitration* (2016), pp. 265-310.

⁷²⁴ *Ibid.*, pp. 755-759.

⁷²⁵ UNCTAD, *Investor-State Disputes: Prevention and Alternatives to Arbitration* (United Nations, 2010), pp. 66-67.

⁷²⁶ *Ibid.*, pp. 67-74.

But clearly such mechanisms say nothing about the governance implications of potential investment claims in those countries. Sottorova notes, on the basis of interviews carried out with Turkish and Uzbek officials, that once the countries had faced a number of investor claims, 'some learning occurred' but this was 'confined to those [officials] who were involved...in defending the government in investment arbitration'. But when she refers to 'learning', Sottorova is not referring to a new policy mindset, but to a revision of investment treaties so as to 'prevent or mitigate future exposure of the government to investment claims'.⁷²⁷ Van Harten and Scott, in turn, find that Canadian officials had varying degrees of knowledge about Canada's investment treaty obligations, but policy proposals were often vetted in light of those obligations.⁷²⁸ This could be taken to mean either that the rule of law was bolstered in Canada or that duly processed policy proposals were chilled for fear of costly litigation. Bonnitcha, Poulsen and Waibel refer to three studies which looked at the World Bank's Worldwide Governance Indicators (WGI) to see whether the conclusion of BITs leads to improvement in a country's WGI 'regulatory quality' and 'rule of law' indicators over time. The respective conclusions of the studies were contradictory, and the WGI data itself is based on assumptions and methods that undermine the quality and reliability of the conclusions.⁷²⁹

One empirical study purported that the conclusion of BITs 'can sometimes have a negative effect on domestic governance quality' when investment disputes are taken away from domestic courts and local institutions are given no incentives to engage in reform.⁷³⁰ Another study concluded that in autocratic countries BITs create parallel property rights regimes, as foreign investors have no incentive to lobby for improved domestic governance, whereas domestic business elites continue to benefit from a 'stagnating domestic property rights environment'.⁷³¹ Similarly, Wälde has argued that 'there is no

⁷²⁷ Mavluda Sottorova, 'Reassertion of Control and Contracting Parties' Domestic Law Responses to Investment Treaty Arbitration: Between Reform, Reticence and Resistance', in Andreas Kulick (ed.), *Reassertion of Control over the Investment Treaty Regime* (Cambridge University Press, 2016), pp. 53-80, at 59-60.

⁷²⁸ Gus van Harten and Dayna Nadine Scott, 'Investment Treaties and the Internal Vetting of Regulatory Proposals: A Case Study from Canada', 7 *Journal of International Dispute Settlement* (2016), pp. 92-116.

⁷²⁹ Bonnitcha, Poulsen and Waibel, *The Political Economy*, supra note 679, pp. 170-172. The studies they refer to are Cesar Aranguri, 'The Effect of BITs on Regulatory Quality and the Rule of Law in Developing Countries' (an unpublished paper, 2010); Tom Ginsburg, 'International Substitutes for Domestic Institutions: Bilateral Investment Treaties and Governance', 25 *International Review of Law and Economics* (2005), pp. 107-123; Jan Peter Sasse, *An Economic Analysis of Bilateral Investment Treaties* (Springer, 2011).

⁷³⁰ Ginsburg, 'International Substitutes for Domestic Institutions', supra note 729, p. 121.

⁷³¹ Soumyajit Mazumder, 'Can I Stay a BIT Longer? The Effect of Bilateral Investment Treaties on Political Survival', 11 *The Review of International Organizations* (2016), pp. 477-521, at 477.

evidence that a developed and effective legal framework [i.e. the rule of law] is either a necessary condition for economic development or for growth in international trade and investment'.⁷³² He also noted that corruption may be more preferable to investors 'familiar with a host country setting' as it 'compensates for over-rigid regulation and bureaucratic inertia'.⁷³³ The merits of his comments aside, the point is that simplistic references to the rule of law seem remarkably out of touch with the dynamics of investment decisions and the varied circumstances under which investors operate. This is not to argue that investment protection is not necessary in many parts of the world, but to point out that sugar-coating the argument with references to the rule of law is, well, sugar-coating rather than a statement grounded in solid evidence. Then again, *if* the investment treaty regime is understood to set and enforce international protection standards, each investment treaty and arbitration can seem to embody the international rule of law. In sum, very little research has been done on the impact that investment treaties and arbitration have on the rule of law and domestic governance, with existing evidence providing no support to the proponents' general argument.

Even the most ardent proponents of the investment treaty regime tend to acknowledge that the rule of law argument is weak in respect of 'countries with well-developed judicial systems',⁷³⁴ but, as an influential advocacy group put it, this is not a reason for excluding investment protection from agreements between developed economies, because 'countries that enact laws and regulations with due process and that respect the rule of law have nothing to fear from international arbitration as their acts are not likely to be challenged'.⁷³⁵ This argument warrants a comment. Generally speaking, the decisions of courts and tribunals are always subject to varying degrees of criticism, even in countries that place highest in rule of law rankings. All courts render judgments that either have devastating consequences for the concerned individuals or that provide less than perfect redress for the disputing parties, and this includes the courts of, say, the Nordic countries. To give an example, the European Court of Human Rights continues to render judgments against Finland although the latter is regularly on the podium of various global rule of law rankings. This means that advocacy groups can always invoke the rule of law argument by

⁷³² Wälde, 'Law, Contract and Reputation, supra note 699, at 191.

⁷³³ Ibid., p. 194-195.

⁷³⁴ Brower and Schill, 'The Legitimacy of international Investment Law', supra note 18, p. 479 (footnote 28).

⁷³⁵ See European Federation for Investment Law and Arbitration, *A response to the criticism against ISDS*, 17 May 2015, para. 9.3.

referring to cases where the members of their constituencies have suffered injustice at the hands of domestic courts or where access to courts is limited in one or another way.⁷³⁶ The argument that developed economies have nothing to fear from investment arbitration diverts attention away from the fact that what the 'rule of law' means is a highly perspectival matter in the circumstances of specific cases, with arbitral tribunals judging cases differently than domestic courts precisely because the applicable standards and assumptions are different.

Hence, although there is broad consensus over the basic components of the rule of law, and although such definitions are useful in analyzing the legitimacy of judiciaries and the perceptions that publics have of them, it seems important to distinguish such assessments from the meaning that the concept has for the disputing parties, on the one hand, and for domestic courts and arbitral tribunals on the other hand. The factual and legal matrix of most investment disputes is contradictory and ambiguous, and the parties can make opposing (and often equally convincing) arguments about how the case should be decided, which suggests that the rule of law is in the eye of beholder in case specific circumstances. The argument that 'countries with well-developed judicial systems' need not worry about investment arbitration is also problematic for another reason. Developed states have faced an increasing number of claims under investment treaties, many of which center on measures adopted in sensitive areas of policy-making. This is not surprising given that arbitral tribunals apply different standards than domestic courts, and resourceful law firms are inclined to test to what extent arbitral tribunals' views on acceptable public policy might differ from those of judiciaries which enjoy widespread legitimacy among the population. A good example of this is provided by the *Bilcon* tribunal's decision on jurisdiction and liability in 2015.⁷³⁷ The case centered on the plans of a US owned company to develop and operate a mining quarry and marine terminal in Nova Scotia. The claimants were obligated to carry out an environmental assessment in accordance with Canadian federal law, which a Joint Review Panel (JRP) was to assess. The tribunal noted

⁷³⁶ In this regard, Schill points out that foreign investors are excluded from the 'enjoyment of fundamental rights' and have no access to the German Constitutional Court. Similarly, he points out that in some countries 'certain government measures may be completely exempt from domestic judicial review'. This creates the impression that lack of access to courts and lack of judicial review affect foreign investors in particular, but Schill provides no evidence in this regard, nor suggests that such evidence exists. See Schill, 'In Defense of International Investment Law', supra note 723, p. 316.

⁷³⁷ *William Ralph Clayton, William Richard Clayton, Douglas Clayton, Daniel Clayton and Bilcon of Delaware Inc. v. Government of Canada*, UNCITRAL, PCA Case No. 2009-04, Award on Jurisdiction and Liability, 17 March 2015.

that the JRP process 'is the most rigorous, protracted and expensive kind of review...[and] involves public hearings and a report by an independent panel'.⁷³⁸ The JRP recommended that the claimant's application for the approval of the project is rejected on the ground that the project would have had significant and adverse effects 'on community core values', and the federal and provincial authorities followed suit by refusing to grant the necessary permits.

This led to the NAFTA arbitration and the tribunal held that Canada had violated its obligations to provide international minimum standard of treatment and national treatment. Neither Canada's federal law nor Nova Scotia's law recognized the concept of 'community core values', with the implication being that it was highly problematic to use it as a basis to make recommendations on the project's approval.⁷³⁹ Similarly, the JRP report failed to specify what the standard means, and the claimant was never informed of the standard's existence, nor of its 'overriding importance' in getting approval for the project.⁷⁴⁰ The JRP report had also failed to consider what mitigation measures the claimants could adopt so as to receive approval, although this is what the federal law arguably required.⁷⁴¹ Taken together, the JRP process amounted to arbitrary and unjustified treatment which breached the minimum standard of treatment under Article 1105 NAFTA.⁷⁴² It also violated the national treatment obligation, because the claimant received less favorable treatment than Canadian investors, because the 'community core values' standard had not been previously applied and similar domestic projects had been analyzed in light of potential mitigation measures.⁷⁴³

As two commentators have noted, Canada's liability stemmed from what the tribunal 'considered to be due process and rule of law deficiencies' in the implementation of its own environmental laws.⁷⁴⁴ The JRP report's reliance on community core values implies that the concerns of the local population were central to the recommendation to reject the claimant's application. That state organs adopt the preferences of local communities in

⁷³⁸ Ibid., para. 15.

⁷³⁹ Ibid., para. 508.

⁷⁴⁰ Ibid., paras. 506 and 555.

⁷⁴¹ Ibid., para. 546.

⁷⁴² Ibid., paras. 588-604.

⁷⁴³ Ibid., paras. 685-731. It is noteworthy that the tribunal was split 2 to 1, with the dissenting arbitrator (appointed by Canada) finding that the JRP process was compatible with the relevant NAFTA obligations.

⁷⁴⁴ Laura Létourneau-Tremblay and Daniel Behn, 'Judging the Misapplication of a State's Own Environmental Regulations', 17 *Journal of World Investment & Trade* (2016), pp. 829-838, at 830.

policy-making is far from evident, but the broader point is that the way in which domestic institutions interpret and apply domestic law in case-specific circumstances is prone to include situations where the law is interpreted and applied in a way that displeases one of the parties, and this holds equally true in respect of countries which are perceived to uphold the rule of law. When reading the *Bilcon* award, one can agree that the JRP report applied the federal law in a manner that was problematic in a formal sense, although both the dissenting arbitrator and a number of Canadian environmental law experts have criticized the tribunal's analysis. In their view, the 'community core values' standard was among the criteria against which the JRP was required to evaluate the project.⁷⁴⁵ The claimants did not exhaust local remedies before initiating the arbitration,⁷⁴⁶ so Canadian courts will not be able to review the legality of the JRP process in light of Canadian law.⁷⁴⁷ The point of *Bilcon* is that foreign investors will undoubtedly think that investment arbitration is a useful remedy in case a dispute arises with the host state, but clearly the same principle applies in respect of each and every interest group. Granting privileged access to foreign investors should be grounded on clear evidence pointing to discrimination and arbitrary treatment in specific countries, and in case of developed (and most developing) countries such evidence awaits discovery. *Bilcon* also suggests that arbitral tribunals may interpret domestic law rules differently than domestic courts, and such inconsistency will seem problematic for many.

In sum, the rule of law argument is less than plausible and should be met with caution, also in the context of intra-EU BITs. While some formerly socialist states place low on global

⁷⁴⁵ One commentator argues that the JRP report used the 'community core values' concept as an umbrella term that brought together the different aspects of the category 'human environment effects', the assessment of which was part of the JRP's mandate. In other words, the term 'community core values' was an alternative description of a criterion that the JRP was obligated to assess under the applicable law. See Meinhard Doelle, 'Clayton Whites Point NAFTA Challenge Troubling', *Environmental Law News*, 25 March 2015 (another general argument was that the tribunal 'lacked, with the exception of the dissenting member, even a basic understanding of the legal context within which the decisions it was asked to rule on were made. It also lacked any real appreciation for the factual context within which the decisions being challenged were made...[and] that the "expert legal advice" was completely misunderstood and misapplied by the majority of the NAFTA tribunal').

⁷⁴⁶ NAFTA does not require investors to exhaust local remedies before bringing a claim. See Article 1121 NAFTA (official citation North American Free Trade Agreement, 32 ILM 289, 605 (1993)).

⁷⁴⁷ Canada has sought the award's annulment before its domestic courts on the ground that the award conflicts with the public policy of Canada. See *Attorney General of Canada v William Ralph Clayton, William Richard Clayton, Douglas Clayton, Daniel Clayton and Bilcon of Delaware*, Notice of Application, FC, T-1000-15 (16 June 2015), para. 16.

rule of law rankings, particularly with respect to 'judicial independence',⁷⁴⁸ this does not necessarily indicate that their courts mistreat foreign investors. Lack of judicial independence could target mostly the host state's own nationals, whether individuals or companies, and its existence could also be based on public perceptions whose validity is impossible to verify. More generally, and as noted, the empirical question of whether foreign investors are subject to mistreatment in host states has not been addressed systematically, and existing research points to an opposite conclusion. Foreign investors are more likely to receive better treatment in comparison to domestic investors.

6.4. Two Economic Arguments

6.4.1. Investment Treaties Increase Investment Flows

A widely-used argument is that the conclusion of BITs will increase investment flows, as the possibility or threat of arbitration stabilizes the host state's regulatory framework and increases the likelihood of positive investment decisions.⁷⁴⁹ Larger investment stocks, in turn, contribute to economic development, as FDI leads to employment opportunities, rises in tax revenue, improved worker skills, and to transfers of technology to developing states. Further, investment treaties increase economic efficiency in their own right by decreasing the political risk that comes with investing in a foreign market. Lower political risk results in more cost-efficient investment projects, with the prices of the investor's products and services going down. Brower and Schill provide a succinct summary of this broad argument: 'investment treaties create a legal infrastructure for the functioning of a global market economy by protecting property rights', and assuming that perfect market conditions exist, BITs contribute to 'the efficient allocation of capital, economic growth and development', and thus 'benefit both capital-exporting and capital-importing countries through an increase in overall well-being'.⁷⁵⁰ If this is what investment treaties contribute to, who could be against them?

The question of whether BITs increase investment flows, however, is a very complex matter, and some of the existing research is of less than stellar quality as the analyses have

⁷⁴⁸ For example, in the World Economic Forum's judicial independence ranking, Bulgaria is placed 126th and the Slovak Republic 130th among 140 countries. See at <http://reports.weforum.org/global-competitiveness-report-2014-2015/rankings/> (accessed 26 August 2017).

⁷⁴⁹ This section focuses on the economic impact that investment treaties have on host states, but not on home states.

⁷⁵⁰ Brower and Schill, 'The Legitimacy of International Investment Law', *supra* note 18, p. 496-497.

ignored important differences between contents of investment treaties and host state characteristics, with some studies paying inadequate attention to the so called 'endogeneity' problem.⁷⁵¹ For example, many early studies failed to make a distinction between investment treaties containing robust arbitration clauses and those that did not.⁷⁵² Similarly, the question whether investment treaties encourage investment only in specific sectors (such as extractive industries) is clearly important, as a positive answer would imply that BITs are redundant for countries that have, for example, scarce natural resources, but there is relatively little research that focuses on this question.⁷⁵³ The endogeneity problem refers to the scenario where a BIT is concluded around the same time that a host state adopts a number of other legislative and administrative reforms, including rules on investment liberalization, and if this is not accounted for in the analysis, the conclusions will be less than plausible.⁷⁵⁴ With these caveats in mind, existing research provides inconclusive answers to the question whether BITs increase investment flows, with one commentator noting that 'some studies show that BITs can have massive positive impacts on foreign investment; others show modest positive impacts; still others show no impact at all, or even a negative impact'.⁷⁵⁵ Bonnitcha, Poulsen and Waibel note that a majority of the studies 'find that investment treaties have a positive and statistically significant impact on inward FDI in at least some circumstances', but the 'scale of the impact varies remarkably', and 'a sizeable minority of studies' find that BITs have no statistically significant effect on FDI flows.⁷⁵⁶

An UNCTAD study on developing economies concluded that investment treaties (whatever their contents) alone are not sufficient to attract FDI, with other determinants - including political stability, access to natural resources, market size, labor costs, tax breaks and other such incentives - playing a 'more powerful role'.⁷⁵⁷ Clearly, the correlation between investment flows and BITs is an intricate question that requires appreciation of

⁷⁵¹ The discussion in this section owes a large debt to Chapters 2, 5 and 6 in Bonnitcha, Poulsen and Waibel, *The Political Economy*, supra note 679.

⁷⁵² Ibid., p. 159.

⁷⁵³ Ibid., p. 161.

⁷⁵⁴ Ibid., pp. 161-162. They also note that the 'quality of FDI stock data is poor' and identify a number of specific deficiencies that undermine the credibility of the relevant data (see at pp. 162-164).

⁷⁵⁵ See Jason Webb Yackee, 'Do Bilateral Investment Treaties Promote Foreign Direct Investment? Some Hints from Alternative Evidence', 51 *Virginia Journal of International Law* (2010), pp. 397-442, at 399

⁷⁵⁶ Ibid., p. 159.

⁷⁵⁷ UNCTAD, *The Role of International Investment Agreements in Attracting Foreign Direct Investment to Developing Countries* (United Nations, 2009), at xi-xii.

the above methodological limitations.⁷⁵⁸ The mixed results of existing research suggests that it is easy to point to studies that either support or undermine the correlation, but the most plausible approach is to acknowledge that as the evidence is highly mixed, and difficult to assess without proper understanding of the attendant methodologies, it does not provide conclusive support to the *general* argument that investment treaties increase investment flows. A country-specific analysis that incorporates other FDI determinants would make much more sense.⁷⁵⁹ Another commonsense observation is that there is even less evidence about the impact of investment treaties on investment flows between developed economies, given the rareness of 'North-North' BITs. It is noteworthy that the Commission's fact sheet on investment treaties notes that investment 'protection provisions, including investor-state dispute settlement are important for investment flows', and this general statement is linked up with the argument that FDI is 'a critical factor for growth and jobs'.⁷⁶⁰ What this suggests is that it does not necessarily matter what empirical evidence says about the correlation between BITs and investment flows if and when policy-makers and state officials share a belief that such correlation exists. I will return to this below.

