



Volume 12

Issue 1 *Symposium on the Law and Politics of Foreign Investment*

Article 7

1-17-2014

The Future Direction of Investment Agreements in the European Union

Mark A. Clodfelter

Follow this and additional works at: <http://digitalcommons.law.scu.edu/scujil>

Recommended Citation

Mark A. Clodfelter, *The Future Direction of Investment Agreements in the European Union*, 12 SANTA CLARA J. INT'L L. 159 (2014).
Available at: <http://digitalcommons.law.scu.edu/scujil/vol12/iss1/7>

This Article is brought to you for free and open access by the Journals at Santa Clara Law Digital Commons. It has been accepted for inclusion in Santa Clara Journal of International Law by an authorized administrator of Santa Clara Law Digital Commons. For more information, please contact sculawlibrarian@gmail.com.

The Future Direction of Investment Agreements in the European Union

Mark A. Clodfelter*

* Mark A. Clodfelter is a Partner with the Washington, D.C. office of Foley Hoag LLP where he specializes in investor-State arbitration. From 2000-2007, he served as Assistant Legal Adviser for International Claims and Investment Disputes, where he led the defense of the United States against claims under NAFTA's investment chapter and helped draft the 2004 US Model bilateral investment treaty. From 1993-1999, he was an Adjunct Professor of Law at the Georgetown Law Center, where he taught a graduate law course on international commercial arbitration. He has served as an arbitrator in investment treaty and international commercial cases and is a member of the ICSID Panel of Arbitrators, the Panel of Arbitrators of the Kuala Lumpur Regional Centre for Arbitration and the International Roster of Neutrals of the International Center on Dispute Resolution (ICDR). He may be contacted at mclodfelter@foleyhoag.com. The author wishes to thank Dr. Constantinos Salonidis for his comments.

TABLE OF CONTENTS

I. Standards of Protection and Treatment	162
II. Investor-State Dispute Settlement	171
III. Intra-EU BITs	177
IV. Conclusion.....	182

First, I would like to express my appreciation both to the Santa Clara University School of Law, for inviting Prof. Reinisch to present on this important subject, and to Prof. Reinisch himself, for his comprehensive survey of where things stand and where things may be going in the European Union with respect to international investment protection. Obviously, I am also grateful for this opportunity to comment on Prof. Reinisch's paper.

As his paper makes clear, the new EU competence over foreign direct investment presents EU decision makers in all of the EU institutions with a multitude of issues and all of them are difficult.

To US lawyers these issues may seem unnecessarily complicated. For the US federal system, these questions are settled by the US Constitution. Internally, we have a single citizenship, total freedom of movement of capital and universal constitutional protections, including equal protection under law. Externally, our constitutional protections extend to foreign investors, the central government enjoys exclusive power in the area of foreign affairs and the executed central government's international undertakings enjoy superiority over the laws of all political subdivisions. As a result, the issues emerging from the EU's new competence were more or less resolved long ago among the fifty United (including the thirteen formerly sovereign) States of America.

But, as was frequently pointed out by the late Prof. Eric Stein, under whom I had the honor of studying then-EC law at the University of Michigan, such problems are an order of magnitude more complicated for Europe, with its mixed sovereignty, different citizenships, wide differences in levels of development and what I see as a broader array of political viewpoints to be accommodated.

So there are real challenges ahead in formulating EU policy under Articles 206 and 207 of the Treaty on the Functioning of the European Union ("TFEU")¹ and Prof. Reinisch's paper succinctly highlights the major ones. Meeting these challenges will be all the more complicated by the newly invigorated role that the European Parliament enjoys in approving any future EU investment treaties, as well as by the increasingly institution-protective influence that the Court of Justice of the European Union ("CJEU") will inevitably have in defining limits to those treaties.

I would like to comment on three of the areas of challenge touched upon by Prof. Reinisch. In particular:

1. What substantive standards are likely to be included in future investment agreements entered into by the EU?
2. What considerations are likely to apply in the design of investor-State dispute settlement ("ISDS") mechanisms?

1. Consolidated Version of the Treaty on the Functioning of the European Union, May 9, 2008, 2008 O.J. (C 115) 47, 93-94 [hereinafter TFEU], available at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2008:115:0047:0199:EN:PDF>.

3. Is there a place for bilateral investment treaties between Member States (“intra-EU BITs”) and what will become of them?

Prof. Reinisch assesses the evidence accessible at the time of his paper, including the “scarce proposals available and some informally leaked documents from the negotiating process,”² to venture predictions of likely outcomes on each of these issues, as well as others, and he is to be commended for his bravery in this endeavor. It is certainly difficult to convincingly second-guess his well thought out prognostications. At the same time, it is possible to read that evidence in different ways, as I do, and fast moving developments on these topics since his paper suggest even more that we may expect different directions to be taken by the EU than he considered most likely.

On each of these issues, the roles of the European Parliament and the CJEU are recognized as taking on an increased importance, and positions of the Commission and Council may be shifting. Moreover, a great deal of new evidence has emerged that provides an even clearer picture than was possible when Prof. Reinisch wrote. In my comments, I will refer to the many new discussions of positions by EU institutions resulting from additional leaked negotiating documents, from the further attention to the Commission’s proposal for a framework for allocating financial responsibility for ISDS awards³ and from the recently approved mandate for the Commission to negotiate a free trade agreement with the United States.⁴

I. Standards of Protection and Treatment

Substantive standards of protection/treatment are at the core of international investment agreements, and their specific wording has immense implications for the impact that such agreements have on the State parties involved and their investors. During the “modern era” of investor-State arbitration, roughly from 1998 to the present, a number of the awards that have been rendered on investor treaty claims, often to the great dissatisfaction of the States involved, have given a clearer picture of the risks posed by such provisions. Many of these awards have involved disputes under international investment agreements (“IIAs”) to which an EU Member State is a party and which have

2. August Reinisch, *The EU on the Investment Path Quo Vadis Europe? The Future of EU BITs and other Investment Agreements*, 8 SANTA CLARA J. OF INT’L L. 111 (2013).

3. *Id.* at 119 n.19 (citing *Proposal for a Regulation of the European Parliament and of the Council Establishing a Framework for Managing Financial Responsibility Linked to Investor-State Dispute Settlement Tribunals Established by International Agreements to Which the European Union is Party*, COM (2012) 335 final (June 21, 2012) [hereinafter European Commission Proposal], available at http://trade.ec.europa.eu/doclib/docs/2012/june/tradoc_149567.pdf).

4. Press Release, 3245th Council Meeting, Foreign Affairs Trade, Luxembourg Council of the E.U., 10862/13 (June 14, 2013), available at http://www.consilium.europa.eu/ueDocs/cms_Data/docs/pressData/EN/foraff/137486.pdf.

traditionally used broadly worded language to describe the substantive protections and treatment that the investors are provided.

Prof. Reinisch sees strong evidence that IIAs negotiated by the EU under its new competence will follow the route taken in Member State BITs including the broad standards they traditionally employ. This evidence includes the 2010 Commission Communication “Towards a comprehensive European international investment policy” which “repeatedly mentions member State BIT provisions ‘that should inspire the negotiation of investment agreements at the EU level.’”⁵ It also includes the Council’s instructions for on-going negotiations on comprehensive trade agreements with Canada, India and Singapore, which he sees as reflecting in their comments on the investment chapters to be included a Council preference for a “traditional ‘European’ approach of strong investment protection including ISDS.”⁶

Prof. Reinisch does acknowledge that, based upon its 6 April 2011 resolution, “On the future of European international investment policy,” the European Parliament “appears much more reluctant towards the traditional strong investor protection contained in many European BITs” and is “much more nuanced, if not reserved, than that of the two other main EU institutions.”⁷ But this may understate the divide that then existed between the Parliament and the other EU institutions. It is possible to see this evidence, and more recent indications, as pointing to standards emerging from EU action that will diverge greatly from the more open-ended language of contemporary Member State BITs, and more closely resemble those adopted by the North American States.

First, consider that the term “standards of protection” is just one side of the coin; the same language defines “standards of liability” as well. This vantage point changes the perspective of the decision-maker considering treaty language. This is clear in the concerns expressed in the European Parliament’s 2011 resolution, which includes the following observations:

G. whereas after the first dispute settlement cases of the 1990s, and in spite of generally positive experiences, a number of problems became clear because of the use of vague language in agreements being left open for interpretation, particularly

-
5. Reinisch, *supra* note 2, at 124 (citing *Communication from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions: Towards a Comprehensive European International Investment Policy*, COM (2010) 343 final (July 7, 2010) [hereinafter 2010 Commission Communication], available at http://trade.ec.europa.eu/doclib/docs/2010/july/tradoc_146307.pdf).
 6. Reinisch, *supra* note 2, at 122. See also Reinisch, *supra* note 2, at 122-23 nn. 37 & 49 (citing *Council Negotiating Directives (2011, EU-Canada/India/Singapore FTAs)*, BILATERALS.ORG, (Sept. 15, 2011), available at <http://www.bilaterals.org/spip.php?article20272&lang=en>).
 7. Reinisch, *supra* note 2, at 122; see also Reinisch, *supra* note 2, at 121 n. 31 (citing *European International Investment Policy: European Parliament Resolution of 6 April 2011 on the Future European International Investment Policy (2010/2203(INI))*, Oct. 2, 2012, 2012 O.J. (C 296) [hereinafter 2011 Parliament Resolution], available at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2012:296E:0034:0040:EN:PDF>).

concerning the possibility of conflict between private interests and the regulatory tasks of public authorities, for example in cases where the adoption of legitimate legislation led to a state being condemned by international arbitrators for a breach of the principle of 'fair and equitable treatment,' [and]

H. whereas the USA and Canada, which were among the first states to face such rulings, have adapted their model BITs in order to restrict the breadth of interpretation by the arbitration and ensure better protection of their public intervention domain.⁸

The Parliament was looking at the prospect of EU treaties as not only providing for protection of EU investors abroad, but as creating liability for the EU and Member States that might impede public authorities from carrying out regulatory tasks. It is clear that this anxiety stems not only from commonly expressed civil society concerns regarding the environment, sustainable development and public health, but also from an acute appreciation of the actual decisions that have emanated from arbitral tribunals since the 1990's. These years of experience have only lightly touched the major capital-exporting states of the EU, which have not been the targets of many investor claims. But this is changing as we now see claims challenging Germany's shift away from nuclear power⁹ and, perhaps even more importantly, claims now emerging challenging actions taken by states in reaction to the fiscal crisis of 2008-09 in Belgium¹⁰ and, more recently, in Greece¹¹ and Cyprus.¹²

As a result of its concerns, the Parliament's resolution expressly "call[ed] on the Commission to produce clear definitions of investor protection standards in order to avoid" overly broad interpretations inconsistent with "legitimate public regulations."¹³ The resolution specifically urged, for example, that any requirement for fair and equitable treatment be "defined on the basis of the level of treatment established by international customary law," and that provisions regarding expropriation be given "a definition that establishes a clear and fair balance between public welfare objectives and private interests."¹⁴ It expressed similar concerns regarding national treatment and most favored nation treatment.¹⁵ It also asked the Commission "to assess the potential

8. 2011 Parliament Resolution, *supra* note 7, pmb1.

9. *Vattenfall AB and others v. Federal Republic of Germany*, ICSID Case No. ARB/12/12, (status of proceeding Pending registered May 31, 2012) (on file with ICSID).

10. *Ping An Life Insurance Company of China, Limited and Ping An Insurance (Group) Company of China, Limited v. Kingdom of Belgium*, ICSID Case No. ARB/12/29, (status of Proceeding is pending, registered Sept. 19, 2012) (on file with ICSID). The author wishes to disclose that his firm represents Belgium in this matter.

11. *Poštová banka, a.s. and ISTROKAPITAL SE v. Hellenic Republic*, ICSID Case No. ARB/13/8, (status of proceeding is pending, registered May 20, 2013) (on file with ICSID).

12. *Marfin Investment Group v. The Republic of Cyprus*, Notice of Dispute (Jan. 23, 2013) (not public).

13. Reinisch, *supra* note 2, at 132 (citing 2011 Parliament Resolution, *supra* note 7, ¶ 24).

14. 2011 Parliament Resolution, *supra* note 7, ¶ 19.