⁷⁵⁸ Bonnitca, Poulsen and Waibel, *The Political Economy*, supra note 679, p. 165. There are also some qualitative studies that survey whether companies consider investment treaties as being relevant for their decision-making. Again, the results are mixed and what should of course note that their reliability is impossible to verify. Relevant studies include Lisa Sachs and Karl Sauvant, 'BITs, DTTs, and FDI Flows: An Overview', in Karl Sauvant and Lisa Sachs (eds.), *The Effect of Treaties on Foreign Direct Investment: Bilateral Investment Treaties, Double Taxation Treaties and Investment Flows* (Oxford University Press, 2009); Jason Webb Yackee, 'Do BITs really work? Revisiting the empirical link between investment treaties and foreign direct investment', in Sauvant and Sachs (eds.), *The Effect of Treaties on Foreign Direct Investment*; Copenhagen Economics, *EU-China Investment Study: Report for European Commission* (Copenhagen Economics, 2012); Hogan Lovells, Bingham Centre for the Rule of Law, and the British Institute of International and Comparative Law, *Risk and Return: Foreign Direct Investment and the Rule of Law* (London, 2015).

⁷⁵⁹ It is also useful to remember that investment treaties are just one instrument for protecting foreign investment: political risk insurance and investment contracts entailing arbitration clauses are regularly used in practice, and though they are not identical to BIT protections, they receive relatively modest attention in the political debate on investment arbitration. For a discussion (based on contractual theories) on why treaty based investment arbitration is 'better' than arbitration under an investment contract, see Anne van Aaken, 'International Investment Law between Commitment and Flexibility: A Contract Theory Analysis', 12 *Journal of International Economic Law* (2009), pp. 507-538. For a tentative argument that political risk insurance provides adequate protection to investors, see Efi Chalamish and Robert Howse, 'Conceptualizing Political Risk Insurance: Toward a Legal and Economic Analysis of the Multilateral Investment Guarantee Agency (MIGA)', in Mathias Audit and Stephan Schill (eds.), *The Transnational Law of Public Contracts* (Bruylant, 2015), pp. 721-736.

⁷⁶⁰ EU Commission, 'Investment Protection and Investor-to-State Dispute Settlement in EU agreements', *Fact Sheet*, November 2013, p. 3.

6.4.2. FDI Promotes Economic Growth and Development

Perhaps the more interesting (and important) question is whether FDI promotes economic growth and development in host states, and if it does, how the attendant costs and benefits are distributed.⁷⁶¹ In this regard, an extreme example is found in the following description of a US\$1.5 billion natural gas plant in Equatorial Guinea, which was built and operated by a US oil company:

'The plant...could have been on the moon for all the benefit it offered local business... Instead of buying cement from a Malabo company that might not deliver on time, Marathon [i.e. the oil company] built a small cement factory on the construction site. Raw materials were imported, and the factory would be dismantled when construction ended. The trailers in which the Asians [i.e. the foreign workers working at the site] lived were prefab units - no local materials or local labor had been used to build them. The plant had its own satellite phone network, which was connected to the company's Texas network - if you pieced up a phone you would be in the Houston area code, and dialling a number in Malabo would be an international call. The facility also had its own power plant and water-purification and sewage system. It existed off the local grid.'⁷⁶²

While this is by no means your average foreign direct investment, it already points to problems in the proponents' argument that there 'has long been consensus that foreign direct investment increases national income and employment and accelerates development and modernization, including by establishing valuable tangible assets within the host country, promoting the development of human capital, facilitating the acquisition of technical knowledge, and creating network effects that create opportunities for future market access abroad'.⁷⁶³ A central conclusion of the economic literature is that FDI '*can* play an important role for economic development in host states...[but] its impact is

⁷⁶¹ There are also number of general arguments for and against investment liberalization, but the following does not focus on these, nor do I address the question whether investment treaties containing liberalization commitments bring about economic benefits. For a discussion (and references to additional sources) on these questions, see Bonnitcha, Poulsen and Waibel, *The Political Economy*, supra note 679, pp. 172-178.

⁷⁶² Peter Maass, *Crude World: The Violent Twilight of Oil* (Vintage, 2009), pp. 35-36.

⁷⁶³ Brower and Blanchard, 'The Truth about Investment Arbitration', supra note 19, p. 703.

contingent on host state and investment-specific conditions'.⁷⁶⁴ Those conditions relate to, for example, how educated the local workforce is,⁷⁶⁵ to the mode of entry of the foreign investor,⁷⁶⁶ and to the 'quality' of domestic institutions.⁷⁶⁷ A related point is that dependence on the exploitation of natural resources has a 'long-run negative effect on economic performance', and these 'problems appear to be particularly acute for poor countries'.⁷⁶⁸ In other words, investments in the extractive industries sector appear to have adverse economic effects for countries struggling with administrative and regulatory incapacity. Given this, Howse argues that investors 'whose activities generate significant negative externalities...will be the most attracted to [investment] treaty protection when they are investing in countries with low regulatory standards and weak governance', although the evidence suggests that FDI is least likely to promote economic development under such circumstances.⁷⁶⁹ Howse infers that even if some of these types of investments are made by virtue of an investment treaty, 'this might not be the kind of FDI that is beneficial to economic development, or it might not be directed towards the kinds of countries likely to benefit developmentally from FDI'.⁷⁷⁰

But does this evidence matter? Challenging the broad proposition that FDI contributes to economic development is not necessarily an easy task, whatever the empirical evidence suggests. For example, trade and investment liberalization is among the top priorities of the Commission for the 2015-2019 period and its recent communication paper noted that foreign direct investment 'is an important source of jobs, growth and innovation'.⁷⁷¹ The 2017 World Investment Report, prepared by UNCTAD, surveyed changes in national laws

⁷⁶⁴ Bonnitcha, Poulsen and Waibel, *The Political Economy*, supra note 679, p. 49.

⁷⁶⁵ See Eduardo Borensztein, José De Gregorio, and Jong-Wha Lee, 'How does Foreign Direct Investment affect Economic Growth?', 45 *Journal of International Economics* (2011), pp.115-135.

⁷⁶⁶ Paula Neto, Antonio Brandão, and Antonio Cerqueira, 'The Impact of FDI, Cross Border Mergers and Acquisitions and Greenfield Investments on Economic Growth', 7 *The IUP Journal of Business Strategy* (2010), pp. 24-44.

⁷⁶⁷ Dani Rodrik, Arvind Subramanian and Francesco Trebbi, 'Institutions Rule: The Primacy of Institutions over Geography and Integration in Economic Development', 9 *Journal of Economic Growth* (2004), pp. 131-165, at 135. See also Theodore Moran, Edward M. Graham and Magnus Blomström (eds.), *Does Foreign Direct Investment Promote Development* (Peterson Institute for International Economics, 2005); Cristina Jude and Grégory Levieuge, *Growth Effect of FDI in Developing Economies: The Role of Institutional Quality* (Banque de France, June 2015); Manuchehr Irandoust, 'A Survey of Recent Developments in the Literature of FDI-Led Growth Hypothesis', 11 *Journal of World Investment & Trade* (2010), pp. 276-291.

⁷⁶⁸ Cullen Hendrix and Marcus Noland, *Confronting the Curse: The Economics and Geopolitics of Natural Resource Governance* (Peterson Institute for International Economics, 2014), p. 121.

⁷⁶⁹ Howse, 'International Investment Law and Arbitration', supra note 718, p. 17

⁷⁷⁰ Idem.

⁷⁷¹ EU Commission, Communication from the Commission: Welcoming Foreign Direct Investment while Protecting Essential Interests, COM(2017) 494 final, Brussels, 13 September 2017, p. 2.

and regulations and noted that most measures adopted in 2016 'aimed at investment promotion, facilitation and liberalization', including the liberalization of entry conditions for FDI.⁷⁷² Most developing countries have adopted 'deep market-oriented reforms',⁷⁷³ and south-south BITs are now counted in the hundreds,⁷⁷⁴ with a number of transitioning and developing countries having become capital-exporters. If and when policy-makers and governments the world over think that promoting cross-border investments is a priority, it seems somewhat irrelevant to point to the myriad ways in which FDI may manifest itself in different parts of the world. The entry conditions of large-scale investments and their post-establishment treatment - under national environmental law, corporate law, tax law and contract law, for example - are matters that fall under the responsibility of local governments whose decision-making various international institutions and actors strive to influence. While governments have much leeway in determining policy priorities and how to achieve them, in practice they are binding their hands in a multitude of ways. As noted, governments actively seek to encourage foreign investments in a number of ways - for example, by providing free consultation services to foreign companies contemplating on whether to make an investment - and the economic incentives that countries offer come in many shapes and forms. In this light, the evidence that suggests that correlation between FDI and economic growth and development is less than clear, may not at all matter for the (broadly understood) political class.

This also suggests that, as Neumayer once put it, 'what really matters is what policy makers believe, not what economic theory and evidence says'.⁷⁷⁵ While these beliefs may be based on crude simplifications and misunderstandings, they can still have important political ramifications when they are considered received wisdom among policy-makers and state officials. In this light, challenging the economic arguments about the virtues of investment treaties is an uphill battle, even if the arguments rely on anecdotal evidence and ideology or even go against the (scant) empirical evidence.

⁷⁷² UNCTAD, *World Investment Report 2017: Investment and the Digital Economy* (United Nations Publications, 2017), at xi.

⁷⁷³ Echandi, 'What Do Developing Countries Expect', *supra* note 719, at 4.

⁷⁷⁴ An UNCTAD study found that at the end of 2006, 27 percent (680 out of some 2500) of all BITs were concluded between developing countries. See UNCTAD, *World Investment Report 2007: Transnational Corporations, Extractive Industries and Development* (United Nations Publications, 2007), p. 17.

⁷⁷⁵ Eric Neumayer, 'Do Countries Fail to Raise Environmental Standards? An Evaluation of Policy Options Addressing "Regulatory Chill"', 4 *International Journal of Sustainable Development* (2001), pp. 231-244 (revised version, pp. 1-27, at 20, available at <http://eprints.lse.ac.uk/18895/>).

6.5. Conclusion

The preceding discussion provides few certain answers. The analysis sought to demonstrate that the arguments for investment treaties rely not on solid empirical evidence but on ambiguous or untested assumptions about the correlation between the investment treaty regime and economic development and the rule of law. While investment treaties *may* have a statistically relevant impact on investment flows between certain countries, on a general level other determinants appear to be more important for investment decisions. Similarly, the alleged correlation between FDI and economic development turned out to be equally equivocal, with evidence suggesting that the strength of the correlation varies 'across sectors and industries' and depends on the host state's political conditions and level of development.⁷⁷⁶ As to the rule of law argument, it has much intuitive appeal given the administrative incapacity and corruption prevalent in many countries as well as individual investment disputes where host states have acted in arbitrary and discriminatory ways. The suggestion was, however, that there is *no* evidence supporting the general argument that investment treaties and arbitration improve the quality of domestic governance. Investment arbitration may be the only effective remedy in many cases, but this does not constitute a plausible reference point for the general argument that promotes the further globalization of investment protection. Then again, if trade and investment liberalization are a top priority of public policy, and if investment treaties are *believed* to increase investment flows, it is likely that the correlation between the rule of law and investment treaties is among the beliefs that policy-makers and state officials have the world over. If everybody around you assumes that such correlation exists, it must exist whatever the evidence might say.

The rule of law argument also relates to the perception that the proponents have about the basic idea of investment arbitration. As Kessler put it, arbitrators 'are charged to apply in a careful and principled way, established international legal standards...[and] they must apply the law as it has been set forth in authoritative form by numerous arbitral tribunals, judges, scholars and practitioners'.⁷⁷⁷ Kessler refers to his own experience 'that, with rare exception, the arbitrators have been highly qualified professionals with broad and deep experience...[and they] felt genuinely honored to have been chosen to serve, and took the

⁷⁷⁶ Bonnitca, Poulsen and Waibel, *The Political Economy*, supra note 679, p. 48.

⁷⁷⁷ Kessler, 'An Arbitrator's Perspective', supra note 723, pp. 265-310, at 297.

responsibility of deciding disputes between private investors and sovereign governments as something akin to a sacred trust'.⁷⁷⁸ A logical corollary of Kessler's reflection is the idea that investment arbitration promotes the rule of law, as arbitrators ('with rare exception') not only have impeccable credentials but also a clear sense of ethics and a strong commitment to decide cases in a manner that holds water upon closer scrutiny by all stakeholders. Kessler appears to be offended by the widespread criticism of the investment treaty regime, which he sees as an 'important bulwark for the rule of law',⁷⁷⁹ and his contribution is animated by the worry that the critics do not appreciate the extent to which governments continue to disrespect basic notions of due process and justice. For him, investment arbitration provides a lifeline for foreign investors operating in an asymmetric threat environment. As Schwebel put it, the host state 'has not only the police power; it has the police. It can bring the weight of its bureaucracy, and its politicians, to bear. It can prescribe, delay, decree, tax, incite, and strangle'.⁷⁸⁰

The following chapter provides an opposing narrative about the reality of investment protection. In the critics' view, investment treaties and arbitration constitute an entirely different species. Rather than setting an international benchmark for what is reasonably acceptable government conduct, investment treaties further entrench the position of the most dominant players in the global economy at the expense of host states' regulatory autonomy and the promotion of public goods. Chapter 7 represents and unpacks the critic's version, after which I strive to join the different chapters of the thesis together and provide a more general assessment of the underlying themes as well as some general conclusions. As noted, the critique comes in many shapes and forms, but my analysis focuses on the general political critique, which questions the *raison d'être* of the regime and leaves the legal quibbling to others.

⁷⁷⁸ Ibid., p. 266.

⁷⁷⁹ Ibid., p. 300.

⁷⁸⁰ Schwebel, 'The Overwhelming Merits of Bilateral Investment Treaties', *supra* note 191, at 268.

7. The Critique of Investment Treaties and Arbitration

'The last two decades have witnessed the silent rise of a powerful international investment regime that has ensnared hundreds of countries and put corporate profit before human rights and the environment.'⁷⁸¹

This quote is from a report published by two NGOs in 2012 and its authors provide a biting description and analysis of the investment treaty regime and of the background of the 'elite arbitrators' who 'dominate' the attendant arbitration industry. The report may have contributed to bringing awareness on what previously was a largely unknown legal field in Europe, with the heated debate on the EU's external investment policy starting soon after. However, the ongoing debate in Europe is in large measure continuation of an earlier debate carried out with respect to the proposal on the Multilateral Agreement on Investment (MAI) and NAFTA investment provisions and arbitrations. The MAI negotiations started in 1995 and the purpose was to reach an agreement on investment protection and investment liberalization and to create effective dispute settlement mechanisms.⁷⁸² Given the relatively small number of OECD member states, MAI was to be a free-standing treaty open to accession by non-member states as well. The negotiations were discontinued in 1998 when France declared its withdrawal from the project after the draft text of the agreement had received extensive criticism from civil society actors and a number of developing countries. In particular, concerns were expressed about the impact that MAI could have on host states' policy space as well as about the political wisdom of providing privileged treatment to foreign investors.⁷⁸³ The current debate is also strikingly similar to the previous debates concerning the legitimacy of the WTO and I will address this debate in Chapter 8.

⁷⁸¹ Pia Eberhardt and Cecilia Olivet, *Profiting from injustice. How law firms, arbitrators and financiers are fuelling an investment arbitration boom* (Corporate Europe Observatory and the Transnational Institute, 2012), p. 7.

⁷⁸² Organization for Economic Co-operation and Development, 'OECD begins Negotiations on a Multilateral Agreement on Investment', News release, 27 September 1995.

⁷⁸³ For a discussion on the MAI negotiations and the attendant public criticism, see Rainer Geiger, 'Towards a Multilateral Agreement on Investment', 31 *Cornell International Law Journal* (1998), pp. 467-475; Jan McDonald, 'The Multilateral Agreement on Investment: Heyday or MAI-day for Ecologically Sustainable Development?' 22 *Melbourne University Law Review* (1998), pp. 617-656.

As to NAFTA, and to the surprise of many, Canada and the US quickly faced a number of claims under NAFTA Chapter 11 once the treaty had entered into force, although it was only Mexico that had resisted the chapter's inclusion. The US had lobbied diligently for Chapter 11 because it wished 'to liberalize Mexican restrictions on investment and to lock in legal protections for [US] investors'.⁷⁸⁴ Once NAFTA tribunals had reviewed US and Canadian legislative acts and domestic court decisions, and in some cases awarded compensation for the claimant investors, the critics started to argue that the decisions constitute an 'extraordinary attack on normal government activity' and threaten the national sovereignty of NAFTA states as well as 'their ability to freely engage in democratic law-making processes'.⁷⁸⁵ As the number of arbitrations under other investment treaties started to rise around the same time as these concerns were expressed, the critique gradually broadened beyond the NAFTA context, but its basic components remain the same, although there is much variation in the analytic rigor of the arguments. Before proceeding to addressing the critique in more detail, it is useful to note that only a relatively small number of states have made changes to their existing investment treaties. Canada and the US have drafted more 'state-friendly' model BITs, and already in 2001, the NAFTA Free Trade Commission issued an interpretive statement providing that the 'fair and equitable treatment' and 'full protection and security' standards found in Chapter 11 are equivalent to the minimum standard of treatment of aliens under customary international law.⁷⁸⁶ This came about as a reaction to awards where NAFTA tribunals had provided more liberal interpretations of the standards.

The 'backlash' against investment arbitration has been particularly strong in Latin America where governments have ratcheted up the controversy with high-octane rhetoric equating investment arbitration to 'colonialism' and 'slavery' with respect to large multinationals, Washington and the World Bank.⁷⁸⁷ Bolivia, Ecuador and Venezuela denounced the ICSID

⁷⁸⁴ United States General Accounting Office, *North American Free Trade Agreement: Assessment of Major Issues: Report to Congress*, GAO/GGD-93-137B (September 1993), at 19.

⁷⁸⁵ The quotes are from Public Citizen, *NAFTA Chapter 11 Investor-to-State Cases: Bankrupting Democracy* (2001), p. 2, and Ray C. Jones, 'NAFTA Chapter 11 Investor-to-State Dispute Resolution: A Shield to Be Embraced or a Sword to Be Feared?', 7 *Brigham Young University Law Review* (2002), pp. 527-559, at 528.

⁷⁸⁶ NAFTA Free Trade Commission, *Notes of Interpretation of Certain Chapter 11 Provisions* (31 July 2001). The statement is available at http://www.naftalaw.org/files/NAFTA_Comm_1105_Transparency.pdf (accessed 25 August 2017). On reactions to the statement by NAFTA tribunals, see Anthea Roberts, 'Power and Persuasion in Investment Treaty Arbitration: The Dual Role of States', 104 *American Journal of International Law* (2010), 179-225, at 180-181.