15. 2011 Parliament Resolution, *supra* note 7, ¶ 19.

impact of the inclusion of an umbrella-clause in future European investment agreements.”¹⁶

The Commission and the Council initially gave the Parliament’s concerns on these issues short shrift. Their immediate responses were more consistent with the “traditional approach” than with a reappraisal and revision like that advocated in the Parliament’s resolution. The Commission did state that it “could” explore the possibility of adopting language that “would possibly express in more explicit terms the common understanding of the EU and its negotiating partners as to the scope of the obligations enshrined in the agreed standards.”¹⁷ At the same time, however, it maintained that there was a “common understanding among experts in the field (lawyers, academics, arbitrators, judges) with respect to [the] content and meaning” of BIT standards and strongly defended the “subjective element” of arbitrators’ interpretation of standards as permitting the “flexibility” necessary for the application of the standards in specific situations.¹⁸

And while the Council’s leaked directions for negotiations on comprehensive trade agreements for the Canada, India, and Singapore specified that standards “shall be without prejudice to the right of the EU and the Member States to adopt and enforce, in accordance with their respective competences, measures necessary to pursue legitimate public policy objectives such as social, environmental, security, public health and safety in a non-discriminatory manner,” its targets for fair and equitable treatment (“FET”) and expropriation include no limitations.¹⁹ In this manner, as Prof. Reinisch points out that, “the instructions appear to favour the traditional European approach by adhering to a rather concise treaty text, without clarifications limiting the scope of FET and indirect expropriation as they are known from US and Canadian BITs as well as NAFTA” and thereby avoid “NAFTA-contamination.”²⁰

-
16. 2011 Parliament Resolution, *supra* note 7, ¶ 20.
 17. Follow Up to the European Parliament Resolution on the Future European International Investment Policy, Adopted by the Commission on 5 July 2011, EUR. PARL. DOC. P7-TA-PROV(2011)0141 5 (2011), available at www.europarl.europa.eu/oeil/spdoc.do?i=19829&j=0&l=en
 18. *Id.* at 4-5.
 19. General Affairs Council, *EU Negotiating Mandates on Investment (2011, EU-Canada/India/Singapore FTAs)*, BILATERALS.ORG (Sept. 15, 2011), <http://www.bilaterals.org/spip.php?article20272&lang=en> (publishing leaked “text of the negotiating mandates approved by the General Affairs Council for investment protection chapters in free trade agreements of the EU with Canada, India and Singapore”).
 20. Reinisch, *supra* note 2, at 123 (citing Luke E. Peterson, *EU Member-States Approve Negotiating Guidelines for India, Singapore and Canada Investment Protection Talks; Some European Governments Fear “NAFTA-Contamination*, INVESTMENT ARBITRATION REPORTER (Sept. 23, 2011), http://www.iareporter.com/articles/20110923_2 (article available through subscription or purchase).

The underlying issue of “NAFTA-contamination” is the tendency of North American States to laden their modern IIAs with qualifications and explanations designed to accomplish the regulatory space they saw as having been threatened by some of the early awards of NAFTA investor-State arbitral tribunals. Famously, these qualifications and explanations include innovative language incorporated in the 2004 US Model BIT. The language resulted after a prolonged attempt by US officials to find formulas for expressing the operational standards that would provide a real measure of protection for US investors abroad while cabining State liability and carving out the kinds of measures that even capital-exporting countries take for granted that they may employ to protect the public interest. As a direct participant in this effort, specifically head of the US State Department’s office in charge of international claims and investment disputes, I can testify that, after a monumental effort, this noble goal proved elusive and the drafters had to settle for explanatory language, exceptions, and even admonitions to future arbitral tribunals.

For example, rather than using language that would expressly define conduct considered to be inconsistent with acceptable conceptions of fair and equitable treatment, the 2004 US Model BIT requires “treatment in accordance with customary international law, *including* fair and equitable treatment and full protection and security,” stating that this means only “the customary international law *minimum standard of treatment* of aliens.”²¹ It then specifies the obligation not to deny justice as a single example of what the customary international law minimum standard includes.²² Previously, the US had stated its view that the international minimum standard of treatment is comprised of sets of rules pre-existing in the customary international law.²³ Thus, in contrast to application by arbitral tribunals of FET provisions not tied to customary international law, the 2004 US Model BIT’s concept of FET, as merely a referent to the pre-existing minimum standard of treatment, truly would clearly seem to “have the potential to

21. Treaty Between the Government of the United States of America and the Government of [Country] Concerning the Encouragement and Reciprocal Protection of Investment, *available at* <http://www.state.gov/documents/organization/117601.pdf> [hereinafter 2004 Model BIT].

22. *See id.* art. 5(2)(a).

23. *See, e.g.,* ADF Group Inc. v. United States of America ICSID Case No. ARB(AF)/00/1, Post-Hearing Submission of Respondent, (June 27, 2002), 6-7 ICSID Rep. 470 (2004), *available at* <http://www.state.gov/documents/organization/11662.pdf> (“The ‘international minimum standard’ embraced by Article 1105(1) is an umbrella concept incorporating a set of rules that over the centuries have crystallized into customary international law in specific contexts. The treaty term ‘fair and equitable treatment’ refers to the customary international law minimum standard of treatment. The rules grouped under the heading of the international minimum standard include those for denial of justice, expropriation and other acts subject to an absolute, minimum standard of treatment under customary international law.”) (citations omitted) (The author wishes to disclose that he was counsel for the United States in connection with this case.).

considerably lower the level of investor protection and, conversely, increase the regulatory discretion of host states.”²⁴

The difficulty of articulating a clear operational definition of indirect expropriation provides another example of how the 2004 US Model BIT had to settle for elaborations and explanations to convey meaningful protection within desired limits. *First*, it proposes that future signatory states expressly “confirm their shared understanding” that the model’s expropriation provisions are “intended to reflect customary international law concerning the obligation of States with respect to expropriation.”²⁵ *Second*, it provides that the case-by-case analysis needed to determine an indirect expropriation must be based upon a consideration of three factors, borrowed from the US Supreme Court’s famous *Penn Central*²⁶ test, namely, “(i) the economic impact of the government action . . . ,” admonishing that an adverse effect on economic value alone does not establish an indirect expropriation; “(ii) the extent to which the government action interferes with distinct, reasonable investment-backed expectations; and (iii) the character of the government action.”²⁷ *Third*, it includes a declaration, intended as guidance for future arbitral tribunals, that “[e]xcept in rare circumstances, non-discriminatory regulatory actions by a Party that are designed and applied to protect legitimate public welfare objectives, such as public health, safety, and the environment, do not constitute indirect expropriations.”²⁸

Finally, in lieu of an umbrella clause, the 2004 US Model BIT provides that its investor-State dispute settlement provisions applicable to breaches of the substantive standards of the model shall also apply to alleged breaches of any “investment agreement,”²⁹ defined narrowly as an agreement with national authorities with respect to natural resources development, the supply of public utilities and infrastructure projects.³⁰

The determination of some Member States acting through the Council to immunize the EU from NAFTA-contamination and pursue what Prof. Reinisch describes as “traditional” European approaches to standards of protection and treatment³¹ was carried through deep into negotiations with Canada, with the EU holding to a conception of FET untethered to customary international law, an extremely narrow exception to the expropriatory effect of regulatory actions and to a broad umbrella clause.³²

24. Reinisch, *supra* note 2, at 130.

25. 2004 Model BIT, *supra* note 21, annex B, 1.

26. *Penn Cent. Transp. Co. v. City of New York*, 438 U.S. 104, 124 (1978).

27. 2004 Model BIT, *supra* note 21, annex B, 4(a)(i)-(ii).