⁷⁸⁷ See statement by then Ecuadorian president Rafael Correa, made on the radio program 'Dialogue with the President' on May 30, 2009, as reported by Fernando Carbrera Diaz in 'Ecuador continues exit from ICSID',

Convention as a response to multiple claims raised against them under the Convention,⁷⁸⁸ and Ecuador took further steps by amending its constitution in 2008, which made entering into treaties containing investment arbitration provisions unconstitutional. Ecuador's Supreme Court has also issued a series of rulings declaring that investment arbitration provisions in a number of Ecuador's BITs are unconstitutional and many of the existing BITs are undergoing termination procedures.⁷⁸⁹ South Africa, in turn, suspended the signing of new investment treaties pending a review of its existing treaties and experience.⁷⁹⁰ Many investment treaties have also undergone different degrees of reform, so as to accommodate some of the perceived flaws in their original design,⁷⁹¹ and some of the procedural rules governing the transparency of arbitral proceedings have been amended to increase public access.⁷⁹² To give two examples, the preambles of many 'second generation' BITs contain references to labor rights, sustainable development, protection of the environment and other similar priorities,⁷⁹³ and some BITs now include general exceptions clauses which provide that the contracting states may take measures whose object is the protection of public health and safety as well as other essential state interests.⁷⁹⁴ In Europe, the Commission's pressure on intra-EU BITs has led to some unilateral terminations, but most of the treaties remain in force and investments that were made prior to the terminations continue to enjoy BIT protections as provided in the treaties' sunset clauses.⁷⁹⁵

Investment Treaty News, 5 June 2009. Available at <http://www.iisd.org/itn/2009/06/05/ecuador-continues-exit-from-icsid/> (accessed 21 August 2017).

⁷⁸⁸ Some of the relevant events are discussed in Diana Marie Wick, 'The Counter Productivity of ICSID Denunciation and Proposals for Change', 11 *The Journal of International Business and Law* (2012), pp. 239-291.

⁷⁸⁹ On some of these developments, see Rodrigo Polanco Lazo, 'Is There a Life for Latin American Countries after Denouncing the ICSID Convention?', 11 *Transnational Dispute Management* (2014), at 15-20.

⁷⁹⁰ Republic of South Africa, Department of Trade and Industry, *Bilateral Investment Treaty Policy Framework Review* (June 2009).

⁷⁹¹ On some of these reforms, see Asha Kaushal, 'Revisiting History: How the Past Matters for the Present Backlash Against the Foreign Investment Regime', 50 *Harvard International Law Journal* (2009), pp. 491-534, at 493-495; Malcolm Langford and Daniel Behn, 'Managing Backlash. The Evolving Investment Treaty Arbitrator?' (September 2016, on file with author), pp. 5-8.

⁷⁹² For a discussion of these amendments, see N. Jansen Calamita, 'Dispute Settlement Transparency in Europe's Evolving Investment Treaty Policy', 15 *Journal of World Investment & Trade* (2014), pp. 645-678.

⁷⁹³ See Andrew Newcombe, 'Sustainable Development and Investment Treaty Law', 8 *Journal of World Investment & Trade* (2007), pp. 357-407, at 398-402.

⁷⁹⁴ To give an example, Article 14(1) of the Finland-Zambia BIT provides that nothing in the agreement 'shall be construed as preventing a Contracting Party from taking any action necessary [...] for the protection of human, animal or plant life or health'. See Agreement between Finland and Zambia on the Promotion and Protection of Investments (SopS 21/2014).

⁷⁹⁵ On these developments, see *supra* note 196.

But an overwhelming majority of BITs have not been amended or terminated, and some countries that had adopted a critical stand on investment treaties have changed tack and are concluding new treaties.⁷⁹⁶ Similarly, countries and/or regions with a major share of global FDI are negotiating so called mega-regional trade agreements, which include investment protection chapters, and this of course includes the EU's trade agreements with Canada, China and the US. The future of the Commission's proposal for an investment court system is uncertain, but that proposal is meant to address the procedural aspects of the critique, whereas the state-of-the-art CETA investment provisions are designed to address the political and substantive critique, in particular by ensuring that host states' regulatory space is safeguarded. I will provide a comment on the relevant CETA provisions below.

The rest of this chapter proceeds as follows. I start by providing a general sketch of the critics' basic view of investment treaties. If the proponents rely on individual cases to show that governments act in ways that are 'blatantly arbitrary, illegal or unconstitutional',⁷⁹⁷ the critics have their own pet cases which relate to policy measures adopted in sensitive areas of public policy, such as public health and protection of the environment. Importantly, these cases (appear to) confirm the more general view that the critics have of economic globalization. I provide some comments on why it is problematic to rely on individual cases - or case outcome statistics - when arguing for or against investment treaties. After this, I look at two arbitrations where the claimant investors challenged measures that were taken as a response to political opposition against the claimant's investment. The tribunals approached the political context in entirely different ways, in part because of the parties' arguments. The first case, *Tecmed*, reflects how difficult it is to maintain a black-and-white view of investment disputes when the factual record is put under the microscope, which also highlights that the critique should become more open about its political preferences in order to make more sense. The second case, *Occidental*, provides a useful basis for a discussion on some of the weaknesses of the critics' political vision. In my view, *Occidental* should not be seen as simplistically juxtaposing the interests of a US oil giant and a poor developing country, but as a reflection of the costs that economic development brings about the world over, including in stable western democracies. These case comments are followed by two more general arguments that academic commentators have

⁷⁹⁶ For example, Australia reversed its policy by signing the Trans-Pacific Partnership (TPP) in 2016. The agreement contains a full-blown investment protection chapter.

⁷⁹⁷ Kessler, 'Arbitrator Perspective', supra note 723, p. 282.

made about the relationship of investment treaties and economic liberalism. The 'regulatory chill' argument asserts that the threat of investment arbitration compels host states to refrain from adopting public interest measures that might affect influential foreign investors, with the question being if there is evidence that supports this intuitively plausible concern. The second argument strives to prove the schematic thesis that international investment law is the handmaiden of neoliberal ideas and policies. This argument forms the core of Sornarajah's recent monograph, and I will provide a summary of its main components as well as consider its limitations and purpose.

7.1. Appearances Matter

A common thread that runs to the critical arguments is that investment arbitration undermines the domestic political process and provides special privileges to already privileged actors. That tribunals may award sizeable compensation only adds insult to the injury by creating uncertainty over the fiscal implications of domestic policy proposals. This basic idea is behind arguments such as that 'traditional' investment arbitration is contrary to sustainable development,⁷⁹⁸ or that it 'fundamentally shift[s] the balance of power between investors, states and other affected parties in a manner that undermines fair resolution of legal disputes'.⁷⁹⁹ Others note that the critics have argued that investors 'may use BIT provisions to challenge human rights-inspired regulations that interfere with...[their] investment',⁸⁰⁰ or that companies may 'demand compensation when a government-initiated change lowers the value of their assets',⁸⁰¹ or that arbitral tribunals 'have on many occasions struck down host states' environmental regulations and awarded

⁷⁹⁸ UNCTAD, *World Investment Report 2012: Towards a New Generation of Investment Policies* (United Nations, 2012), pp. 89-90.

⁷⁹⁹ Open Letter from Lawyers to the Negotiators of the Trans-Pacific Partnership Urging the Rejection of Investor-State Dispute Settlement, 8 May 2012, available at <http://tpplegal.wordpress.com/open-letter/>. See also the statement by 121 scholars in respect of the TTIP's planned investment protection provisions, Statement of Concern about Planned Provisions on Investment Protection and Investor-State Dispute Settlement (ISDS) in the Transatlantic Trade and Investment Partnership (TTIP) (arguing that '[a]t root, the [investment treaty] system involves a shift in sovereign priorities toward the interests of foreign owners of major assets and away from those of other actors whose direct representation and participation is limited to democratic processes and judicial institutions.'), available at https://www.kent.ac.uk/law/isds_treaty_consultation.html (accessed 1 July 2016).

⁸⁰⁰ Ursula Kriebaum, 'Privatizing Human Rights: The Interface between International Investment Protection and Human Rights', in August Reinisch and Ursula Kriebaum (eds.), *The Law of International Relations: Liber Amicorum Hanspeter Neuhold* (Eleven International Publishing, 2007), pp. 165-189, at 177.

⁸⁰¹ Joseph Stiglitz, 'Regulating Multinational Corporations: Towards Principles of Cross-Border Legal Frameworks in a Globalized World Balancing Rights with Responsibilities', 23 *American University International Law Review* (2008), pp. 451-558, at 457.

large damages to investors'.⁸⁰² At the outset, it should be noted that while tribunals in principle may order host states to repeal or amend the challenged measure, monetary compensation is the main (if not only) remedy used in practice. Hence, the argument about tribunals striking down 'environmental regulations' is clearly misleading, as is the argument that investors can win cases solely on the basis of lost profits.

In addition to scholarly arguments, the media has reported cases that provide much fodder for the critique, with the attendant circumstances juxtaposing private and public interests. For example, Indonesia's exemption of a number of mainly foreign-owned mining companies from a ban on open-pit mining in protected forests appeared to stem from the companies' previous threats to take Indonesia to arbitration if the ban is adopted.⁸⁰³ Another news story related to a lead-acid battery factory in El Salvador, which was owned by members of a prominent El Salvadorian family who also held United States citizenship. The factory's operation produced clouds of ash, which contained lead and reportedly caused severe health problems among the local population, including deaths of children. The government ordered closing of the factory and brought charges of aggravated environmental pollution against the owners who quickly fled to the United States. The owners then threatened to bring an expropriation claim against El Salvador under the relevant BIT, which eventually led El Salvador's prosecutors to settle the case, with the owners moving back from the threat of arbitration.⁸⁰⁴ An oft-quoted news article contributed to this shady image by starting with the following description of how arbitral tribunals operate: 'Their meetings are secret. Their members are generally unknown. The decisions they reach need not be fully disclosed'.⁸⁰⁵

The 2012 NGO report, referred to above, uses equally vivid language to condemn the investment treaty regime, with the central message being that by 'signing investment treaties and agreeing to arbitration, states have...accepted to be sued by the devil in hell'.⁸⁰⁶

⁸⁰² Lisa Bennett, 'Note, Are Tradable Carbon Emissions Credits Investments? Characterization and Ramifications Under International Investment Law', 85 *New York University Law Review* (2010), pp. 1581-1617, at 1584-1585.

⁸⁰³ Kyla Tienhaara, 'What You Don't Know Can Hurt You: Investor-State Disputes and the Environment', 6(4) *Global Environmental Politics* (2006), pp. 73-100, at 87-96; Stuart G. Gross, 'Inordinate Chill: BITS, non-NAFTA MITS, and Host-State Regulatory Freedom: an Indonesian Case Study', 24 *Michigan Journal of International Law* (2003), pp. 893-960.

⁸⁰⁴ This story is reported in Chris Hamby, 'The court that rules the world', *BuzzfeedNews*, 28 August 2016.

⁸⁰⁵ Anthony Depalma, 'Nafta's Powerful Little Secret; Obscure Tribunals Settle Disputes, but Go Too Far, Critics Say', *The New York Times*, 11 March 2011.

⁸⁰⁶ Eberhardt and Olivet, *Profiting from injustice*, supra note 781, p. 11.

The report invokes eye-catching cases, such as *Philip Morris v. Australia/Uruguay* and *Vattenfall v. Germany* to argue that arbitrators 'tend to defend private investor rights above public interest, revealing an inherent pro-corporate bias', as tribunals 'have granted big business millions of dollars from taxpayers' pockets...in compensation for the alleged impact on company profits of democratically made laws that protect the environment, public health or social well-being'.⁸⁰⁷ One cause of this bias stems from the 'vested interests' of arbitrators and counselling law firms. The logic of this argument is that because investment arbitration is highly profitable, arbitrators are more likely to interpret vague treaty provisions in investor-friendly ways so as to facilitate growth in the number of claims. The report's conclusion is that governments should 'turn away' from investment arbitration because the suggested reforms are inadequate: 'the system will remain skewed in favour of big business and the highly lucrative arbitration industry'.⁸⁰⁸ As part of the conclusions, the report notes how 'the world has seen the enormous social costs of excessive corporate control over the financial system and of short-sighted deregulation of capital', which has led to an increase in 'calls for reregulation and corporate accountability'.⁸⁰⁹ These quotes testify how the investment treaty regime is seen as a symptom of the wider problem where governments are bending their knees to transnational economic forces so as to promote further trade and investment liberalization. As noted, the critique relies on individual cases to prove how arbitral tribunals downplay the public interest or how the mere threat of investment arbitration compels governments to refrain from adopting legitimate public interest measures. At this stage, it is useful to provide some examples of the kind of cases that animate the critique.

One case that is often invoked is *Occidental v. Ecuador*, which dealt with Ecuador's termination of a participation contract, the purpose of which was to allow the claimant investor to explore and exploit hydrocarbons in the Ecuadorian Amazon region.⁸¹⁰ The case was decided with a two to one majority, with the dissenting arbitrator voicing strong critique against the majority's reasoning on the calculation of damages.⁸¹¹ The tribunal

⁸⁰⁷ Ibid., p. 8 and 11.

⁸⁰⁸ Ibid., p. 9.

⁸⁰⁹ Ibid., p. 72.

⁸¹⁰ *Occidental Petroleum Corporation and Occidental Exploration and Production Company v. The Republic of Ecuador*, ICSID Case No. ARB/06/11, Award (hereinafter Occidental award), 5 October 2012.

⁸¹¹ Arbitrator Stern argued that she was 'in complete disagreement with the way damages have been calculated, which I consider to be resting on grossly incorrect legal bases.' See *Occidental Petroleum Corporation and Occidental Exploration and Production Company v. The Republic of Ecuador*, ICSID Case No. ARB/06/11, Dissenting Opinion of Brigitte Stern, 20 September 2012, para. 1.

awarded the claimant US\$ 1.77 billion in damages, but Ecuador filed a request for annulment, and in October 2015 the annulment committee annulled parts of the award 'on the ground of manifest excess of powers' and cut the compensation by some forty percent,⁸¹² with the Ecuadorian president vowing to continue negotiations to further decrease the payment. What is noteworthy is that the tribunal acknowledged that the claimant's actions preceding the contract's termination had breached both Ecuador's national law and the terms of the participation contract, but the tribunal held that the termination was a disproportionate act to the scale of the claimant's breach. Another much discussed case used to demonstrate the potentially sky-high cost of investment arbitration centers on Ronald Lauder, a US billionaire who brought parallel claims under the Dutch-Czech and US-Czech BITs for a string of regulatory decisions which had caused *CME*, the Dutch company he owned, to divest itself of a TV network. The two tribunals came to different conclusions on the question of damages, with the other tribunal awarding no damages and the other some USD\$270 million (plus ten percent in interest to be paid retroactively for a period of three years), although the causes of action and the claimants' arguments were the same.⁸¹³ The compensation equaled roughly the Czech Republic's health-care budget and 'adjusted for population size and gross national income, it was equivalent to an award of... \$131 billion against the United States'.⁸¹⁴ Soon after the Czech Republic had decided to pay the award in full, it was reported that Mr. Lauder had purchased a Gustav Klimt painting for USD\$135 million, 'at the time the highest sum ever paid for a painting'.⁸¹⁵ A third example relates to the at least dozen claims raised against Libya, most of which are pending and which relate to the deteriorating security situation in the aftermath of the collapse of the Gaddafi regime.⁸¹⁶ In one of the arbitrations, concluded in 2013, the tribunal awarded the Kuwaiti claimants around USD\$935 million in damages in relation to a resort complex the claimants had planned to build on the coast of Libya,⁸¹⁷ with Libya immediately challenging the award. It appears that before the claim was raised

⁸¹² *Occidental Petroleum Corporation and Occidental Exploration and Production Company v. The Republic of Ecuador*, ICSID Case No. ARB/06/11, Decision on Annulment of the Award, 2 November 2015, para. 590.

⁸¹³ See *Ronald S. Lauder v. The Czech Republic*, UNCITRAL, Award, 3 September 2001; *CME Czech Republic B.V. v. The Czech Republic*, UNCITRAL, Final Award, 14 March 2003.

⁸¹⁴ Gus Van Harten, *Investment Treaty Arbitration and Public Law* (Oxford University Press, 2008), p. 7.

⁸¹⁵ See Carol Vogel, 'Lauder Pays \$135 Million, a Record, for a Klimt Portrait', *New York Times*, 19 June 2006.

⁸¹⁶ See Luke Eric Peterson, 'Investigation: As fight continues over \$1 billion award, Libya facing at least a dozen investment treaty arbitrations - possibly more - in aftermath of Arab Spring', *IAR Reporter News*, 31 March 2017.

⁸¹⁷ *Mohamed Abdulmohsen Al-Kharafi & Sons Co. v. Libya*, Final Award, 22 March 2013.

the claimants had proposed that the dispute is settled if Libya agrees to pay USD\$5 million in compensation for the claimant's losses, but Libya declined the offer.⁸¹⁸ Over 90 percent of the compensation consisted of future and lost profits resulting from 'real and certain lost opportunities', as the English version of the award puts it,⁸¹⁹ and one can only wonder what those 'real and certain lost opportunities' were in light of Libya's chaotic political situation.

These cases, along many others, provide background material to the argument that BITs provide leverage and opportunities for large corporations and wealthy individuals to challenge a wide range of policy measures, which reflect public interest considerations or constitute a legitimate response to the claimant's action or relate to circumstances where the host state has drifted into a protracted political crisis or is in the middle of an armed conflict. *Occidental v. Ecuador* also juxtaposes the interests of a multinational corporation and a poor developing state, which carries strong echoes of colonialism and its many injustices. The examples also indicate that in the critics' eyes it is irrelevant to distinguish between investors in accordance with their 'size', as the regime grants additional privileges to the well-off of the global economy without imposing any obligations on them. That the world's Mr. Binders (referred to in Chapter 3) may suffer injustice at the hands of state authorities is a marginal concern because of the systemic impact that investment treaties and arbitration are understood to have on the distribution of wealth and power at the global level and on the relative weight of public and private interests in global economic governance. For every Mr. Binder, there is a Mr. Lauder, a billionaire who utilizes an investment treaty in a way that makes the human rights analogy seem ludicrous.

Although the above discussion is highly impressionistic, it is tempting to side with the critics. The chain of association that begins from cases such as *Occidental v. Ecuador* leads easily to bleak images dominated by growing inequality, environmental degradation, systemic tax evasion, rogue multinationals, the interests of the top one percent, and erosion of faith in the democratic political process and public institutions in general. The daily newsfeed provides ample support to a dystopian worldview where governments collude with big business to make myopic policy with little consideration given to the preservation of the global commons. If this is the imagery with which the investment treaty regime is associated, reform proposals targeting the procedural aspects of investment arbitration and

⁸¹⁸ Ibid., para. A.2 (of chapter five of the award).

⁸¹⁹ Ibid., p. 369 ff.

specification of protection standards will seem entirely inadequate. This also highlights how differently the two sides evaluate the implications of economic globalization. If the proponents argue that BITs contribute to global well-being, with globalization being an unstoppable and largely beneficial force, the critics argue the very opposite. This basic difference stems in part from the way in which the proponents externalize or marginalize the costs of economic globalization, whereas the critics' focus is solely on the costs. What is remarkable is the way in which both sides are at ease in making sweeping statements about the import of BITs and how such statements are accompanied by equally sweeping narratives about the global economy. But diagnosing the forces that drive and benefit from economic globalization, and their potential antidotes, is an immensely complex task. The political and legal arrangements that support the functioning of the global economy are highly complex, as are the various technologies that constitute its lifeline and drive its evolution forward. Given this, it is tempting to focus on individual cases and default arguments about the normative and distributive outcomes that the investment treaty regime is understood as producing. I will return to this issue below.

Generally speaking, as important as individual cases are for an analysis of the regime's costs and benefits, they are a problematic reference point for a number of reasons. First, if individual case outcomes are used to argue for or against the investment treaty regime, choosing the sample cases will shape (if not determine) the conclusions reached. Second, at the time of writing, 528 arbitrations have been concluded, out of which 36.6 percent were decided in favor of host states and 26.9 percent in favor of claimant investors, with 23.5 percent settled and 10.6 percent discontinued.⁸²⁰ One could suggest that these figures undermine the critics' basic arguments, but this is hardly the case. It may well be that many of the cases that states won were based on frivolous claims that would have been dismissed immediately before domestic courts. On the other hand, in cases decided in favor of the claimant, the tribunal's reasoning may be based on a 'series of errors and defects', with the tribunal applying the law 'cryptically and defectively', or the tribunal's calculation of damages could rest on 'grossly incorrect legal bases'.⁸²¹ These quotes are from the decision of an ICSID annulment committee and a dissenting opinion related to an ICSID arbitration, but only the latter 'misapplication' was rectified (partly) at the annulment stage. Clearly,

⁸²⁰ See at <http://investmentpolicyhub.unctad.org/ISDS> (accessed 25 August 2017).

⁸²¹ *CMS Gas Transmission Company v. The Republic of Argentina*, ICSID Case No. ARB/01/8, Decision of the ad hoc Committee on the Application for Annulment of the Argentine Republic, 25 September 2007, paras. 136 and 158; *Occidental v. Ecuador*, Dissenting Opinion, supra note 811, para. 1.

the above statistics cannot be used as a yardstick to measure the regime's gravitation toward one way or the other. At best, the figures provide impressionistic evidence about the legitimacy of the regime and should thus be met with caution. Moreover, a focus on case outcomes ignores the way in which tribunals have reached their conclusions as well as the underlying factual record, both of which are central components in case law analysis.

Although case outcomes provide a less than convincing analytic base for evaluating the regime, I will nonetheless analyze two decisions that both the critics and proponents have invoked when making their respective cases. This should, again, allow a better understanding of the different views that the two sides have about the purposes and implications of the regime, as well as how these views affect the way in which they read individual awards (and statistics on case outcomes).

7.2. Political Opposition in *Tecmed* and *Occidental*: Bad Economics, Populism or Legitimate Concerns?

7.2.1. *Tecmed*

In their study on how arbitral tribunals take account of the politics of investment disputes, Cotula and Schröder note how there are

'tensions between the mindsets and approaches of lawyers on arbitral tribunals and the real world of community relations. In the latter, the politics are often complex and solutions can require interventions to address technical issues and promote public participation in contested terrains. Capacity constraints may be at play, and the officials delivering these interventions may not be familiar with legal concepts and language. This could increase the risk that public action to address community issues may expose states to successful arbitration claims... For investments that require approval from, and ongoing relations with, multiple government agencies at local and national levels, consistency in public action can prove difficult to achieve. This is particularly so in low- and middle-income countries where capacity challenges may be more acute. Public authorities may not be equipped to tackle technically complex and politically

sensitive community dimensions in ways that would not expose them to arbitration claims.⁸²²

Such sensitive community dimensions were part and parcel of the *Tecmed* and *Occidental* arbitrations. In *Tecmed*, a Spanish company had purchased a hazardous waste landfill situated thirteen kilometers from Hermosillo, the capital of the state of Sonora.⁸²³ The claimant had bought the landfill through public auction in 1996. In March 1997, reports started to circulate how a truck driver, hired to transport waste from California to the landfill, had developed a burn in his leg after coming in contact with contaminated soil headed for the site. Local residents investigated the facility and found 'a dump of toxic waste lying exposed to the open air' which contained lead, cadmium, cyanide and other waste materials.⁸²⁴ As a result, they made complaints to local authorities, with the main concern being that the 'wastes were uncontained and exposed to the elements', which 'posed threats to the environment, to the health and welfare of residents, and jeopardized the underground water supply'.⁸²⁵ An almost two-year campaign ensued during which the local residents used a variety of tactics to exert pressure on local and federal authorities, and in November 1998 a federal agency, the National Ecology Institute of Mexico (INE), rejected the claimant's application for renewal of the landfill's operating permit and ordered its closure without providing compensation.

The investor raised a claim under the Spain-Mexico BIT and argued that the permit's cancellation constituted an expropriation for which no compensation was paid as well as a breach of the fair and equitable treatment standard. Without the permit, the company was unable to operate the landfill 'in accordance with its sole intended purpose'. The claimant argued that 'political circumstances... rather than... legal considerations' motivated the decision not to renew the permit, with local authorities 'encouraging' the grassroots opposition, which in turn influenced the INE decision.⁸²⁶ As to the alleged environmental and public health threats, the claimant noted that another federal agency (PROFEPA) had investigated the site to assess whether its operation complied with the relevant

⁸²² Lorenzo Cotula and Mika Schröder, *Community Perspectives in Investor-State Arbitration* (International Institute for Environment and Development, 2017), pages 3 and 28.

⁸²³ *Tecmed* award, supra note 689.

⁸²⁴ Anna Ochoa O'Leary, 'Of Information Highways and Toxic Byways: Women and Environmental Protest in a Northern Mexican City', *MASRC Working Paper Series 30* (University of Arizona, 2002), p. 1.

⁸²⁵ *Tecmed* award, supra note 689, para. 96.

⁸²⁶ *Ibid.*, paras. 42-43.

requirements, and while 'certain breaches' were identified, these did not 'endanger the environment or the health of the population', as the federal agency had only issued fines against the company and noted that 'the infringements committed...are not sufficient to immediately cancel, suspend or revoke the permit for carrying out hazardous material and/or waste management activities, nor do they have an impact on public health or generate an ecological imbalance' - this implied that the landfill's forced closure was a disproportionate act.⁸²⁷ Mexico's counsel noted that INE was acting within its statutory powers when ordering the landfill's closure, and that INE alone is authorized to renew an expired permit on conditions provided under federal law. Hence, that the other agency (PROFEPA) had only imposed fines on the claimant was materially irrelevant. Mexico also referred to the 'negative attitude of the community towards the landfill due to its location and to the negative and highly critical view taken by the community' on the transportation of hazardous toxic waste from other locations, which highlighted 'the importance of demanding strict compliance with the new operating permit granted by INE...on November 19, 1997'.⁸²⁸ More generally, Mexico argued that the refusal to renew the permit 'was a regulatory measure issued in compliance with the State's police power within the highly regulated and extremely sensitive framework of environmental protection and public health'.⁸²⁹

The tribunal referred to the maxim that a state may not invoke provisions of its domestic law to justify a breach of its treaty obligations, but also recognized that a state's 'exercise of its sovereign powers within the framework of its police power may cause economic damage to those subject to its powers as administrator without entitling them to any compensation whatsoever is undisputable'.⁸³⁰ Similarly, regulatory measures that purport to benefit a local community or the society as a whole - such as the INE decision - have to be assessed in light of the consequences they have on the claimant's investment. In other words, the stated purpose of a measure alone cannot determine whether it is compatible with the BIT. Likewise, it was necessary to assess whether the INE decision was 'proportional to the public interest protected...and to the protection legally granted to

⁸²⁷ Ibid., paras. 43 and 100. The refusal to renew the permit was justified on four grounds, which related to the storing or receiving of unauthorized substances at the landfill, but the claimant referred e.g. to the statement quoted as well as to the fact that it had reported to INE of some of the four grounds without the latter making no 'objection or reservation'. See paras. 100-102.

⁸²⁸ Ibid., paras. 49-50.

⁸²⁹ Ibid., para. 97.

⁸³⁰ Ibid., paras. 119-120.

investments, taking into account that the significance of such impact has a key role upon deciding the proportionality'.⁸³¹ The tribunal understood that the breaches for which the claimant was previously fined also constituted the ground for the INE decision, as the same breaches, by and large, were referred to as reasons for the decision. When imposing the fines, PROFEPA had noted that 'the inspections conducted by this Office to the landfill...have not shown any indication that risks for the population's health or the environment might exist'.⁸³² Similarly, the INE decision's text provided no support to the argument that the claimant's breaches had threatened public health or impaired 'ecological balance'.⁸³³ Other statements made by Mexican authorities supported this view. For example, Mexico's environmental ministry had noted just two months before the INE decision that the claimant 'handles hazardous waste in strict compliance with the law, that the last stage of the landfill has the maximum safety conditions required, which provide the necessary grounds to authorize the relevant operations'.⁸³⁴

For the tribunal, a central reason for the community opposition stemmed from a Mexican law requiring that landfills are located at least twenty-five kilometers from residential areas. However, as this law had entered into force after the claimant had obtained and started to operate the landfill, the law could not be applied retroactively to the claimant's site. But the community opposition had led the claimant to agree on relocating the landfill's operations (mostly at its own cost) to another site which would comply with the twenty-five-kilometer rule. In June 1998, during the negotiations concerning the relocation, the federal, state and local authorities issued a joint statement which provided that while the investigations at the landfill had not provided 'evidence of any risk to health and the ecosystems', the relocation was necessary to 'secure environmental safety in view of the rapid urban growth of Hermosillo, provide a response to the concerns that had been expressed and guarantee, in the long term, the environmental infrastructure to handle and dispose of industrial waste'.⁸³⁵ The view that the landfill's location was the main source of concern among the opposition movement was supported by a number of additional statements made by Mexican authorities. During the proceedings Mexico's counsel argued that the 'problem was not a problem with a company or with an investor, but with a

⁸³¹ Ibid., para. 122.

⁸³² Ibid., para. 124.

⁸³³ Idem.

⁸³⁴ Idem.

⁸³⁵ Ibid., para. 110.

specific site'.⁸³⁶ Similarly, the head of INE noted that the landfill's unresolved relocation was one of the reasons for denying the renewal of the permit, with the relocation being closely related to the socially and politically 'tense circumstances surrounding' the landfill's operation.⁸³⁷ This led to the conclusion that although the INE decision made no reference to the local opposition, it 'was [nonetheless] mainly driven by [such] socio-political factors'.⁸³⁸

The tribunal then addressed the question whether these socio-political factors amounted to a 'serious emergency situation, social crisis or public unrest'. The gravity of such factors was relevant to the tribunal's analysis of whether the INE decision was a proportionate measure.⁸³⁹ The tribunal noted that the grassroots opposition against the landfill had begun almost three years before the INE decision, but none of the complaints made by local groups had led to the cancellation of the claimant's permit. As noted, in the tribunal's view, the local opposition was 'mainly based...on the site's proximity to Hermosillo's urban center and on the circumstance...that the landfill's location' breached the twenty-five kilometer rule.⁸⁴⁰ As to the intensity of the community opposition, the tribunal characterized it as not being 'massive' in any way and as not going 'further than the positions assumed by some individuals or the members of some groups' opposing the landfill.⁸⁴¹ The public protests against the landfill 'could gather on two occasions a crowd of only two hundred people the first time and of four hundred people the second time out of a community with a population of almost one million inhabitants'.⁸⁴² This meant that the local opposition did 'not constitute a real crisis or disaster of great proportions, triggered by acts or omissions committed by the foreign investor or its affiliates'.⁸⁴³ In sum, the tribunal understood that the real problem was the location of the landfill and not the manner in which the claimant was operating it, which was 'confirmed by the fact that the Mexican federal, state and municipal authorities, including INE, did not hesitate to entrust' the claimant 'with the construction and operation of a new hazardous waste landfill located

⁸³⁶ Ibid., paras. 125-126.

⁸³⁷ Ibid., para. 131.

⁸³⁸ Ibid., paras. 129-130.

⁸³⁹ Ibid., para. 133.

⁸⁴⁰ Ibid., paras. 140-141.

⁸⁴¹ Ibid., para. 144.

⁸⁴² Idem.

⁸⁴³ Idem.

outside Hermosillo, with characteristics, activities and a scope apparently wider and more ambitious than the operation' at the contested site.⁸⁴⁴

In the end, the tribunal held that the INE decision amounted to an expropriation and also violated the Mexico-Spain BIT's FET standard, with Mexico ordered to pay around 5.5 million dollars plus interest in damages to the claimant. The critics of investment arbitration have not been impressed with the tribunal's reasoning. Schneiderman reads the award as indicating that the tribunal separated the public health concerns from the 'socio-political motivations' behind the INE decision, which allowed it to 'shield itself from accusations that it had thwarted legitimate environmental or public-health regulation [i.e. the INE decision]'.⁸⁴⁵ This argument assumes that the refusal to renew the permit was based on public health concerns instead of the political opposition, and while the factual record in *Tecmed* is less than straightforward, Schneiderman takes no issue with the tribunal's reading of the facts. Odumosu, in turn, sees that the tribunal's decision implies that even if government action 'is beneficial to the society as a whole', it is not excluded from the scope of a BIT if it has 'negative economic impacts on the financial position of the investor'.⁸⁴⁶ In his view, the tribunal paid lip service to the public interest by analyzing the intensity of the local opposition, but ultimately 'downplayed the significance of peoples' voices... foregrounded the political nature of the protests, and interpreted... [the INE decision] as a response to political circumstances', rather than seeing it as a legitimate public health measure.⁸⁴⁷ Framing the dispute as only pitting the community interest against the investor's economic interest already implies that the tribunal got it wrong, and assumes either that the INE decision *was* motivated by overriding public health considerations instead of political pressure and that the tribunal should have in any case deferred to the political opposition. However, while *Tecmed's* factual record is open to interpretation, it is clear that the tribunal was acting within its jurisdiction when characterizing the opposition as marginal and as being based on fears and hearsay rather than on legitimate public health concerns. In this light, I understand the criticisms to stem more from the ability of the tribunal to second-guess the motives of Mexican authorities, and less from the quality of its reasoning. That domestic policy-making is prone to respond

⁸⁴⁴ Ibid., para. 145.

⁸⁴⁵ David Schneiderman, 'Investing in Democracy? Political Process and International Investment Law', 60 *University of Toronto Law Journal* (2010), pp. 909-940, at 917.

⁸⁴⁶ Ibiwonke T. Odumosu, 'The Law and Politics of Engaging Resistance in Investment Dispute Settlement', 26 *Penn State International Law Review* (2007), pp. 251-287, at 278.

⁸⁴⁷ Ibid., p. 279.

to 'populist' concerns on occasion is to be expected, and arbitral tribunals will necessarily approach such concerns differently than domestic institutions.

A number of commentators have also taken issue with the *Tecmed* tribunal's dictum on the FET standard. In the official English translation (translated from Spanish), the relevant part of the award held that the standard,

'requires the Contracting Parties to provide to international investments treatment that does not affect the basic expectations that were taken into account by the foreign investor to make the investment. The foreign investor expects the host State to act in a consistent manner, free from ambiguity and totally transparently in its relations with the foreign investor, so that it may know beforehand any and all rules and regulations that will govern its investments, as well as the goals of the relevant policies and administrative practices or directives, to be able to plan its investment and comply with such regulations. Any and all State actions conforming to such criteria should relate not only to the guidelines, directives or requirements issued, or the resolutions approved thereunder, but also to the goals underlying such regulations.'⁸⁴⁸

Roberts refers to this passage to make the argument that when 'defining the requirements for certain standards, such as fair and equitable treatment, some tribunals have adopted idealized standards of perfect governmental conduct and regulation divorced from any real consideration of state practice'.⁸⁴⁹ Similarly, Douglas notes that the '*Tecmed* "standard" is actually not a standard at all; it is rather a description of perfect public regulation in a perfect world, to which all states should aspire but very few (if any) will ever attain'.⁸⁵⁰ These readings carry two problems. First, it is easy to refer to individual paragraphs of awards to make arguments about interpretative overreach, although the tribunals' reasoning in other paragraphs may qualify those interpretations, and although the tribunals' findings on the merits are not necessarily based on such 'idealized standards'. When reading the *Tecmed* tribunal's analysis of whether Mexico had also breached the FET standard, for example, it becomes clear that the tribunal was not applying such fantasy standard, but

⁸⁴⁸ *Tecmed* award, supra note 689, para. 154.

⁸⁴⁹ Roberts, 'Power and Persuasion', supra note 786, p. 223.

⁸⁵⁰ Zachary Douglas, 'Nothing if Not Critical for Investment Treaty Arbitration: Occidental, Eureko and Methanex', 22 *Arbitration International* (2006), pp. 27-52, at 28.

assessed Mexico's actions on the basis of its construction of the factual record as outlined above. The *Tecmed* award was first written in Spanish and only later translated into English. However, as Kessler notes, the above English translation 'is actually a very poor - even grossly distorted - translation of the original Spanish version'.⁸⁵¹ The demands of 'total transparency' and 'free of ambiguity', for example, were inventions of the translator and it is somewhat embarrassing that the incorrect translation has been used as an example of interpretative overreach by arbitral tribunals.

In sum, one can disagree with the tribunal's framing of the factual record as well as with its approach on the nature of the local opposition and the implications this had on the outcome. But it is difficult to agree with the contention that the INE decision was motivated by overriding public health concerns, given the repeated statements to the contrary. One can also question the economic and environmental wisdom of the INE decision. As the *Tecmed* award notes, Mexico was in urgent need of hazardous waste services,⁸⁵² and, apparently, the claimant operated a much larger landfill in another location. One can also argue over the amount of compensation the investor received, but the general principle that measures tantamount to expropriation should be compensated is difficult to dispute. Host state reactions to domestic political pressure will of course vary from one case to the next, and analyzing the question whether tribunals should defer to such pressure when assessing a state's attendant policy measure should depend on the factual record rather than on a principled position, unless the point is to make an argument against the idea of investment arbitration. Brower and Blanchard note that the refusal to renew the claimant's permit 'was refused on a pre-textual basis discordant with Mexican administrative law and without due process'.⁸⁵³ This sounds somewhat categorical, but its tone is similar to the above criticisms of the award, with both sides providing one-sided representations of the political sensitivities.