28. *Id.* annex B, 4(b).

29. *See id.* art. 26.

30. *Id.* section A.

31. *See* Reinisch, *supra* note 2, at 117, 123.

32. *Canada-EU CETA Draft Consolidated Text – February 2012*, WORLD TRADE ONLINE 15-16, 18-19 (Feb. 2012), available at <http://www.tradejustice.ca/wp-content/uploads/2013/10/CETA-Text->

However, the European Parliament does not appear ready to cede the issue to the other institutions. In May 2013, after debating the Commission's proposal for a framework for allocating financial responsibility for ISDS awards,³³ the Parliament adopted a series of amendments at odds with both the Council and the Commission.³⁴ One amendment drew a direct link between the question of financial responsibility and the breadth of treaty standards, noting that "[f]inancial responsibility cannot be properly managed if the standards of protection afforded in investment agreements were to exceed significantly the limits of liability recognized in the Union and the majority of the Member States."³⁵ Accordingly, it recommended that future treaties should afford "no higher level of protection than Union law and the general principles common to the laws of the Member States grant to investors from within the Union."³⁶ Another amendment declared that "the Union's liability for legislative acts, especially in the interaction with international law, must be framed narrowly and cannot be engaged without the clear establishment of fault."³⁷

The Parliament's latest remonstrations are clearly having an impact. Indeed, during the debate over the Commission's proposal, the Commission responded to questions by offering reassurances "that the level of investment protection afforded by future investment agreements to foreign investors will be in line with general principles common to EU and Member State law . . . [and] in line with the best practices of EU Member States."³⁸ This represents a subtle but significant shift on previous formulations that called for new treaties to be based upon "Member States' experience and best

February-2012.doc (article available through subscription or purchase) (publishing leaked text pertaining to "secret negotiating process of the Canada-European Union free trade negotiations (CETA)").

33. See generally *European Commission Proposal*, supra note 3; see generally Responsibility in Investor-State-Arbitration in the EU, EUR. PARL. DOC. PE 457.125 (2012), available at <http://www.europarl.europa.eu/committees/en/studiesdownload.html?languageDocument=EN&file=79450> (setting forth results of a study commissioned by the European Parliament's Committee on International Trade, upon which Parliament, in part, based its amendments); see generally Jan Kleinheisterkamp, *Financial Responsibility in the European International Investment Policy*, (LSE Law, Society and Economy Working Paper Series, Paper No. 15/2013, 2013), available at <http://dx.doi.org/10.2139/ssrn.2271526>.
34. *Amendments Adopted by the European Parliament on 23 May 2013 on the Proposal for a Regulation of the European Parliament and of the Council Establishing a Framework for Managing Financial Responsibility Linked to Investor-State Dispute Settlement Tribunals Established by International Agreements to which the European Union is Party* (COM(2012) 0335 final (May 23, 2013), available at <http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//TEXT+TA+P7-TA-2013-0219+0+DOC+XML+V0//EN&language=EN>).
35. *Id.* amend. 4.
36. *Id.*
37. *Id.* amend. 5.
38. See Remarks of Commissioner De Gucht, EUR. PARL. DEB. (339) (May 22, 2013), available at <http://www.europarl.europa.eu/sides/getDoc.do?type=CRE&reference=20130522&secondRef=ITM-019&language=EN&ring=A7-2013-0124>.

practise regarding their bilateral investment agreements.”³⁹ The new formulation implies that it is the best practices of Member States’ law that is important, not the best practices of their investment treaties. Moreover, the Commission stated that it “is endeavouring to better clarify the content of our investment protection standards without reducing the level of protection, for example by including useful guidance on the practice of arbitral tribunals,”⁴⁰ signaling that, as had already been expressed by the Parliament, the decisions of arbitral tribunals on traditional standards have to be taken into account in the design of future standards.

On the ground, developments also point to a shift in the EU negotiating positions. For example, it appears that the disavowal of any connection between FET and the customary international law minimum standard of treatment that reflected the EU’s opening position with Canada⁴¹ has given way to at least a partial connection.⁴² This perhaps should not be seen as such difficult step for the EU to take given the strong roots that such a connection has in the history of European BITs, originally based as they were on the OECD Draft Convention on the Protection of Foreign Property.⁴³ That Convention, drafted in 1962 and approved by the OECD in 1967,⁴⁴ made express the fact

39. *EU Negotiating Mandates*, *supra* note 19.

40. See Commissioner De Gucht in the Plenary debate in the European Parliament on May 22, 2013, *supra* note 38.

41. See Canada-EU CETA Draft Consolidated Text – February 2012, *supra* note 32.

42. See *EU, Canada Approach to Investment Could Have Mixed Impact on U.S. Talks*, WORLD TRADE ONLINE (June 28, 2013), <http://insidetrade.com/Inside-US-Trade/Inside-U.S.-Trade-06/28/2013/eu-canada-approach-to-investment-could-have-mixed-impact-on-us-talks/menu-id-710.html> (article available through subscription or purchase). (“A confidential text on the investment provisions of the Canada-European Union free trade agreement (CETA) shows that the two parties have broken new ground in defining the key concept of fair and equitable treatment for investors. The language that they have agreed upon contains similarities but also differences to the approach that the United States has taken in its investment deals, which could pose problems in the upcoming U.S.-EU trade and investment talks, according to copy obtained by Inside U.S. Trade. Moving closer to the U.S. negotiating stance, the EU has agreed to partially link a government’s obligation to accord fair and equitable treatment to investments with the concept of customary international law. It does so by stating a violation of the fair and equitable treatment under the CETA is any treatment contrary to the fair and equitable treatment obligation recognized by the general practice of states as accepted as law, which experts say is a clear reference to customary international law”). It should be noted that the EU has also announced that it will embark on negotiations with China. See Commission Proposal to Open Negotiations for an Investment Agreement with China ~~IP/13/458~~, COM (2013) 358 final (May 23, 2013), available at <http://trade.ec.europa.eu/doclib/press/index.cfm?id=900>. China’s prototype BIT does not link FET to customary international law. See People’s Republic of China, Agreement Concerning The Encouragement & Reciprocal Protection Of Investments [Prototype], art. 3(1), <http://unctad.org/sections/dite/ia/docs/Compendium/en/65%20volume%203.pdf>.

43. See UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT, BILATERAL INVESTMENT TREATIES IN THE MID-1990’S 54 (1998). (“The use of the standard of fair and equitable treatment in BITs dates from the OECD 1967 Draft Convention on the protection of Foreign Property.”).