⁸⁵¹ Kessler, 'An Arbitrator's Perspective', supra note 723, p. 300. The Spanish version of the quoted passage reads as follows: 'El Tribunal Arbitral considera que esta disposición del Acuerdo, a la luz de los imperativos de buena fé requeridos por el derecho internacional, exige de las Partes Contratantes del Acuerdo brindar un tratamiento a la inversión extranjera que no desvirtúe las expectativas básicas en razón de las cuales el inversor extranjero decidió realizar su inversión. Como parte de tales expectativas, aquél cuenta con que el Estado receptor de la inversión se conducirá de manera coherente, desprovista de ambigüedades y transparente en sus relaciones con el inversor extranjero, de manera que éste pueda conocer de manera anticipada, para planificar sus actividades y ajustar su conducta, no sólo las normas o reglamentaciones que regirán tales actividades, sino también las políticas perseguidas por tal normativa y las prácticas o directivas administrativas que les son relevantes.'

⁸⁵² *Tecmed* award, supra note 689, para. 147.

⁸⁵³ Brower and Blanchard, 'The Truth about Investor-State Arbitration', supra note 19, pp. 739-740.

The critics strive to point out how arbitral tribunals place too much emphasis on investor interests, as if an objective standard exists against which tribunals should carry out the balancing act. This suggests, again, that they should openly acknowledge that the real problem is the ability of arbitral tribunals to review policy measures in the first place, rather than how such review is carried out in individual cases. The purpose of investment protection rules is *investment protection* and no amount of treaty reform can compel arbitral tribunals to defer to domestic policy in a way that would appease the critics. This is of course what the proponents are arguing - that the idea of investment arbitration is to provide a neutral analysis of the factual record in light of international protection standards that pay due consideration to the interests of foreign investors. Again, this is a political disagreement about the propriety of investment treaties and arbitration, rather than a technical disagreement about the proper balance of private and public interests in individual investment disputes.

To return to *Tecmed*, one can empathize with the position of the INE staff. Caught between grassroots opposition and the claimant's request for new site, the INE decision strove to speed up the relocation and attenuate the local opposition, but the award suggests that, for some reason, the relocation had not moved forward in the following 15 months.⁸⁵⁴ The claim was raised in July 2000, which implies that the Mexican federal and local authorities had probably no knowledge about the Mexico-Spain BIT, let alone about its potential fiscal implications, as the first investment claim against Mexico was raised only in 1997. Generally speaking, the proponents could use *Tecmed* as an example of how investment arbitration provides incentives for host states to improve their decision-making processes as well as to give due consideration to the interests of foreign investors vis-à-vis the interests of domestic interest groups. For the critics, *Tecmed* demonstrates how arbitral tribunals are prone to downplay the wisdom of the relevant public interest, as they focus on the economic impact of the challenged measure. *Tecmed* could also be invoked to point out how an unsuspecting developing country is disciplined for a decision that could just as well have been taken by an agency in a developed country. After all, bureaucracies overseeing projects that involve sensitive public health and environmental concerns often have to take decisions that go against the interests of some stakeholders and that are based on contested evidence. I will return to this idea in the following pages.

⁸⁵⁴ *Tecmed* award, supra note 689, para. 143.

7.2.2. *Occidental*

The *Occidental v. Ecuador* award was already discussed shortly above. The monumental compensation that the tribunal awarded has diverted attention away from the dispute's factual record and the tribunal's reasoning. The award extends to over three hundred pages and the dissenting arbitrator described the case as being 'a very complex case to which the three members of the tribunal have been extremely devoted during many years'.⁸⁵⁵ Clearly, understanding these complexities would appear to be central to appreciating the tribunal's conclusions as well as the dissenting arbitrator's concerns with the majority's calculation of damages. These complexities also suggest that focusing only on one aspect of the award is bound to create an incomplete picture and may distort the conclusions reached. To give an example, Sornarajah criticizes the *Occidental v. Ecuador* award on the ground that the tribunal used a proportionality test to determine whether the challenged action breached the FET standard. He argues that there was 'no justification in the text of' the relevant BIT 'to use such a test', neither were there grounds to hold that proportionality 'constitutes a general principle of law', and the 'proportionality test calls for the making of highly subjective value judgments', which is one of the reasons why its use is limited in many 'European systems'.⁸⁵⁶ While these points may have some general merit, Sornarajah takes no issue with the factual record of *Occidental v. Ecuador* nor appears to recognize that the disputing parties had agreed that the principle of proportionality is part of the applicable law.

When reading the award, it seems plausible to assume that Ecuador's termination of the participation contract, which the claimant challenged, was at least partly motivated by another arbitration (concerning value added tax refunds) where Ecuador was ordered to pay roughly \$US 70 million in compensation to *Occidental*.⁸⁵⁷ As the tribunal put it, the 'VAT award had created anger and disappointment in Ecuadorian political circles'.⁸⁵⁸ The liberalization of Ecuador's oil sector had been a contentious affair from the scratch. 'Anti-neo-liberal activists' had contributed to the removal from office of two governments by 2005 and *Occidental's* operations had been criticized repeatedly by indigenous and

⁸⁵⁵ *Occidental v. Ecuador*, Dissenting Opinion, supra note 811, para. 1.

⁸⁵⁶ Sornarajah, *Resistance and Change*, supra note 23, pp. 377-378, 380-381.

⁸⁵⁷ See *Occidental Exploration and Production Company v. The Republic of Ecuador*, LCIA Case No. UN3467, Award, 1 July 2004.

⁸⁵⁸ *Occidental* award, supra note 810, para. 442.

environmental groups.⁸⁵⁹ These political divisions between indigenous peoples and Ecuador's economic and political elite reflect broader conflicts plaguing the Ecuadorian society, which one commentator described as being 'characterized by deep racism, widespread poverty, extreme inequality, and discrimination against indigenous peoples and the poor', alongside 'pervasive corruption and a discredited judiciary and political class'.⁸⁶⁰

In case of Occidental, the indigenous and environmental groups were demanding 'a larger share in the benefits [of oil production] and the adoption of more sustainable environmental practices'.⁸⁶¹ As a result of the protests, members of Ecuador's congress called for the impeachment of the Minister of Energy and Mines unless he terminates the contract. Soon after Ecuador acted accordingly and justified the termination on the ground that the claimant had failed to seek prior approval for a transfer of certain rights to another company that had operations in Ecuador. Quite interestingly, however, during the proceedings Ecuador's former Minister of Energy and Mines argued that the transfer was 'a good idea since it was beneficial to the country',⁸⁶² and the company to which the rights were transferred was an 'approved operator in Ecuador', which 'continued to receive further approvals in relation to other projects/fields' after signing the contested agreement with Occidental.⁸⁶³ The broader political context of Occidental's operations in Ecuador is not discussed in the tribunal's award. As noted, the track record of crude oil production in Ecuador is rather depressing, with Texaco's early operations in the 1970s embodying the destruction that oil production can bring in the absence of regulatory oversight.⁸⁶⁴ As to Occidental, writing in 2001, Kimerling noted that 'despite a clear trend on paper towards increasingly detailed - albeit incomplete - environmental requirements, implementation, oversight and compliance remain poor', and 'Occidental has negotiated a legal framework with the government that, for the most part, seems designed to perpetuate and even legalize the exclusive reliance on corporate environmental self-regulation'.⁸⁶⁵ The *Occidental* award

⁸⁵⁹ Julia Kalvert, 'Civil Society and Investor-state Dispute Settlement: Assessing the Social Dimensions of Investment Disputes in Latin America', 22 *New Political Economy* (2017), pp. 1-20, at 7.

⁸⁶⁰ Judith Kimerling, 'International Standards in Ecuador's Amazon Oil Fields: The Privatization of Environmental Law', 26 *Columbia Journal of Environmental Law* (2001), pp. 289-397, at 304-306. A more general account is found in John Martz, *Politics and Petroleum in Ecuador* (Routledge, 1987).

⁸⁶¹ Kalvert, 'Civil Society and Investor-state Dispute Settlement', supra note 859, at 9.

⁸⁶² *Occidental* award, supra note 810, para. 444.

⁸⁶³ *Ibid.*, para. 445.

⁸⁶⁴ The relevant events are found in *Chevron and Texaco v. Ecuador*, PCA Case No. 2009-23, Third Interim Award on Jurisdiction and Admissibility, 27 February 2012.

⁸⁶⁵ Kimerling, 'International Standards in Ecuador', supra note 860, pp. 313 and 392.

contains a single generic reference to 'protection of the environment' in the context where the tribunal is listing the claimant's obligations under the participation contract.⁸⁶⁶

Sornarajah's discussion of the *Occidental* award is limited to the proportionality principle. He argues that the tribunal 'was hunting fruitlessly for a peg on which to hang the proportionality rule, which it had decided to use',⁸⁶⁷ but, as noted, both Ecuador and Occidental had agreed that the rule is part of the applicable law, with Ecuador arguing that the termination satisfied the applicable test.⁸⁶⁸ One can of course disagree with the tribunal's interpretation and application of the principle, and even more so with the sky-high compensation, but what makes the award interesting (or problematic) is the exclusion of the political context, apart from few incidental references. In one way, the tribunal's reasoning is representative of the argument that tribunals set an international benchmark for what is reasonably acceptable government conduct in a market economy. The tribunal could not take a stand on the environmental concerns associated with Occidental's operations, because Ecuador did not raise them. Had those concerns been raised, it is doubtful if they would have influenced the tribunal's analysis. The case centered on the question whether the termination of the participation contract breached the US-Ecuador BIT, and the broader societal implications of oil production are by and large extraneous to answering such question. That 'pervasive corruption' plagues Ecuador, with successive governments being disinterested or incapacitated to exercise any effective regulatory oversight in respect of ongoing oil operations, is clearly not a problem that arbitral tribunals can address. It is also noteworthy that although Ecuador denounced the ICSID Convention and terminated a number of investment treaties, the US-Ecuador BIT remains in force. An Ecuadorian state official reasoned that 'the BIT is a necessary legal intervention that helps to attract and retain foreign capital despite the risk of future investor claims'.⁸⁶⁹

Another observation is that Article 47 of the ICSID Convention allows the respondent state to raise a counterclaim 'arising directly out of the subject-matter of the dispute'. Ecuador

⁸⁶⁶ *Occidental* award, supra note 810, para. 116 (simply noting that the claimant 'had various other obligations under the Participation Contract, including payment of all Ecuadorian taxes and duties; periodic reporting of certain information to Ecuador; the establishment of good relations with the community; and the protection of the environment').

⁸⁶⁷ Sornarajah, *Resistance and Change*, supra note 23, p. 378.

⁸⁶⁸ *Occidental* award, supra note 810, para. 425.

⁸⁶⁹ Kalvert, 'Civil Society and Investor-state Dispute Settlement', supra note 859, p. 10 (based on an interview with a member of Ecuador's National Assembly in October 2014).

has raised counterclaims in two other cases on the ground of environmental harm caused by the claimant,⁸⁷⁰ but did not do so in *Occidental* as its defense focused solely on the legality of the termination of the participation contract. It is easy to criticize the *Occidental* tribunal for excessively disciplining Ecuador, but such critique misunderstands the tribunal's mandate in the circumstances of the case, and one can again ask whether electoral pressure alone can ever constitute a rational and legitimate policy motive in the eyes of arbitral tribunals. As noted, Ecuadorian activist groups 'did not object to oil exploitation' as such, but sought to receive some of the attendant benefits and compel the government to enforce more efficiently the relevant environmental laws and regulations.⁸⁷¹ Ecuador's crude oil production fluctuates, but is on a much higher level than in the early 2000s.⁸⁷² The left-wing party that seized power in 2007 in the wake of widespread protests quickly increased social welfare spending which appears to have reduced Ecuador's poverty rates, even considerably.⁸⁷³ Since global oil prices have remained at a much lower level in the past few years, it remains to be seen whether or not the incumbent president, Lenín Moreno, is able to continue the 'socialist revolution' of the past decade. For those on the political left, *Occidental* may represent a form of neocolonialism whose only upside was the rising into power of a leftist government. However, without downplaying the environmental harm that Occidental's operations caused in Ecuador, the arbitration could be framed in another way.

Large-scale projects in the extractive industries sector create different type of social costs in developed countries as well. A good example is provided by the *Talvivaara* mining-project in Finland. In 2012, the mine's waste reservoirs leaked into the environment, which acidified the neighboring lakes and led to a rise in toxic metal levels. The capacity of the reservoirs was inadequate to cope with the volume of waste water which led to additional releases of contaminated water. The mining company recovered nickel through a method known as bioleaching, which had previously been used to recover other metals from ores. Many of the environmental problems stemmed from the unforeseen consequences of bioleaching which were not considered at the time the company received the permit to start

⁸⁷⁰ These are *Burlington Resources Inc. v. Republic of Ecuador*, ICSID Case No. ARB/08/5, Decision on Ecuador's Counterclaims, 7 February 2016; *Perenco Ecuador Ltd v Republic of Ecuador*, ICSID Case No. ARB/08/6, Interim Decision on the Environmental Counterclaim, 11 August 2015.

⁸⁷¹ Kalvert, 'Civil Society and Investor-state Dispute Settlement', supra note 859, p. 9.

⁸⁷² See at <https://tradingeconomics.com/ecuador/crude-oil-production> (accessed 23 August 2017).

⁸⁷³ See Mark Weisbrot, Jake Johnston and Lara Merling, *Decade of Reform: Ecuador's Macroeconomic Policies, Institutional Changes and Results* (Center for Economic and Policy Research, 2017).

operating the mine. The *Talvivaara* company went bankrupt in 2014 (also because of world market prices), with some 80 000 minority shareholders losing their investment. There were some reports that the minority shareholders planned to bring claims against the Finnish government on the ground that the bankruptcy was caused by the decisions of Finnish authorities, with one reporter hinting that some foreign shareholders were contemplating of bringing a claim under the Energy Charter Treaty. The Finnish Government became the majority shareholder of the company that continued operating the mine, and at the end of 2016 it was estimated that the government had spent around €700 million at various stages to support the continuation of the mine's operations, although they continue to adversely affect the ecological balance of the adjacent environment. The point of this story is that large-scale investment projects come with various types of risks, and if such risks materialize, the question is who bears responsibility for the costs. Whether *Talvivaara* has brought any benefits to the Finnish economy is an open question, but the general population in Finland is largely disinterested in the attendant economic and environmental costs, although the mine's operation continues to cause direct harm to local residents and the environment.

In this light, *Occidental* should not be described simplistically as juxtaposing the interests of a poor developing country and a US oil giant. Rather, it is a standard example of the various costs that economic development brings about the world over. It is also reflective of how the functioning of the global economy depends on large-scale resource extraction and of the burden it places on the environment. Ecuador's termination of the participation contract was, arguably, a symbolic move which created the impression that the government was defending the sovereignty and self-determination of its 'people'. The generous social welfare programs that followed the change of government also testify that crude oil production in the Ecuadorian Amazon region has brought tangible benefits to large segments of Ecuador's population, whatever its environmental and social costs may be. This is the paradox at the heart of the critique of the investment treaty regime. Crude oil production continues in Ecuador, with a large number of foreign companies having operations therein, but whether the government exercises any oversight of the operations is a question that is of no concern to those discussing the (lack of) legitimacy of the investment treaty regime. Seizing the moral high ground by referring to cases such as *Occidental* is tempting, but such move may strike as inconsequential and hypocritical. Inconsequential because Ecuador's leftist government has already reformed the country's

investment policy without protesters demanding that the US-Ecuador BIT is also terminated, and hypocritical because the way in which the costs and benefits of Ecuador's crude oil production are allocated will not depend on policy debates concerning the investment treaty regime but on the energies and resources of the indigenous and environmental groups living and operating in Ecuador. The critics could argue that Ecuador's termination of a number of BITs has provided policy space for its government to regulate and oversee oil production, but it is entirely unclear whether the government does so. It is also problematic to assume that investment treaties would have prevented Ecuador from exercising effective oversight previously. Investment treaties do not prevent the adoption and enforcement of environmental laws whose purpose is to contain or prevent the harm that large-scale resource extraction brings about. The proponents, in turn, could argue that *Occidental* supports the broad argument that arbitral tribunals provide a neutral venue for the resolution of investment disputes where the populist pressures that governments face are not allowed to replace a rational, fact-based analysis of the underlying events.

7.3. Sornarajah's Account

At this juncture, it is useful to remember that arbitration clauses became a standard part of BITs from the middle of the 1980s onward. Alvarez has argued that the 1984 United States model BIT was central to the later investment arbitration boom as its core provisions were included in most BITs concluded in the following twenty years. These included a broad definition of what constitutes an investment; the umbrella clause; guarantees of most-favored nation, national, and fair and equitable treatment; a further injunction against arbitrary and discriminatory measures; a right to 'prompt, adequate, and effective' compensation in the event of direct and indirect expropriation; and, finally, the United States model treaty included an arbitration clause, although its text remained somewhat vague in comparison to later clauses. According to Alvarez, the US model treaty 'revolutionized' the field and was 'instrumental in enabling the wave of investor-state arbitral disputes many years later'.⁸⁷⁴ Before the first investor-state claim was raised in

⁸⁷⁴ Jose E. Alvarez, 'The Once and Future Foreign Investment Regime', in Mahnoush H. Arsanjani, Jacob Katz Cogan, Robert D. Sloane and Siegfried Wiessner (eds.), *Looking to the Future: Essays on International Law in Honor of W. Michael Reisman* (Martinus Nijhoff Publishers, 2011), pp. 607-648, at 616. The text of the 1984 US Model BIT is available at http://www.law.nyu.edu/sites/default/files/ECM_PRO_066871.pdf (accessed 12 May 2017).

1987, it was entirely unclear how the core BIT provisions should be interpreted. To give an example, one question was whether the arbitration clause, as such, should be understood as constituting the host state's standing expression of consent to submit disputes to arbitration, or whether the host state should give its consent to arbitration each time an investor invokes a BIT's arbitration clause. A basic principle of arbitration is that tribunals receive their jurisdiction from the consent of the disputing parties, but it was uncertain how this principle should be interpreted in the context of BITs. In the very first investment arbitration award, rendered in 1990 under the ICSID Convention, the tribunal held that the UK-Sri Lanka BIT's arbitration clause constituted a standing offer for investors to bring claims against the host state, with no additional expression of consent required from the latter. Sri Lanka did not raise the issue at the proceedings, and the *AAPL v. Sri Lanka* tribunal's approach has transformed into an uncontested dictum, although in 1990 'this [approach] was far from evident and remained unprecedented'.⁸⁷⁵ Lowenfeld, who was closely involved in the drafting of the ICSID Convention, notes that 'the possibility that a host state in a bilateral treaty could give its consent to arbitrate with investors from the other state without reference to a particular investment agreement or dispute' was not even addressed during the drafting process.⁸⁷⁶

Sornarajah argues that *AAPL v. Sri Lanka* constituted the 'original sin' of investment arbitration, which paved the way for later expansions 'of the bases of jurisdiction' that go 'well beyond what was originally intended by the parties to investment treaties'.⁸⁷⁷ In Sornarajah's account, the central cases in this respect have been *Maffezini* where the scope of the most-favored-nation obligation was extended to cover arbitration clauses in the host state's other BITs,⁸⁷⁸ *Tokios Tokelés* where Ukrainian nationals were considered as Lithuanian investors for the purposes of the Ukraine-Lithuania BIT,⁸⁷⁹ and *Abaclat v. Argentina*, the 'acme of aberrations' in Sornarajah's view, where the acquisition of Argentina's junk bonds through a foreign secondary market constituted an investment for the purposes of the relevant BIT, and where the number of claimants stood at 60 000,

⁸⁷⁵ Joost Pauwelyn, 'Rational Design or Accidental Evolution? The Emergence of International Investment Law', in Zachary Douglas, Joost Pauwelyn and Jorge E. Viñuales (eds.), *The Foundations of International Investment Law: Bringing Theory into Practice* (Oxford University Press, 2014), pp. 11-44, at 31.

⁸⁷⁶ Andreas W. Lowenfeld, 'The ICSID Convention: Origins and Transformation', 38 *Georgia Journal of International and Comparative Law* (2009), pp. 47-61, at 55.

⁸⁷⁷ Sornarajah, *Resistance and Change*, supra note 23, pp. 136 and 138.

⁸⁷⁸ *Maffezini* award, supra note 162.

⁸⁷⁹ *Tokios Tokelés v. Ukraine*, ICSID Case No. ARB/02/18, Decision on Jurisdiction, 29 April 2004.

raising the prospect of future mass claims.⁸⁸⁰ Sornarajah also argues that the interpretations that tribunals have made of standard expropriation and fair and equitable treatment provisions reflect a similar type of expansionary trend. As to the former, he argues that as a result of the interpretations that tribunals made of expropriation provisions, states started to introduce restrictions and limitations in more recent BITs, which 'restricted the scope of expropriation' and reduced its significance as a ground of investor claims.⁸⁸¹ As a consequence, 'once the door of expropriation began closing', the 'viability' of investment arbitration required opening 'another door through the awakening of the, hitherto dormant, fair and equitable standard'.⁸⁸² In other words, the FET standard served the purpose of holding states accountable for measures not otherwise caught by BITs, with the introduction of the doctrine of 'legitimate expectations', the 'most glaring example of expansionary activism', being central in this respect.⁸⁸³

For Sornarajah, the central reason for the 'expansionary activism' that started with the *AAPL v. Sri Lanka* award was the 'institutional context' of investment arbitration, which favored 'inclination towards solutions geared to neoliberal norms that induced the course of decisions towards solutions acceptable to foreign business'.⁸⁸⁴ With 'institutional context', he refers not only to the institutions that administer investment arbitrations,⁸⁸⁵ but to the 'global acceptance' of trade and investment liberalization as a recipe for economic growth, which took root from the early 1990s onward and facilitated the 'establishment of a neoliberal system of investment protection'.⁸⁸⁶ Sornarajah recognizes that in many cases arbitrators have dismissed investor claims and notes that the 'expansionary activism' of tribunals has been met with broad resistance, also within the investment arbitration community,⁸⁸⁷ but these counterforces may not necessarily succeed in bringing about 'the retreat of neoliberalism...because of its adaptive capacity and its ability to morph into

⁸⁸⁰ *Abaclat and Others v. Argentine Republic*, ICSID Case No. ARB/07/5, Decision on Jurisdiction and Admissibility, 4 August 2011; Sornarajah, *Resistance and Change*, supra note 23, p. 168. Sornarajah also refers to *Deutsche Bank v. Sri Lanka* where a hedging agreement was held as constituting an investment. See *Deutsche Bank AG v. Sri Lanka*, ICSID Case No. ARB/09/2, Award, 31 October 2012.

⁸⁸¹ Sornarajah, supra note 23, p. 74 (Chapter 4 of the book deals with expropriation).

⁸⁸² *Idem*.

⁸⁸³ *Ibid.*, p. 248 (Chapter 5 of the book deals with the FET standard).

⁸⁸⁴ *Ibid.*, p. 389.

⁸⁸⁵ Such as ICSID, which is one of the organizations of the World Bank Group and administers the highest number of investment arbitrations.

⁸⁸⁶ Sornarajah, *Resistance and Change*, supra note 23, pp. 137-138.

⁸⁸⁷ For example, Sornarajah refers to arbitrators who enhance the 'norms of power' and those who defend the 'norms of justice'. *Ibid.*, p. 28.

different forms when faced with criticism'.⁸⁸⁸ Hence, Sornarajah suggests that the only way in which states can resist neoliberalism as it expresses itself in arbitral practice is by denouncing their existing treaties: 'Wiping the slate clean seems to be the only possible way forward'.⁸⁸⁹

If one looks at Sornarajah's argument from the proponents' perspective, it is unlikely to make much sense. In their view, arbitral tribunals are called upon to determine the balance of public and private interests in light of international investment protection standards. This basic mandate extends to all domestic policy across the three branches of government, and while one can debate about the soundness of individual decisions, the basic orientation of the regime reflects the will of the participatory states, as also corroborated by their modest reactions to the critique and hitherto case law. As to the 'expansive' interpretations of arbitral tribunals, they reflect how most investment treaties emphasize solely the investment protection function without making references to public regulatory functions, with tribunals correctly emphasizing the former in accordance with the applicable law. The regime is also capable of self-correction as other tribunals have taken a different approach than the tribunals on which Sornarajah relies when developing his argument. For example, unlike the *Maffezini* tribunal, the *Plama* tribunal held that the claimant investor could not rely on more favorable arbitration clauses found in the host state's other BITs because the contracting states clearly had no intention to allow this when concluding the relevant BIT.⁸⁹⁰ Moreover, the claim that arbitral tribunals *only* emphasize and protect investor interests to the exclusion of public interests is simply misleading in light of existing case law. The claims by Philip Morris against Australia and Uruguay concerning plain packaging of tobacco products are a case in point. Philip Morris Asia (domicile in Hong Kong) had acquired its Australian subsidiaries at a time when it was reasonably clear that the Australian government was going to adopt plain packaging measures requiring the removal of all brand insignia from tobacco products. The tribunal concluded that the initiation of the arbitration constituted 'an abuse of rights', as the acquisition of the Australian subsidiaries 'was carried out for the principal, if not sole, purpose of gaining...protection' under the Hong Kong-Australia BIT, and the tribunal held that the

⁸⁸⁸ Ibid., p. 67.

⁸⁸⁹ Ibid., p. 408.

⁸⁹⁰ See *Plama Consortium Limited v. Bulgaria*, ICSID Case No. ARB/03/24, Decision on Jurisdiction, 8 February 2005, paras. 183-227.

claimant's claims were inadmissible.⁸⁹¹ Similarly, in *Philip Morris v. Uruguay*, the tribunal noted that the 'responsibility for public health measures rests with the government and investment tribunals should pay great deference to governmental judgments of national needs in matters such as the protection of public health'.⁸⁹² The tribunal dismissed the claimant's claims and ordered the claimant to bear Uruguay's legal costs as well as the costs of the arbitration.

This testifies to the difficulties in using individual cases to make a broad argument about the purposes and implications of the regime. There are always cases that point to a different conclusion, and most arbitral awards are based on contested and fact-intensive circumstances that are open to varied interpretations. Perhaps Sornarajah's argument should be seen as a political intervention in investment law debates, the purpose of which is to point to the ambiguities of economic globalization and to raise discussion about the proper allocation of jurisdiction between domestic and international institutions and about the attendant model of state-market relations. Generally speaking, Sornarajah's assumption that 'wiping the slate clean' would promote 'notions of fairness and global justice' and bring about a law 'that takes human needs into account rather than caters for the human greed of a few' is understandable,⁸⁹³ but whether states would be more free and willing to protect, for example, the environment if the investment treaty regime were removed from the policy equation is an unsubstantiated hypothesis. This brings us to the regulatory chill argument, which is less ideological than Sornarajah's account, but similarly concerned about the impact that investment treaties have on domestic policy-making. An interesting fact is that New Zealand postponed the application of its plain packaging legislation until the *Philip Morris v. Australia* tribunal had dismissed the claimant's claims. This isolated example suggests that there appears to some evidence that proves the existence of regulatory chill.

⁸⁹¹ See *Philip Morris Asia Limited v. Australia*, PCA Case No. 2012-12, Award on Jurisdiction and Admissibility, 17 December 2015, para. 588.

⁸⁹² *Philip Morris Brands Sàrl, Philip Morris Products S.A. and Abal Hermanos S.A. v. Oriental Republic of Uruguay*, ICSID Case No. ARB/10/7, Award, 8 July 2016, para. 399.

⁸⁹³ *Ibid.*, p. 76.

7.4. Regulatory Chill

The above discussion showed that there is very little empirical research on the question whether legislators, policy-makers and state officials have knowledge about the investment treaty obligations to which their home states have committed. The regulatory chill argument assumes that state authorities know and understand the content of such obligations when they contemplate whether to adopt specific policy proposals. Some commentators have argued that this means that public officials, at all levels of government, 'will take account of the possibility of a reaction on the part of a foreign investor' if a relevant BIT exists, and in this way 'investor interests will be *internalized* in the process of public decision-making'.⁸⁹⁴ In other words, the mere existence of BITs will discourage states from adopting or enforcing good faith 'regulatory measures because of a perceived or actual threat of investment arbitration'.⁸⁹⁵ Such impact is commonly known as 'regulatory chill' and the quotes suggest that it can be understood in two ways. First, as referring to 'a *broad* phenomenon whereby regulatory progress is dampened across all areas that impact foreign investors because government officials are aware of, and seriously concerned about, the risk of an investor-state dispute arising, and, second, as referring to 'the chilling of specific regulatory measures that have been proposed or adopted by governments'.⁸⁹⁶ As Tienhaara recognizes, the first type of regulatory chill 'would be quite difficult to measure' without 'detailed surveys or in-depth interviews with regulators',⁸⁹⁷ whereas the latter type of regulatory chill is much narrower and relates to situations where a state entity has specific knowledge about a claim that an investor aims to raise against a regulatory measure that he opposes.

The regulatory chill debate is not limited to the investment treaty regime. Already in the 1990s many political scientists asked whether 'countries might fail to raise environmental

⁸⁹⁴ Martti Koskenniemi, 'It's not the Cases, It's the System', 18 *Journal of World Investment & Trade* (2017), pp. 343-353, at 351-352.

⁸⁹⁵ Christian Tietje and Freya Baetens, *The Impact of Investor-State Dispute Settlement (ISDS) in the Transatlantic Trade and Investment Partnership* (A study prepared for Minister for Foreign Trade and Development Cooperation and Ministry of Foreign Affairs of the Netherlands, 2014), p. 40.

⁸⁹⁶ These definitions are from Kyla Tienhaara, 'Regulatory Chill and the Threat of Arbitration: A View from Political Science', in Chester Brown and Kate Miles (eds.), *Evolution in Investment Treaty Law and Arbitration* (Cambridge University Press, 2012), pp. 606-628, at 607. Tienhaara discusses the various methodological questions that the narrower type of regulatory chill raises.

⁸⁹⁷ *Idem*.

standards for fear of capital flight'.⁸⁹⁸ Interest groups were arguing that raising environmental standards weakens the competitiveness of domestic industries vis-à-vis economies with less stringent standards, whereas in the present context the concern relates to potential reactions by foreign investors. Similarly, and as will be discussed below, the debates in the early 2000s on the legitimacy of the WTO focused on the constraints that the world trade regime placed on the 'decisional capacities' of its member states,⁸⁹⁹ with the WTO bodies suddenly reviewing measures which had previously fallen 'within the universe of domestic economic regulation'.⁹⁰⁰ One specific concern was that national environmental protection laws were increasingly 'challenged as unfair trade barriers',⁹⁰¹ just as a high number of investor claims now challenge environmental laws and regulations.⁹⁰² This suggests, again, that the regulatory chill debate, and the critique of the investment treaty regime in general, stem from the same tradition as the previous waves of resistance against economic globalization.

The general problem with regulatory chill is that it is difficult to obtain evidence of something that has not happened. State officials and policy-makers will be less than eager to reveal if and when a policy proposal was buried for fear of investment arbitration.⁹⁰³ There are studies that touch upon the regulatory chill issue in one or another way. For example, one recent study analyzed the question whether states have engaged in investment treaty reform as a reaction to BIT claims and pro-investor awards, and the author's main conclusion was that 'the impact of *investment claims* is considerably smaller than expected', whereas arbitrations ending in the claimant's favor have had a 'traceable influence' on the content of investment treaties.⁹⁰⁴ Howse has looked at the terms of

⁸⁹⁸ Neumayer, 'Do Countries Fail to Raise Environmental Standards?', supra note 775, p. 233. See also Gareth Porter, 'Trade Competition and Pollution Standards: "Race to the Bottom" or "Stuck at the Bottom"?', 8 *Journal of Environment & Development* (1999), pp. 133-151.

⁸⁹⁹ Deborah Z. Cass, *The Constitutionalization of the World Trade Organization. Legitimacy, Democracy, and Community in the International Trading System* (Oxford University Press, 2005), p. 212.

⁹⁰⁰ Larry DiMatteo et al., 'The Doha Declaration and Beyond: Giving a Voice to Non-Trade Concerns Within the WTO Trade Regime', 36 *Vanderbilt Journal of Transnational Law* (2003), pp. 95-160, at 98.

⁹⁰¹ *Ibid.*, p. 99.

⁹⁰² See e.g. *Metalclad Corp. v. United Mexican States*, ICSID Case No. ARB(AF)/97/1, Award, 30 August 2000; *Methanex Corp. v. United States*, UNCITRAL, Final Award on Jurisdiction and Merits, 3 August 2005. Langford and Behn count 26 arbitrations 'where it is known that the host state's justification for the domestic measure is based, in whole or part, on environmental grounds'. See Daniel Behn and Malcolm Langford, 'Trumping the Environment? An Empirical Perspective on the Legitimacy of Investment Treaty Arbitration', 18 *Journal of World Investment & Trade* (2017), pp. 14-61, at 18.

⁹⁰³ See Van Harten and Scott, 'Internal Vetting of Regulatory Proposals', supra note 728.

⁹⁰⁴ Wolfgang Alschner, 'The Impact of Investment Arbitration on Investment Treaty Design: Myths versus Reality', 42 *Yale Journal of International Law* (2017), pp. 1-66, the quotes are from pages 50 and 62. See also Roberts, 'Power and Persuasion', supra note 786.

settlement in arbitrations that were settled before the merits stage, and he notes that the settlements 'for which public information was available, almost all appeared to involve either significant monetary relief for the investor...or significant adjustment of the regulatory framework to the benefit' of the claimant investors.⁹⁰⁵ The caveat here is that without detailed information it is impossible to tell whether the settlements concerned 'legitimate' policy measures or whether they were settled because of perceived regulatory overreach on the part of the host state. There are also a few studies and investigative news reports that give direct support to the regulatory chill argument,⁹⁰⁶ as there are studies (or examples) of situations where states have adopted a measure, although an investor had notified that it will challenge the measure under an investment treaty.⁹⁰⁷ For example, it was reported that a Dubai real estate mogul was condemned to prison for acquiring a huge stretch of land from Egyptian officials for a fraction of the market value so as to build a luxury resort on the coast of the Red Sea. The land was declared forfeit by an Egyptian court, and immediately after the conviction the company (owned by the mogul) notified Egypt that it will raise a claim under the Egypt-UAE BIT, with the basic argument being that the deal was made in accordance with Egyptian law. Soon after, the case was settled and the investor's prison sentence abolished.⁹⁰⁸

The proponents of the investment treaty regime rebut the regulatory chill argument in different ways. One commentator has argued that an increase in environmental legislation in Canada proves that NAFTA's Chapter 11 (dealing with investment protection) has had no impact on progressive policy-making in that field.⁹⁰⁹ Schill, in turn, argues that

⁹⁰⁵ Rob Howse, 'International Investment Law and Arbitration: A Conceptual Framework, forthcoming in Helene Ruiz-Fabri (ed.), *International Law and Litigation* (Nomos, 2017).

⁹⁰⁶ See e.g. Bonnitca, Poulsen and Waibel, *The Political Economy*, supra note 679, p. 241; Gross, 'Inordinate Chill', supra note 803; Chapter 4 in David Schneiderman, *Constitutionalizing Economic Globalization: Investment Rules and Democracy's Promise* (Cambridge University Press, 2008); Howard Mann, *Private Rights, Public Problems: a Guide to NAFTA's Controversial Chapter on Investor Rights* (IISD and World Wildlife Fund, 2001); Tariana Turia, 'Government moves forward with plain packaging of tobacco products', *New Zealand Government Official Website*, 19 February 2013. See at <https://www.beehive.govt.nz/release/government-moves-forward-plain-packaging-tobacco-products> (accessed 12 August 2017); Chris Hamby has written four separate pieces on the dark sides of the investment treaty regime, which are available at <https://www.buzzfeed.com/globalsupercourt> (accessed 19 August 2017).

⁹⁰⁷ Bonnitca, Poulsen and Waibel, *The Political Economy*, supra note 679, p. 241. It is also useful to remember, as Bonnitca, Poulsen and Waibel note, that regulatory chill could also refer to a situation where a host state plans to nationalize a given investment without compensation. However, the term is only used to refer to a chilling effect on the adoption of policy proposals whose purpose is considered rational and legitimate (difficult as it may be to define what is rational and legitimate). *Ibid.*, p. 240.

⁹⁰⁸ Hamby, 'The court that rules the world', supra note 804.

⁹⁰⁹ Julie Soloway, 'NAFTA's Chapter 11: Investment Protection, Integration and the Public Interest', 9 *Choices* (2003), pp. 1-47, at 19.

'investment treaties neither obstruct nor chill state regulation that aims at reducing greenhouse gas emissions',⁹¹⁰ but his conclusion is based on an analysis of a number of awards, rather than on situations where the *threat* of arbitration links with the withdrawal of a policy proposal.