44. ORGANISATION FOR ECON. CO-OPERATION & DEV. [OECD], DRAFT CONVENTION ON THE PROTECTION OF FOREIGN PROPERTY (1962) available at

that requirement of Article 1 to “ensure’ fair and equitable treatment of the property of the nationals of the other Parties,”⁴⁵ “conforms in effect to the ‘minimum standard’ which forms part of customary international law.”⁴⁶ It appears that, in this respect at least, the EU is merely catching up to its own heritage in accepting a more NAFTA-like approach in its negotiations with Canada; it will bear watching whether the EU will be forced to move even further in its talks with US.

Similar movement also appears to be developing with respect to expropriation standards. While the EU’s opening position with Canada had included guidance that superficially resembled the 2004 US Model BIT declaration regarding indirect expropriation, a leaked text from subsequent rounds of negotiations are reported to include a significant relaxation.⁴⁷ Whereas the opening text stated that a State’s non-discriminatory measures are subject to a straightforward proportionality test and are recognized to be non-expropriatory only if they are “necessary’ and applied in a way that “genuinely meet[s]” stated objectives, the new text apparently covers any such measure unless it is “so severe in light of its purpose that it appears manifestly excessive”; the proposed necessity and genuineness tests have been dropped.⁴⁸

Recent reports do not include information about a possible resolution of differences regarding the protection of contract rights and whether the EU is similarly relaxing its positions on umbrella clauses. However, it is noteworthy that the EU has intensified its

<http://www.oecd.org/investment/internationalinvestmentagreements/39286571.pdf>. The Draft Convention was prepared on the instruction of the OECD Council given in April 1960 and “[r]epresentatives and experts from fifteen countries Members of the latter Organisation participated in the work.” *Id.* at 1. The Draft Convention was adopted by a Resolution of the OECD Council, which “reaffirmed the adherence of the Member States to the principles of international law embodied in the draft,” including “the Notes and Comments constituting its interpretation.” See OECD, *Resolution of the Council on the Draft Convention on the Protection of Foreign Property*, at 2, Oct. 12, 1967), <http://www.oecd.org/investment/internationalinvestmentagreements/39286571.pdf>. Member State confirmed this understanding of FET in a survey conducted in 1984 according to which “all Member countries which have commented on this point, fair and equitable treatment introduced a substantive legal standard referring to general principles of international law even if this is not explicitly stated . . .” See OECD, COMMITTEE ON INTERNATIONAL INVESTMENT AND MULTINATIONAL ENTERPRISES, INTERGOVERNMENTAL AGREEMENTS RELATING TO INVESTMENT IN DEVELOPING COUNTRIES ¶ 36 AT 12 Doc. No 84/14 (May 27, 1984) cited in Y. Small, *Fair and Equitable Treatment Standard in International Investment Law*, in INTERNATIONAL INVESTMENT LAW: A CHANGING LANDSCAPE 97 (2005), available at <http://www.oecd.org/daf/inv/internationalinvestmentagreements/40077877.pdf>.

45. DRAFT CONVENTION ON THE PROTECTION OF FOREIGN PROPERTY, *supra* note 44, art 1.

46. DRAFT CONVENTION ON THE PROTECTION OF FOREIGN PROPERTY, *supra* note 44, art. 1 n.4(a).

47. See *Canada-EU CETA Draft Consolidated Text – February 2012* (Feb. 7, 2013), *supra* note 32, at 19.

48. See *CETA Investment Approach Has Similarities, Differences To U.S. Model*, WORLD TRADE ONLINE (Jun. 28, 2013), <http://insidetrade.com/Inside-US-Trade/Inside-U.S.-Trade-06/28/2013/ceta-investment-approach-has-similarities-differences-to-us-model/menu-id-710.html>. (article available through subscription or purchase).

efforts to have government procurement included in its negotiations with the US⁴⁹ since a potential conflict arises between these two aims. This is an area where tribunals have made widely varying holdings, but one line of cases has held that the umbrella clause – under which a State undertakes generally that it will fulfill all other obligations it has entered into with respect to an investment – elevates all contract disputes with the State into treaty disputes, and all contract breaches into treaty breaches.⁵⁰ Under this view, a treaty umbrella clause would trump EU Member State special mechanisms for the resolution of procurement disputes. It may well be that these two goals will collide in the course of negotiations.

Whatever its initial goals when it first began outlining its preferred positions on treatment and protection standards under its new competence over FDI, the EU appears to be reconciling itself to concerns expressed by the EU Parliament and long recognized by the North American States.⁵¹ Future EU BITs are likely to set the bar on prohibited State conduct much more carefully, and much more specifically, than have traditional EU Member State BITs.

II. Investor-State Dispute Settlement

The movement we have seen in the EU in recent months on standards of conduct and treatment are being matched by non-traditional thinking concerning dispute settlement. Indeed, the debate that has been engendered as the EU approaches the prospect of agreeing to arbitrate treaty claims with American investors is pointing in the direction of a fundamental re-examinations of dispute settlement institutions.

The “tradition” of EU BITs was built upon agreements between EU capital exporting Member States and countries that were essentially capital importers in the developing world. As a result, the exporting States saw little threat in waiving sovereign immunity and agreeing to arbitrate compliance of their own public decisions with international law principles, since it was unlikely that there would be many such tests. This was previously the same for the United States and Canada. But this all changed with NAFTA, which represents the first time that two countries with major bi-directional

49. *Id.* See also, *Mandate Shows EU Will Push On Financial Services Rules, Safeguard SPS*, WORLD TRADE ONLINE (Jun. 28, 2013), <http://insidetrade.com/Inside-US-Trade/Inside-U.S.-Trade-06/21/2013/mandate-shows-eu-will-push-on-financial-services-rules-safeguard-sps/menu-id-710.html>. (“The final mandate also makes clear that -- as EU trade officials have said on numerous occasions -- European negotiators will aim to secure market access commitments in the area of public procurement at all levels of government, including federal, regional and local.”)

50. *Eureko B.V. v. Republic of Poland*, NAFTA/UNCITRAL Trib., Partial Award, ¶ 232 (Aug. 19, 2005), *available at* <http://ita.law.uvic.ca/documents/Eureko-PartialAwardandDissentingOpinion.pdf>.

51. For critical recognition of this prospect, see Nikos Lavranos, *The New EU Investment Treaties: Convergence towards the NAFTA Model as the New Plurilateral Model BIT Text?*, (March 29, 2013), *available at* <http://ssrn.com/abstract=2241455> and <http://dx.doi.org/10.2139/ssrn.2241455>.

flows of investment have agreed to ISDS for related disputes. The US and Canada already had a trade agreement in place between them, but in seeking to include investment protection and bring Mexico into the arrangement, they were forced to add ISDS to address what were perceived to be concerns about the Mexican courts. The result has been that all of the numerous ISDS proceedings against Canada have been brought by US nationals, and all but one of the numerous ISDS proceedings against the US have been brought by Canadian nationals. This is clearly what is facing the EU in its efforts to strike trade deals with the Canada and the US that include investment protection; inevitably, numerous claims will be brought against them under any ISDS mechanism included in the resulting agreements.

Nonetheless, as Prof. Reinisch points out, after some initial reluctance, the EC eventually weighed in heavily in favor of including ISDS in future BITs entered into under its new competence.⁵² Moreover, despite its concerns with the latitude enjoyed by arbitrators under the ISDS system,⁵³ the Parliament also took “the view that, in addition to state-to-state dispute settlement procedures, investor-state procedures must also be applicable in order to secure comprehensive investment protection.”⁵⁴

The traditional approach to ISDS has been to import the commercial arbitration model into treaties. This has been a curious, and too little remarked upon, development. One cannot read the debates among the drafters of the ICSID Convention, for example, without realizing that they very much had in mind using ISDS primarily for contract disputes with States, a natural progression of commercial arbitration techniques.⁵⁵ Little debate was had on the implications of using the commercial model to resolve treaty claims for violations of international legal principles.⁵⁶

52. Reinisch, *supra* note 2 at 119 *citing* European Commission, Communication from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions, Towards a comprehensive European international investment policy, COM(2010) 343 final (Jul. 7, 2010).

53. 2011 Parliament Resolution, *supra* note 7, at para. 24 (“Expresses its deep concern regarding the level of discretion of international arbitrators to make a broad interpretation of investor protection clauses, thereby leading to the ruling out of legitimate public regulations; calls on the Commission to produce clear definitions of investor protection standards in order to avoid such problems in the new investment agreements.”).

54. *Id.*

55. *See generally*, ICSID, HISTORY OF THE ICSID CONVENTION: DOCUMENTS CONCERNING THE ORIGIN AND THE FORMULATION OF THE CONVENTION ON THE SETTLEMENT OF INVESTMENT DISPUTES BETWEEN STATES AND NATIONALS OF OTHER STATES, vols. I-IV, (1970).

56. Indeed, the Report of the Executive Directors on the draft convention makes no reference to treaties at all. *See* Convention on the Settlement of Investment Disputes between States and Nationals of Other States Report of the Executive Directions on the Convention on the Settlement of Investment Disputes between States and Nationals of Other States para 24, Mar. 18, 1965, *available at* https://icsid.worldbank.org/ICSID/StaticFiles/basicdoc/CRR_English-final.pdf (*reprinted in* Apr. 2006).

But the commercial arbitration model was designed to resolve unique, private contract disputes, principally because it was seen as faster, cheaper and more confidential than court proceedings. It relies upon private, generally part-time (and even only occasional) arbitrators from the private business sector, as opposed to public officials or judges. It gives both of these private disputing parties an equal role in selecting arbitrators. It affords arbitrators tremendous latitude in deciding claims with less than strict adherence to legal principles because their decisions are not subject to any meaningful review of legal holdings or factual findings.

These characteristics have served the commercial sector well, but are they equally appropriate for treaty claims, which involve a sovereign State party, the public interest, public policy decisions and repeated invocation of the same international law standards?

The greatest discomfort with the “fit” of commercial arbitration with treaty claims has been expressed with regard to (1) lack of transparency, which commercial arbitration’s emphasis on confidentiality entails, and (2) inconsistent decisions, a direct result of the decentralized nature of arbitration and the relative lack of review.

The EU institutions are all well aware of the transparency problem and have included means of addressing it in their design of EU investment protection policy. Prof. Reinisch points out how the Commission has led in proposing transparency measures,⁵⁷ including public access to requests for arbitration and other written submissions, open hearings, amicus curiae briefs and the publication of awards.⁵⁸ These objectives were all included in the leaked draft 2012 ISDS text the Commission developed for use in future EU BITs, and in the Canada, India and Singapore negotiations in particular.⁵⁹ Indeed, the Commission stated that “[t]he inclusion of effective rules on transparency is unavoidable.”⁶⁰

The more difficult problem is that of arbitral outcomes, of which inconsistency has been the main concern voiced. Criticisms based on the lack of consistency in ISDS usually frame the issue as one of impeding predictability and therefore efficiency of

57. Reinisch, *supra* note 2, at 135.

58. See 2010 Commission Communication, *supra* note 5, at 10.

59. See Text on investor state dispute settlement of EU agreements, Note for the Attention of the Trade Policy Committee (Services and Investment), art. 11 and Annex III, WORLD TRADE ONLINE (Jun. 5, 2012), http://insidetrade.com/iwpfile.html?file=apr2013%2Fwto2013_1036a.pdf. In particular, the draft text makes explicit reference to future incorporation by reference of the UNCITRAL Rules on Transparency in Treaty-based Investor-State Arbitration. Rep. of the United Nations Commission on International Trade Law, 46th Sess., 8-26 July 2013, U.N. DOC. A/CN.9/784 (Mar. 6, 2013), available at <http://www.uncitral.org/pdf/english/texts/arbitration/rules-on-transparency/pre-release-UNCITRAL-Rules-on-Transparency.pdf>. See Press Release, United Nations Commission on International Trade Law, U.N. Press Release UNIS/L/186 (Jul. 12, 2013), available at <http://www.unis.unvienna.org/unis/pressrels/2013/unisl186.html>.

60. See Text on investor state dispute settlement of EU agreements, Note for the Attention of the Trade Policy Committee (Services and Investment), *supra* note 59, art. 2.

investment decisions and certainty in public policy decisions.⁶¹ But whenever there are two or more divergent lines of decision on frequently invoked provisions that are common to many treaties, as we have seen on numerous such issues, the problem goes way beyond unpredictability. It goes to whether too many tribunals are misinterpreting, and thus misapplying, these common provisions; on any particle issue, only one of the divergent lines of reasoning can be right.

One solution might be to narrow the universe of deciders by having a closed roster of arbitrators. This may have been what the Commission had in mind when it floated the idea of “quasi-permanent arbitrators” in its 2010 Communication.⁶² In the event, this notion has apparently gone no further than the proposed creation of an agreed list of arbitrators from which appointing authority appointments may be made, when required – hardly a novel idea.⁶³

But much more significant is the renewed attention given to the possibility of establishing an appellate process for a broader and more substantive review of arbitral awards than is currently available under post-award proceedings under municipal law or the ICSID Convention. In the author’s view, this would be the single most effective way to reduce inconsistency and, more importantly, increase accountability for arbitral awards.