This very short discussion on regulatory chill shows that the relevant evidence is scant and impressionistic. It is intuitively plausible to assume that much of the 'chilling' takes place under the radar, with corporate lobbyists referring to all sorts of legal and political strategies if the host state adopts a less than desired policy change affecting high-value investments. But this type of background chilling in no way depends on investment treaties, as it is more or less a standard aspect of politics. More generally, the proponents could also point out that the very purpose of international law is to limit state action, with treaty-making being the most common tool in this respect. As Tietje and Baetens put it, 'the essential thrust of international investment protection is to achieve some level of "chill", that is, to chill governments from treating foreign investors unfavorably'.⁹¹¹ This observation brings us back to the debate on the purposes and implications of the investment treaty regime. As repeatedly noted, the proponents argue that investment treaties and arbitration promote and enforce international protection standards, with tribunals' jurisdiction extending to all type of policy measures. In their view, the 'chilling effect' that investment treaties create is a welcomed development, because it compels host states to pay due consideration to the interests of foreign investors. The proponents could also support this argument with reference to cases where tribunals have paid (in their view at least) due respect to the relevant public interest, as it suggests that investment treaties chill less than the critics imply.

At the risk of repeating myself, it seems clear that even if we have very little evidence of regulatory chill (or lack thereof), governments will often co-opt the preferences of foreign investors instead of domestic stakeholders, with a relevant investment treaty possibly playing some role in such decision. On the other hand, if investment treaties lead governments to *further* prioritize investor interests at the expense of other regulatory interests, the critics will again think that the only way in which this can be countered is by

⁹¹⁰ Stephan W. Schill, 'Do Investment Treaties Chill Unilateral State Regulation to Mitigate Climate Change?', 24 *Journal of International Arbitration* (2007), pp. 469-477, at 470.

⁹¹¹ Tietje and Baetens, *The Impact of Investor-State Dispute Settlement*, supra note 895, p. 46.

exiting the investment treaty regime. I will return to this issue below, but a preliminary observation is that I am not in disagreement with the 'exit strategy' as such, because there is very little evidence that would corroborate the contention that investment treaties are important in the manner suggested by the proponents. However, I am less than convinced about the idea that exiting the regime would have a significant impact on the protection of the public goods over which the critics worry.

The regulatory chill argument is also at the heart of the debate on the EU's external investment policy. The Commission has argued that the investment protection provisions of the Comprehensive Economic and Trade Agreement (CETA)⁹¹² between Canada and the EU will ensure 'that the right to regulate for public policies is fully preserved', as in Article 8.9(1) CETA the parties 'reaffirm their right to regulate within their territories to achieve legitimate policy objectives, such as the protection of public health, safety, the environment or public morals, social or consumer protection or the promotion and protection of cultural diversity'.⁹¹³ Article 8.9(2) CETA is also relevant as it provides that 'the mere fact that a Party regulates, including through a modification to its laws, in a manner which negatively affects an investment or interferes with an investor's expectations, including its expectations of profits, does not amount to a breach of an obligation under this Section'. These two paragraphs are quite empty in content as they merely state the obvious: paragraph one provides that the investment protection provisions do not prevent the parties from adopting public interest measures, and although such provision is not typically included in member state BITs, no investment treaty has ever proscribed public interest measures. Paragraph two, in turn, states that if a measure affects an investment negatively, this does not, per se, constitute a breach of the investment protection obligations. In other words, a measure constitutes a breach of the investment protection obligations only if the relevant criteria are met. In yet other words, paragraph two creates the perception that an investor cannot raise a claim if (for example) his future

⁹¹² See Comprehensive Economic and Trade Agreement (CETA) between Canada, of the one part, and the European Union and its Member States, of the other part, OJ L 11, 14.1.2017, pp. 23-1079.

⁹¹³ Paragraphs 2 to 4 of Article 8.9 aim at preventing claims based on the revocation of subsidies, including claims such as *Micula* (for example, paragraph 4 provides that 'nothing in this Section shall be construed as preventing a Party from discontinuing the granting of a subsidy or requesting its reimbursement where such measure is necessary in order to comply with international obligations between the Parties *or has been ordered by a competent court, administrative tribunal or other competent authority, or requiring that Party to compensate the investor therefor*', emphasis added, footnotes omitted). CETA will enter into force (provisionally) before the end of 2017, but the investment protection chapter enters into force only after the agreement has been ratified by the parliaments of all EU member states.

profits diminish as a result of a measure, although such impact may well be part and parcel of a claim that allegedly constitutes a breach of the host state's investment protection obligations. Generally speaking, however, Article 8.9 CETA may have practical effect in the sense that it guides the interpretation of the other investment protection provisions to a direction that gives more emphasis to the relevant public interest.

Article 8.10(1) CETA lays down the contracting states' investment protection obligations. It provides that the parties shall accord to investments 'fair and equitable treatment and full protection and security', and paragraph two specifies that a party breaches the fair and equitable treatment standard if a measure constitutes 'denial of justice', 'fundamental breach of due process', 'manifest arbitrariness', 'targeted discrimination on manifestly wrongful grounds', or 'abusive treatment of investors, such as coercion, duress and harassment'.⁹¹⁴ Paragraph four provides that when applying the FET obligation, CETA tribunals 'may take into account whether a Party made a specific representation to an investor to induce a covered investment, that created a legitimate expectation, and upon which the investor relied in deciding to make or maintain the covered investment, but that the Party subsequently frustrated', whereas paragraph five provides that full protection and security 'refers to the Party's obligations relating to the physical security of investors and covered investments'.⁹¹⁵ The argument that CETA protects the parties' right to regulate is clearly misleading in the sense that the expression in Article 8.9(1) does not mean that investors cannot challenge measures that protect 'public health, safety, the environment or public morals, social or consumer protection or the promotion and protection of cultural diversity'. The real questions are whether such measures are likely to fill the criteria of what constitutes a breach of the FET obligation under Article 8.10(2) and to what extent the 'legitimate expectation' clause may affect the tribunal's analysis of the criteria in specific cases. Public interest measures that are adopted in accordance with due process of law are unlikely to lead to successful claims under CETA's investment protection rules, but the economic, environmental and technological uncertainties that relate to large-scale

⁹¹⁴ The parties also breach the fair and equitable treatment standard if a measure constitutes 'a breach of any further elements of the fair and equitable treatment obligation adopted by the Parties.' This 'adoption' refers to the ability of the CETA Joint Committee to adopt decisions on the 'content of the obligation to provide fair and equitable treatment' under paragraph 3 of Article 8.9.

⁹¹⁵ Paragraphs 6 of Article 8.10 provide that 'a breach of another provision of this Agreement, or of a separate international agreement does not establish a breach of this Article', and paragraph 7 provides that 'the fact that a measure breaches domestic law does not, in and of itself, establish a breach of this Article. In order to ascertain whether the measure breaches this Article, the Tribunal must consider whether a Party has acted inconsistently with the obligations in paragraph 1'.

investment projects, particularly in the extractive industries sector, may well lead to non-frivolous claims that challenge measures whose sole purpose is to protect public values. The above example concerning the Talvivaara mine in Finland is a case in point.

The idea that the CETA provisions are a step forward resembles the idea that the critique has already served its purpose as arbitral tribunals have reacted to the various signals that states have sent as a reaction to particular case outcomes, which finds support in the fact that most states have not reacted to the critique in any substantive way. In other words, and as Miles puts it, there might be 'a sense that even if the substantive law on investment protection has not yet changed dramatically, the wider environment in which it is operating has - whilst the importance of foreign investment protection is appreciated, *tolerance for investment rules that operate so as to trump other interests has waned*'.⁹¹⁶ In yet other words, while 'virtually all known' investment arbitration cases have been raised under 'old-generation' BITs containing vague protection standards,⁹¹⁷ this should not give rise to concern as arbitral tribunals now provide leeway for host states to adopt legitimate public interest measures. Even if individual tribunals have gone rogue and provided expansive interpretations of central investment treaty provisions, the investment arbitration community, through doctrinal elaboration, ensures that the threat of interpretive overreach is gradually neutralized. The content of academic journals focusing on investment arbitration is largely doctrinal, which approach is facilitated by an increasing number of publicly available arbitral awards and funding by global law firms with an active investment arbitration practice. The increasing doctrinal effort is understood as providing a remedy against the vagueness of investment protection standards, such as fair and equitable treatment and indirect expropriation, with scholar-practitioners⁹¹⁸ identifying and describing their core elements in ever more detail, which then allows the various stakeholders to understand what is fair and equitable treatment and what is not. In the words of Brower and Schill, 'growing doctrinal analysis' will 'prove that concepts relating to investors' rights...are not as vague and indeterminate as some argue',⁹¹⁹ with a coherent

⁹¹⁶ Kate Miles, *Investor-State Dispute Settlement: Conflict, Convergence, and Future Directions*, Bungenberg et al. (eds.), *European Yearbook of International Economic Law*, supra note 723, pp. 274-308, at 295 (emphasis added).

⁹¹⁷ UNCTAD, *World Investment Report 2017*, supra note 772, at xii.

⁹¹⁸ One report noted that 74 % of the editorial board members of key arbitration journals 'have a background in the arbitration industry'. Eberhardt and Olivet, *Profiting from Injustice*, supra note 781, p. 65.

⁹¹⁹ Brower and Schill, 'The Legitimacy of International Investment Law', supra note 18, pp. 473-474.

body of law emerging from the initial uncertainty. Or, as the saying goes, 'good judgment comes from experience, and a lot of that comes from bad judgments'.

Generally speaking, the narrative of progress, which undergirds both the Commission's storyline on CETA and the idea that doctrinal analysis will enhance the legitimacy of the investment treaty regime is not entirely unconvincing. It is clear that frivolous investor claims have less chance of succeeding given the increased publicity of investment arbitration and the amendments made to investment treaties. Scholarly consensus over core aspects of standard treaty provisions may also decrease the uncertainties that stem from the decentralized and ad hoc structure of investment arbitration. One could also point to the fact that while an overwhelming majority of existing BITs are 'old-fashioned', tribunals are using public law analogies to fill gaps in investment treaties,⁹²⁰ which testifies that arbitral tribunals are both reacting to specific signals states are sending as well as engaging in self-regulation as a result of the broader public and political debate. If the investment court system materializes at some point, the procedural shortcomings associated with the present regime - such as double hatting, lack of appellate review and lack of transparency - are by and large eliminated. However, whether this amounts to progress in the eyes of the critics is a different matter, and one that I will address below.

As to the issue pro-investor bias, which straddles the critique, its existence will in large measure depend on the view one has of the purposes and implications of investment treaties. If the regime is understood to promote the rule of law, increase investment flows, and contribute to economic development, the argument about bias will seem quite strange, also because the very purpose of investment treaties is to take the perspective of the investor. On the other hand, if investment treaties and arbitration are perceived as undermining the public interest, the argument will have direct appeal because it confirms the critic's basic assumption. In other words, vaguely formulated treaty standards, lack of references to states' regulatory powers in many investment treaties, and the background of many arbitrators in private sector legal practice are all factors that relate to the issue of bias,⁹²¹ but combining these factors to demonstrate its existence already assumes that arbitral tribunals should show more deference to domestic policy. Van Harten has noted

⁹²⁰ For examples and discussion, see Roberts, 'Clash of Paradigms', *supra* note 641, pp. 45-94.

⁹²¹ On this last element, see Joost Pauwelyn, 'The Rule of Law without the Rule of Lawyers? Why Investment Arbitrators are from Mars, Trade Adjudicators from Venus', 109 *American Journal of International Law* (2015), pp. 761-805.

that his research on the question of bias 'lend[s] support to *perceptions* that the design of investment treaty arbitration does not support fair and independent adjudication of the boundaries of sovereign authority and of disputes involving public funds'.⁹²² Statistical and empirical research on the issue of bias is fraught with difficult methodological questions, with one commentator noting that 'scholars generally acknowledge that definitively proving or disproving systemic bias in adjudication is, quite simply, impossible'.⁹²³

The proponents have also taken issue with the question of bias by arguing, for example, that the highest priority for and the fundamental self-interest of arbitrators is to build a reputation of impartiality, with the 'crucial factor for appointment' being 'not the possible or real bias of an arbitrator' but 'rather his or her reputation for impartial and independent judgment'.⁹²⁴ As to the claim that arbitrators place investor interests above public interests, the proponents argue that such partisan approach would be harmful or even 'suicidal' for arbitrators, given the widespread and increasing public scrutiny of arbitral awards.⁹²⁵ These arguments are based on an idealized picture of a wise and impartial judge who transcends partisan motives through sheer will and applies the law objectively on the basis of the factual record. But arbitrators are mere mortals and 'bring policy preferences, their education, career background and their life experience to...arbitrations', and such factors will influence the choices they make when filling 'ambiguities and gaps' in the applicable law.⁹²⁶ Again, these arguments miss the critics' main point of contention, which stems from the fact that tribunals are able to review domestic policy. This basic authority alone creates a perception of 'pro-investor' bias in the eyes of many critics, and it is irrelevant whether or not the reasoning of tribunals is formally impeccable and based on a balanced reading of the factual record. Similarly, if empirical and statistical analyses of arbitral awards and arbitrator backgrounds can only provide hypotheses, it is unlikely that a 'data-driven

⁹²² Gus van Harten, 'Arbitrator Behaviour in Asymmetrical Adjudication: An Empirical Study of Investment Treaty Arbitration', *Osgoode CLPE Research Paper*, No. 41/2012, the quote is from the abstract (emphasis added).

⁹²³ Catherine A. Rogers, 'The Politics of International Investment Arbitrators', 12 *Santa Clara Journal of International Law* (2014), pp. 223-262, at 233.

⁹²⁴ Brower and Schill, 'The Legitimacy of International Investment Law', *supra* note 18, pp. 491-492.

⁹²⁵ *Ibid.*, pp. 492-493. The word 'suicidal' is from Alec Stone Sweet, 'Arbitration and Judicialization', 1 *Oñati Socio-Legal Series* (2011), pp. 1-23, at 21.

⁹²⁶ Michael Waibel and Yanhui Wu, 'Are Arbitrators Political? Evidence from International Investment Arbitration' (unpublished manuscript, January 2017), pp. 23-24.

approach⁹²⁷ changes the perceptions that the critics and proponents have of the investment treaty regime.

In one sense, it is not surprising that 'data-driven' scholarship is on the rise. Such approach reflects the current economic zeitgeist to which societal problems are more technical and less political, and the 'allure of the ostensibly neutrality of empirical research' will probably hold much sway with many financiers of academic research.⁹²⁸ This is not an argument against empirical and statistical scholarship, and those who do it willingly admit the attendant limitations and challenges.⁹²⁹ Rather, the point is that such evidence may well look like tinkering around the edges for the critics, if and when the results provide no conclusive answers either way or only point to 'patterns' in decision-making. If the critique of the investment treaty regime is about the underlying political stakes - who gets to decide, who benefits and who loses, whose values and interests receive recognition - no amount of data crunching can end the disagreement between the opposing sides.

7.5. Conclusion

As was the case with the arguments for the investment treaty regime, the arguments against the regime rely on individual case outcomes and anecdotal evidence, which are understood as demonstrating a systematic lack of deference to domestic policy-making on the part of arbitral tribunals. For some, this default approach suggests that arbitral tribunals are hostile toward non-economic values in general because of an ideological predisposition toward a neoliberal philosophy under which political intervention in the economy is considered largely unnecessary or even inimical. More generally, and as noted, if the critique of investment treaties and arbitration is political, it does not matter what the scant empirical evidence says. The critics are aiming to provide more latitude for governments to adopt public interest measures, and since investment treaties *may* constrain domestic policy-making it is wiser to remove them from the equation. Whether or not this leads governments to protect and promote various public values is a different matter, but it does remove one potential obstacle. When defending the proposal for an investment court system (ICS), Trade Commissioner Malmström noted that 'there is a fundamental and

⁹²⁷ The phrase is from Wolfgang Alschner, Joost Pauwelyn and Sergio Puig, 'The Data-Driven Future of International Economic Law', 20 *Journal of International Economic Law* (2017), pp. 217-231.

⁹²⁸ Rogers, 'The Politics of International Investment Arbitrators', *supra* note 923, p. 233.

⁹²⁹ See Alschner, Pauwelyn and Puig, 'Data-Driven Future', *supra* note 927, pp. 226-231.

widespread lack of trust by the public in the fairness and impartiality of the old ISDS model'. Yet investment protection remains 'an important part of the EU's investment policy', as EU investors have been 'the most frequent users of the existing system'. This meant that 'we, from the EU side, must take our responsibility to reform and modernize' the investment treaty regime.⁹³⁰ These arguments are based on the perception that the critique is legal-technical and that the legitimacy of investment treaties can be reformed through treaty reform. I return to Malmström's rhetoric shortly.

The ICS proposal as well as the CETA investment protection provisions have received mixed reviews. On the business side, the worry is that the express reference to the 'right to regulate' as well as the specifications made to the FET standard could lead tribunals to excessively defer to regulatory measures that negatively affect investments.⁹³¹ Conversely, the critics fail to see the wisdom of the proposal as it continues to provide special privileges to foreign investors in the absence of evidence proving the necessity of such privileges.⁹³² Generally speaking, the Commission attempts to ensure that the reformed investment treaty regime defers to domestic policy-making to an extent that wipes away the twin-fear of regulatory chill and interpretive overreach on the part of arbitral tribunals. The proposals also seek to ensure that the new system is akin to a public court system where the parties no longer choose the judges, where transparency is the rule rather than the exception, and where an appellate body guarantees the emergence of a more coherent jurisprudence. Should the proposal move forward in the coming years, and should it gradually 'multilateralize', one could argue that this is a step forward in comparison to the existing investment treaty regime, which consists mostly of old-fashioned BITs. Malmström's use of the personal pronoun 'we' also implies that she is trying to convince the 'European public' that the Commission's efforts are premised on the existence of a collective purpose that guides the Commission's policy proposals and serves the interests of all EU citizens. The concluding chapter looks at this idea more closely by drawing an analogy to the previous debates on the legitimacy of the WTO as well as by providing some comments on the EU's future investment policy.

⁹³⁰ Cecilia Malmström, 'Proposing an Investment Court System', 16 September 2015. Available at https://ec.europa.eu/commission/commissioners/2014-2019/malmstrom/blog/proposing-investment-court-system_en (accessed 1 September 2017).

⁹³¹ See e.g. BusinessEurope, 'The Commission proposal on a new investment court system', *BusinessEurope Note*, 23 October 2015; Nikos Lavranos, 'The Shortcomings of the Proposal for an "International Court System" (ICS)', *EFILABlog*, 2 February 2016.

⁹³² Gus van Harten, 'ISDS in the Revised CETA: Positive Steps, But is it the "Gold Standard"?', *Investor-State Arbitration Commentary Series No. 6*, Centre for International Governance Innovation, 25 May 2016.