The issue appears to be trending in favor of more serious consideration of an appellate mechanism in future EU BITs. The Commission stated that “appellate mechanisms” should be considered in its 2010 communication, together with or as an alternative option to “quasi-permanent arbitrators.”⁶⁴ The Parliament was more direct in its 2011 resolution, calling, not merely for consideration of the issue, but expressly for the inclusion of “the opportunity of parties to appeal.”⁶⁵

The Commission’s draft 2012 ISDS text would establish a “Committee for the Settlement of Investor-State Disputes” made up of representatives of the treaty parties and, among other things, would require it to examine “whether, and if so, under what conditions an appellate mechanism could be created or integrated into this section to

61. See, e.g., D. Jones, *The Problem of Inconsistency and Conflicting Awards in Investment Arbitration*, German-American Lawyers' Association Practice Group Day, Frankfurt (Mar 26, 2011), *available at* <http://www.ciarb.net.au/sites/www.ciarb.net.au/files/files/520%20GALA%20Paper%20-%20Investor-State%20Arbitration%20%282%29.pdf> (“[I]n recent years, concerns have been raised about the appropriateness of arbitration in light of issues of inconsistency and conflicting awards in investment disputes. These are legitimate concerns, as the existence of conflicting decisions threatens the confidence and legal predictability required by international business transactions.”).

62. See 2010 Commission Communication, *supra* note 5, at 10.

63. See Text on investor state dispute settlement of EU agreements, *supra* note 59, art. 8(5).

64. See 2010 Commission Communication, *supra* note 5, at 10.

65. 2011 Parliament Resolution, *supra* note 8, at para. 31.

review, on points of law, awards rendered under this [treaty] section.”⁶⁶ This goes somewhat beyond the requirement that the US has been able to include in all of its modern IIAs calling upon the parties to consult within a stated period of time on the possibility of an appeals mechanism, leaving, however, adoption of such a mechanism to possible future amendment of the agreements;⁶⁷ disappointingly, it does not appear that the required consultations have ever been held in connection with any of those agreements within the periods provided or since. But the draft Commission text goes even further to empower the Committee to itself “amend this section in order to create, or integrate, an appellate mechanism if the Committee concludes that this is desirable.”⁶⁸

The most recent indication of direction of EU intentions does not go so far as the Commission’s draft ISDS text. Perhaps in light of the serious constitutional problems that would inevitably arise for the US side in allowing a treaty provision to be amended by a bilateral committee, the leaked Council Negotiating Directives of June 14, 2013 for negotiations on a comprehensive trade and investment agreement with the United States only provides that “[c]onsideration should be given to the possibility of creating an appellate mechanism applicable to investor-to-state dispute settlement under the Agreement.”⁶⁹

It is of course difficult to judge whether it will eventually be EU policy to insist upon award review in its IIAs. The Parliament’s position appears clear and the Commission

66. See Text on investor state dispute settlement of EU agreements, *supra* note 59, art. 19(2)(c).

67. See, e.g., “Within three years after the date of entry into force of this Treaty, the Parties shall consider whether to establish a bilateral appellate body or similar mechanism to review awards rendered under Article 34 in arbitrations commenced after they establish the appellate body or similar mechanism.” Treaty Between The United States Of America And The Oriental Republic Of Uruguay Concerning The Encouragement And Reciprocal Protection Of Investment, U.S.-Uru., Annex E Nov. 1, 2006, 44 I.L.M. 268, *available at* http://unctad.org/sections/dite/ia/docs/bits/US_Uruguay.pdf. The US required inclusion of such provisions in order to comply with requirements contained in Congress’s authorization for fast-track trade talks. See, Bipartisan Trade Promotion Authority Act of 2002, § 2201(b)(3)(G), 19 U.S.C.A. § 3802 (West Supp. 2005) (including as one of the stated negotiating objectives for investment, “seeking to improve mechanisms used to resolve disputes between an investor and a government through . . . providing for an appellate body or similar mechanism to provide coherence to the interpretations of investment provisions in trade agreements”). It is also worth noting that, in 2004, ICSID included in its proposed revision of the Arbitration Rules the possibility of appeals mechanism. ICSID Secretariat, *Possible Improvements of the Framework for ICSID Arbitration* Discussion Paper, pp. 14-16, (Oct. 22, 2004), *available at* https://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=OpenPage&PageType=AnnouncementsFrame&FromPage=NewsReleases&pageName=Archive_%20Announcement14. This proposal did not survive the process that led to the 2006 revised Rules.

68. See Text on investor state dispute settlement of EU agreements, Note for the Attention of the Trade Policy Committee (Services and Investment), *supra* note 59, at art. 19(3)(b).

69. *Council of the European Union, Negotiating Directives (United States of America)*, WORLD TRADE ONLINE (Jun. 17, 2013) [hereinafter *Council Negotiating Directives*], para. 23, *available at* http://insidetrade.com/iwppfile.html?file=jun2013%2Fwto2013_1935a.pdf. (article available through subscription or purchase).

and Council have evidenced a heightened awareness of the problems that have prompted calls for such review. The technical difficulties with creating a workable appellate mechanism are not to be underestimated. But as the EU enters into serious negotiations with the US, it will become increasingly apparent the stakes in getting the ISDS mechanism right are higher than they have ever been. This could very possibly lead to the revolutionary step of subjecting ISDS to the kind of accountability that municipal courts face as a matter of course.

But it appears that there may be even more revolutionary thinking afoot as the EU struggles with the implications of its new competence in light of the uncertainties of the current ISDS system. As Prof. Reinisch points out, the early thinking regarding investor-State arbitration of all of the EU institutions included the option of opting for “the *Calvo*-inspired, Australia-US BIT approach to abandon it outright and to rely exclusively on domestic courts.”⁷⁰ It is therefore ironic that, after moving quickly to a consensus in favor of investor-State arbitration, there are now unmistakable signs of a fundamental reassessment.

The first hint of this came in the Parliament’s 2011 resolution calling for inclusion of “the obligation to exhaust local judicial remedies where they are reliable enough to guarantee due process.”⁷¹ Proposing to reinstate the local remedies rule where there are reliable court systems in place raises, of course, the very real question of whether it is worth having a completely separate second level of dispute resolution at all. Over the next two years, the Parliament’s thinking took that very turn during the 2013 debates on the Commission’s proposal regarding financial responsibility for ISDS awards arising from future agreements. One spokesman stated that his group “does not believe that investor-state dispute settlements are necessary between mature legal systems,” mentioning Canada and the US in particular.⁷²

The amendment to the Commission proposal adopted after the debate provided that ISDS can be included in future EU IIAs only “[i]n the cases where it is justifiable.” As explained in the Parliament’s accompanying summary of the amendments, “Members consider that it is not obligatory to include an investor-to-state dispute settlement mechanism clause in future EU investment agreements and that their inclusion should be a conscious and informed policy choice that requires political and economic justification.”⁷³ Thus, the Parliament, which must approve future agreements, has strongly signaled that ISDS is not to be considered an indispensable element of

70. Reinisch, *supra* note 2, at 151.

71. 2011 Parliament Resolution, *supra* note 7, at ¶ 31.