8. Conclusion

The essence of the critical arguments is remarkably similar to the arguments raised in the previous debate concerning the legitimacy of the WTO, and the political agenda of the critics is strikingly similar with the agenda of the global justice movement that made headlines from the 1999 Seattle protests onward. Lang has provided a first-rate account and analysis of the debates concerning the world trade system around the turn of the millennium as well as of the preceding rise of neoliberal thinking. I will first provide a summary of Lang's account, after which I attempt to show how the reactions to the critique of investment arbitration follow a similar type of pattern as the reactions to the critique of the WTO. My suggestion is that the Commission's proposal for an investment court system and the Trade Commissioner's sentimental references to a collective purpose fail to understand what the critics of the investment treaty regime are trying to achieve.

Lang defines neoliberal thinking as 'a turn away from an idea of politics as the creation, mobilization, and realization of the collective purposes of a political community, towards an idea of politics as the facilitation of individuals' pursuit of their own private goals and purposes'.⁹³³ In the economic domain this idea translates into a 'strong normative preference for...free and competitive markets, combined with strong private property rights' and the retreat of the state 'from a direct role in economic production through the privatization of state-owned industries and utilities, and sometimes the provision of social services'.⁹³⁴ In Lang's account, the rise of neoliberal thought had a profound impact on the way in which politics was understood in and around the WTO. The world trade regime came to be understood as the global political and economic marketplace where traders were protected from arbitrary exercises of public power, with the WTO legal framework 'imagined as the embodiment of the rule of law in global trade governance, and...restructured in accordance with such rule of law values as neutrality, predictability, certainty, generality, and objectivity'.⁹³⁵ A corollary of this view was the 'delegitimization' of the notion 'that governments could intervene in the economy in the pursuit of collective social purposes', with the purported purpose of a measure transforming into a subjective and unpredictable yardstick, which could no longer be used to establish a measure's

⁹³³ Andrew Lang, *World Trade Law After Neoliberalism. Reimagining the Global Economic Order* (Oxford University Press, 2011), p. 1.

⁹³⁴ *Ibid.*, pp. 1-2.

⁹³⁵ *Ibid.*, p. 6.

compliance with WTO law.⁹³⁶ Instead, 'technical bodies of knowledge...concerning appropriate and optimal regulation' of economic activity became the dominant method with which domestic measures were assessed, hiding from sight the fact that this method was premised on a particular vision of state-market relations.⁹³⁷

This ideological shift also meant that domestic measures, previously perceived as 'part of the "normal" range of governmental action in the marketplace, undertaken for a clearly legitimate purpose',⁹³⁸ were increasingly challenged at the WTO as deviations of the new neoliberal normal. As a result, WTO bodies were asked to determine 'the legality of a variety of different regulatory measures having to do with public health, consumer protection, and environmental protection, among other matters of considerable political sensitivity'.⁹³⁹ With the ideological foundations of the WTO having shifted, the GATT panels rendered a string of decisions in which trade liberalization trumped other (and for many more important) public values. As a reaction, the critics made the basic argument that it should be left to the discretion of WTO members to determine how they organize state-market relations and 'for the WTO to pass judgment on the optimality or appropriateness of regulatory measures passed through legitimate domestic processes' was an 'illegitimate intrusion' into those processes.⁹⁴⁰ While Lang agrees with these criticisms in principle, he takes issue with the way in which the WTO dispute-settlement system has responded to the criticisms. In essence, Lang argues that the critique led to the 'proceduralization' of WTO review in that the focus shifted from substantive review to the 'quality' of the domestic institutional processes through which regulatory measures were adopted. This was meant to signal increasing deference to domestic policy-making on the part of WTO bodies. Lang problematizes this notion by arguing that this type of 'procedural review' is de facto equally intrusive as substantive review, because the WTO bodies are not simply interested in due process questions but also analyzing the appropriateness of the scientific methodologies on the basis of which WTO members took the challenged regulatory decisions.

⁹³⁶ Ibid., p. 7.

⁹³⁷ Idem.

⁹³⁸ Ibid., p. 17.

⁹³⁹ Ibid., p. 314. See also Robert Howse, 'From Politics to Technocracy - and Back Again: the Fate of the Multilateral Trading Regime', 96 *American Journal of International Law* (2002), pp. 94-117, at 102 ff.

⁹⁴⁰ Ibid., p. 8.

His broader point is that proposals that seek to ensure that non-economic public values are given more weight in and around the WTO regime are bound to fail unless the neoliberalist assumptions which form the ideational basis of the regime are brought into the open, recognized and challenged with a set of new assumptions. Lang notes that while 'the distributive, environmental, or social costs of international trade liberalization' have received relatively little attention within the WTO, this is not because such matters are considered unimportant, 'but because such matters are not considered appropriate topics of conversation given the limited purpose of international economic governance, as redefined within the neoliberal imagination'.⁹⁴¹ Rather, these are matters that are 'more appropriately addressed at the domestic level, or in other venues and regimes of international governance'.⁹⁴² As noted, Lang sees this mindset as stemming from the underlying neoliberal paradigm, and for him only by moving away from basic neoliberal assumptions can non-economic values receive broader recognition within the WTO. Hence, the WTO critics should focus more on redirecting the debate to 'the collective purposes of global trade governance' and less on the 'institutional and procedural structures' governing world trade.⁹⁴³

This sounds very familiar. The critics of investment treaties are also arguing that arbitral tribunals intrude illegitimately into the domestic political process by determining the appropriateness of a wide variety of regulatory measures. Since domestic policy-making entails value choices, such decisions should be left to the discretion of domestic institutions rather than of arbitral tribunals. If Lang considers that institutional and procedural reforms are unlikely to lead to the kind of changes the WTO critics were seeking, the same concern is expressed by those who see the reform proposals of the investment treaty regime as not remedying its casting defect, namely, the ability of arbitral tribunals to review domestic policy measures in the first place. On a more general level, Lang's account of how an ideational change toward neoliberalism had systemic and concrete consequences for WTO decision-making resembles the ideational order under which the proponents of investment treaties and arbitration evaluate state-market relations. As repeatedly noted, the proponents understand that the role of arbitrators is to determine what is reasonably acceptable government conduct in a market economy. While arbitral

⁹⁴¹ *Ibid.*, p. 10.

⁹⁴² *Idem.*

⁹⁴³ *Ibid.*, p. 11.

tribunals are increasingly taking account of the public interest, this does not mean that they defer to it in a manner that would appease the critics, even if the applicable protection standards become less indeterminate, because the critics are trying to ensure that the domestic polity gets back what shouldn't have been taken away in the first place, that is, its regulatory autonomy. In this light, the Commission's central reform proposals - safeguarding the right to regulate and the new investment court system - cannot lead to a fundamental attitudinal change in the mindset of the judges who interpret the 'next generation' investment protection provisions. Their task is still to provide a full review of domestic measures in light of the refined *investment protection* standards.

Lang also notes that the more fundamental problem with the WTO reforms is that they hide from sight the fact that regulatory autonomy is 'itself something of an illusion in contemporary conditions'. He continues:

'It is apparent that states' regulatory freedom is already constrained by international economic structures, and to a significant extent is subject to the logics of those structures. It is no longer possible to imagine a world in which sovereign states pursue regulatory policies and choices entirely free of the constraining and constitutive influences of the global economic structures in which they are embedded. Even in the absence of international economic law, states could not simply regulate freely without having regard to the potential reactions of foreign actors, both public and private - on which they may rely for investment, aid, and access to foreign markets for both capital and goods, and to whose coercive pressures they may in practice be subject. Moreover, states regulate in response to political and economic pressures which are themselves deeply shaped by the structure and operation of the global economy, and indeed of international economic law.'⁹⁴⁴

In other words, the idea that states would be capable of determining for themselves the model of state-market relations according to their preferences is a pipedream. The proponents of the investment treaty regime would probably argue that Lang's description is both correct and normatively desirable. The benefits of economic globalization depend on

⁹⁴⁴ Ibid., p. 344.

an open and global marketplace, and an ever deeper and broader economic integration process guarantees that the benefits continue to trickle-down. The propensity of host states to make policy on populist grounds necessitates a neutral dispute-settlement venue that pays due consideration to the economic interests of the investor (and of the host state as the case may be). Those with a more moderate view of the investment treaty regime would probably endorse Lang's description, but also think that the Commission's reform proposals are a step in the right direction, however modest their impact may be in light of the structural constraints imposed on domestic policy-making. The critics, in turn, would probably say that the only way forward is to wipe out the investment treaty regime so as to remove one external constraint from the domestic political process. In their view, it is *impossible* to create an investment protection mechanism that honors the 'sanctity' of the domestic political process, because the fundamental purpose of investment protection is to create an *external* review mechanism. Malmström's references to 'we' in the statement that defended the investment court system seem naïve in light of the distance that prevails between the Commission's rhetoric and the political concerns of the critics. In Malmström's view, the investment court system '*will...benefit investors...[and the proposed] changes will create the trust that is needed by the general public, while encouraging investment*'.⁹⁴⁵

The managerialism that undergirds this quote is familiar from other Commission documents dealing with investment protection. The documents create a sense that the Commission has come more than half way to meet the critics' concerns, and that debating the matter further is futile and counterproductive, and based on a dubious political agenda that finds no support in European public opinion - it's time to move forward! Lang's proposed solution to the legitimacy crisis of the WTO was the 'reformulation of a legitimating collective purpose to ground the work of the trade regime, and as a consequence the generation of a substantive and meaningful discussion of what that purpose should be in the light of contemporary global challenges and competing normative priorities'. In other words, the primary goal is to 'pursue precisely the mode of governance that neoliberal thought made more difficult to achieve - the exercise of public power in international trade governance in pursuit of a collectively defined legitimating purpose, and a form of governing which does not shy away from the experience of moral

⁹⁴⁵ Malmström, 'Proposing an Investment Court System', supra note 930 (emphasis added).

responsibility for the full range of outcomes it produces'. Transposed to the present context, Lang's call for a collective purpose (upon which the debates on the investment treaty regime should be grounded) is something that the critics are also calling for, if in less explicit terms. It is not necessarily so that the critics are categorically against trade and investment liberalization per se, because these are abstract notions which are put into practice in different ways in different parts of the world. Rather, at least some of the critique may stem precisely from the loss of collective purpose that Lang describes. Economic rhetoric has permeated most aspects of social life, and moral and cultural meanings of community, work, and the marketplace have little room in public and political talk. Given this, it is not surprising that the sentiment that 'we' are no longer on the same boat is increasing also in western democracies, with the EU appearing as a distant and cold apparatus whose representatives claim to represent the European body politic without realizing their own privileged position within the 'ever closer union' and without appreciating the deep socio-economic, cultural, linguistic and political dividing lines that prevail in Europe.

The discussion in Chapters 4 and 5 showed that the ECJ will have some leeway in deciding the *Achmea* case. In his Opinion, Advocate General Wathelet noted how the EU membership was divided over the question whether intra-EU BITs are compatible with EU law. Austria, Finland, France, Germany and the Netherlands argued for compatibility, whereas eleven member states argued the opposite.⁹⁴⁶ The Advocate General noted that this division reflected the member states' different experiences of investment arbitration, with the first group having faced only a few or no investor claims and the second facing a much higher number of claims. He also observed that the purpose of intra-EU BITs is to 'encourage and attract foreign investment', and referred to a string of arbitral awards where the tribunals had emphasized how investment arbitration is 'an indispensable guarantee that encourages and protects investments'.⁹⁴⁷ The preceding discussion has shown that the empirical evidence on the correlation between BITs and investment flows is scant and somewhat inconclusive, but the studies that were concluded before the sharp rise in the number of investment claims show that investment treaties were not relevant for investment decisions, apart from isolated cases, because investors were largely unaware of

⁹⁴⁶ Case C-284/16, Opinion of Advocate General Wathelet, *supra* note 257, paras. 34-35. These were Cyprus, the Czech Republic, Estonia, Greece, Hungary, Italy, Latvia, Poland, Romania, the Slovak Republic and Spain.

⁹⁴⁷ *Ibid.*, paras. 76-77.

the treaties' existence and potential until the attendant public and political debate became more widespread.⁹⁴⁸ Poulsen has also demonstrated how developing country officials in charge of investment treaty negotiations were 'neither aware of the costs' or of the fact that the treaties 'could lead to arbitration' in the first place.⁹⁴⁹ The Advocate General is of course entitled to his opinion but it reflects rather poorly the historical record, and also ignores the critique that centers on the procedural and substantive provisions of old-fashioned BITs (including intra-EU BITs) under which investors continue to raise claims on a steady pace. The Advocate General framed the object and purpose of intra-EU BITs by pointing to their perceived necessity in the immediate post-Communist era when the formerly socialist states were still unfamiliar with the basic tenets of the rule of law. The Commission made this precise argument during the oral hearings, but the Advocate General dismissed it by arguing that if intra-EU BITs were only meant to remain in force until EU accession, the Commission should have ensured that the accession treaties had provided for the termination of intra-EU BITs.⁹⁵⁰ However, a more commonsensical argument is that the Commission failed to register entirely the scenario where investors challenge domestic measures that relate to the requirements of EU law. Given that EU law and BITs share a similar ethos in that they oppose anti-competitive conduct and promote market-oriented reforms, it would not be surprising if the Commission's staff failed to appreciate their potential threat to fundamental principles of EU law. Moreover, most intra-EU BITs were concluded well before 2000. For example, when Romania signed its association agreement in 1993, in which it was encouraged to conclude BITs, the overall number of BIT claims was less than ten, with most stakeholders being entirely unaware of the implications of investment treaties, as Poulsen's study convincingly demonstrates.

In this light, the ECJ could send a signal of 'mutual trust' or collective purpose by declaring that intra-EU BITs are incompatible with the founding treaties. Since the economic arguments for investment treaties and arbitration are less than compelling, and since there is no evidence that foreign investors are treated arbitrarily within the EU, the Court could point out that intra-EU BITs no longer serve the purpose with which their conclusion was justified, and the different treatment they bring about has no other objective justification either. A finding that intra-EU BITs constitute prohibited discrimination would make it

⁹⁴⁸ See Lauge N. Skovgaard Poulsen, *Bounded Rationality and Economic Diplomacy. The Politics of Investment Treaties in Developing Countries* (Cambridge University Press, 2015), pp.7-9.

⁹⁴⁹ *Ibid.*, p. 105 (quoting a Czech official).

⁹⁵⁰ Case C-284/16, Opinion of Advocate General Wathelet, *supra* note 257, paras. 40-41.

unnecessary for the Court to address the other preliminary questions concerning its exclusive jurisdiction and the autonomy of EU law. Given that the Court will have to address those questions in relation to the Belgium's request for an opinion on the investment court system, the Court could take a deep breath and engage in a more comprehensive analysis of the pros and cons of investment treaties, and then provide an answer that relies (implicitly) on a political vision of the EU that takes more seriously the values upon which the Union claims to have built itself and that recognizes the implications of the value choices it makes.

Epilogue

According to a recent report made under the leadership of research centers at Yale and Columbia University, Finland was ranked the 'greenest' country in the world.⁹⁵¹ Finland's top ranking was based on its 'commitment to achieve carbon-neutral society that does not exceed nature's carrying capacity by 2050'.⁹⁵² An even more recent news story reported how an informal partnership between the Finnish government, Finnish MEPs, Finnish ministry officials, and unions representing Finnish industries had engaged in a lengthy and successful lobbying campaign so as to amend the Commission's proposal for a regulation on the inclusion of greenhouse gas emissions from land use, land use change and forestry (LULUCF) into the EU's 2030 climate and energy framework. The idea behind the LULUCF regulation was that all business sectors should contribute to the EU's 2030 emission reduction target. Just before the European Parliament's (EP) vote on the regulation, an amendment proposal was put forward on the initiative of a Finnish MEP, which excluded references to how logging should be taken account of when country-specific reduction targets are measured. The EP accepted the amendment proposal by a narrow margin, with the Finnish government seeing the vote as promoting the Finnish national interest. Promotion of the bioeconomy is a top priority of the Finnish government, and increasing logging is perceived as central to ensuring an adequate and steady supply of biomasses for the relevant domestic industries. Environmental organizations were less enthusiastic. In their view, increasing logging in the next ten to fifteen years means that Finland's carbon sink will shrink, as its forests absorb less emissions than previously. Since combatting climate change requires immediate and comprehensive action, the watered-down version of the LULUCF regulation is perceived as a myopic special interest measure that sends an entirely wrong message to countries such as Brazil and Indonesia where the majority of the world's rainforests are located (and where illegal logging is a huge problem).

The Finnish government also subsidizes energy-intensive industries and production of peat energy with hundreds of millions of euros annually, although there is undisputed empirical evidence that the former have no impact on the competitiveness of the beneficiary companies (the publicly stated aim of the aid), and although the combustion of peat creates

⁹⁵¹ A. Hsu et al., *2016 Environmental Performance Index* (Yale University, 2016).

⁹⁵² See Finland Promotion Board, *Finland in International Rankings and Comparisons* (2017).

far more greenhouse gas emissions than coal.⁹⁵³ Likewise, in mid-April 2017, the Finnish branch of World Wide Fund for Nature announced that Finland's resource consumption in the first three and half months of 2017 had exceeded the earth's capacity to produce resources for the whole year of 2017. In other words, if other states' resource consumption would reach the same level as Finland's, humanity's ecological debt to earth, in respect of 2017 alone, would start to accumulate from mid-April onward. At the global level, while climate scientists are warning that the earth's life-support systems are being damaged in ways that may threaten humanity's survival, global carbon emissions from fossil fuels, for example, show no sign of abating. A recent study estimated that global fossil fuel subsidies in 2015 amounted to \$5.3 trillion, with coal subsidies accounting for about half of them.⁹⁵⁴ If the existence of regulatory chill was difficult to substantiate in the context of investment treaties, the above anecdotes point that regulatory chill manifests itself in many shapes and forms. Academic arm-wrestling over the future of the investment treaty regime consumes resources and time, provides financial and travel opportunities to the debate's participants,⁹⁵⁵ but it is difficult to tell whether it has any relevance for the resolution of the concerns that animate the debate. If the discrepancy between the normative ideals of scholarship and social reality starts to feel too wide, and if those ideals nonetheless feel important, it is best to reconsider how to use one's limited energies and resources.

⁹⁵³ See Päivi Isotalus, 'VATT: Suuryritykset saavat energiatukea turhaan', *Kauppalehti*, 21 June 2016; Fionnuala Murphy, Ger Devlin and Kevin McDonnell, 'Benchmarking Environmental Impacts of Peat Use for Electricity Generation in Ireland - A Life Cycle Assessment', 7 *Sustainability* (2015), pp. 6376-6393.

⁹⁵⁴ David Coady, Ian Parry, Louis Sears and Baoping Shang, 'How Large are Global Fossil Fuel Subsidies?', 91 *World Development* (2017), pp. 11-27.

⁹⁵⁵ See Lauge N. Skovgaard Poulsen and Emma Aisbett, 'Diplomats Want Treaties: Diplomatic Agendas and Perks in the Investment Regime', 7 *Journal of International Dispute Settlement* (2016), pp. 72-91.

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