72. See Remarks of Mr. David Martin, O-000043/2013 (B7-0120/2013 (May 22, 2013) (European Parliament debates), <http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//TEXT+CRE+20130522+ITEM-019+DOC+XML+V0//EN>.

73. See *Committee Report Tabled for Plenary, 1st Reading/Single Reading* (Mar. 26, 2013), available at <http://www.europarl.europa.eu/oeil/popups/summary.do?id=1255871&t=d&l=en>.

investment protection and that the risks posed by the ISDS system must be weighed against the gains. This would be surprising enough had not the Commission indicated that it fully agreed with this approach.

In his answer on this point during the debates, Commissioner De Gucht stated that “[o]bviously you need [ISDS] when it is an agreement with a third country that does not have a properly-functioning judicial system, where one can have doubts about the rule of law.”⁷⁴ The implication is clear: the US-Australia solution of dispensing with ISDS altogether is a real option for the EU.

Subsequently, in its directives for the negotiations with the US, the Council did not expressly engage in such “Calvo-inspired” heresy, but nonetheless left no doubt that it considers the need for ISDS to be an open question, stating that “[c]onsideration should be given . . . to the appropriate relationship between ISDS and domestic remedies. . . The inclusion of investment protection and investor-to-state dispute settlement (ISDS) will depend on whether a satisfactory solution, meeting the EU interests concerning [other issues], is achieved.”⁷⁵

Thus, a major shift appears to be brewing in the EU that was only hinted at six months ago. If ISDS finds its way into future EU IIAs at all, a question that may depend upon the identity of the EU counter-party concerned, it is likely to carry features that will dramatically affect its operation. At very least, IIAs emerging from the new competence of the EU are likely to be quite innovative and will set a new standard for balancing the rights of investors and the prerogatives of States, and in inserting a greater measure of accountability into the commercial arbitration model.

III. Intra-EU BITs

Whether future EU BITs include ISDS, and how ISDS will look if they do, will also accentuate the uncomfortable place that inter-EU BITs hold within the EU legal structure. Prof. Reinisch gives a fair overview of the issues implicating the continued viability of the 176⁷⁶ existing intra-EU BITs and reviews how BIT tribunals have dealt with some of those issues. As he points out, arguments that intra-EU BITs are no longer valid and that their arbitration provisions are no longer operative, and thus that tribunals lack jurisdiction, have not fared well before tribunals that have considered them thus far.

74. See Remarks of Commissioner De Gucht, *supra* note 38.

75. *Council Negotiating Directives*, *supra* note 69, at paras. 22-23.

76. *Commission Staff Working Document on the Free Movement of Capital in the EU*, at 11, SWD (2013) 146 final (Apr. 15, 2013), available at http://ec.europa.eu/internal_market/capital/docs/reports/130415_market-monitoring-working-document_en.pdf.

He is certainly correct in stating that these issues must, and will, eventually be authoritatively resolved by the CJEU. This may happen sooner than later; there are a number of actions in EU Member State courts that raise these issues either in connection with efforts to overturn arbitral awards rendered after tribunals have upheld the continued validity of intra-EU BITs or that involve direct court claims for treaty violations.

In the meantime, the issues are likely to be addressed by yet other investor-State tribunals under intra-EU BITs, based upon new considerations and developments. Despite previous adverse outcomes, I believe that the arguments against such continued validity and “operativeness” are compelling.⁷⁷

When a State accedes to the EU it enters into an entirely new legal order and a fundamental re-organization of its economic relations with all other Member States. The legal relations previously governed by any BITs there might be between the acceding State and existing Member States are, upon accession, addressed simultaneously, if in different ways, by the new EU legal order to which they have subscribed. Both the BITs and the EU legal order govern the free movement of capital under uniform principles of non-discrimination and treatment, with a constant recognition of rights in property. Thus, they address the same subject matter, even if the scope of EU law is much wider, and thus qualify for the threshold application of tests of incompatibility found in the international law principles reflected in Articles 59 and 30(3)⁷⁸ of the Vienna Convention on the Law of Treaties.

It is difficult to conceive how the patchwork of bilateral treaties between only certain pairs of Member States, with different provisions and scopes of application, could be anything but incompatible with the uniform and comprehensive principles of EU law. This is true with respect to the standards of State conduct applicable under the BITs compared to those applicable under EU law, which inevitably lead to specific incompatibilities (as was shown in the instance of extra-EU BITs in the infringement proceedings against Finland, Sweden and Austria, cited by Prof. Reinisch in the extra-

77. The author wishes to disclose that he and his firm represent the Slovak Republic in a number of investor-State arbitrations in which these issues have been, and are being, litigated.

78. Vienna Convention on the Law of Treaties art. 30(3), May 23, 1969, 1155 U.N.T.S. 331 (“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.”); art. 59(1) (“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) [i]t appears from the later treaty or is otherwise established that the parties intended that the matter should be governed by that treaty; or (b) [t]he 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.”).

EU BIT context⁷⁹). But is also clearly evident with respect to the contending roles foreseen for arbitral tribunals in BITs and for courts in the EU treaties.

With respect to questions of EU law, which arise necessarily in every intra-EU BIT case at least with respect to the jurisdiction of the tribunal, ISDS provisions clash in particular with two provisions of the TFEU regarding the roles of EU courts. The first conflict arises with TFEU Article 344, which provides that “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.”⁸⁰ As Prof. Reinisch notes, in the *Mox Plant* case, the then-named European Court of Justice (“ECJ”) held that Member States violate this provision when they arbitrate issues that fall within the scope of EU competence and thereby putting at issue the interpretation or application of EU law.⁸¹

But Prof. Reinisch’s statement that “both the *Mox Plant* case as well as Article 344 TFEU expressly refer to inter-state disputes”⁸² is not correct to the extent that it suggests that that provision does not affect investor-State arbitration under inter-EU BITs. The ECJ decision in *Mox Plant* certainly concerned an inter-State dispute, but it nowhere suggested that Article 344 is limited to cases involving only State parties. Moreover, the text of Article 344 itself is manifestly silent in this respect and the absence of any limitation to inter-State disputes could very well suggest instead that any submission by a Member State, regardless of the character of the counter-party to the dispute, to a non-EU treaty forum violates the obligation of Article 344. As one commentator has recently pointed out, the fact that there is conclusive authority that Article 344 applies to disputes between Member States and that it does not apply to disputes between private parties “does not say anything yet regarding a dispute with one Member State on the one side, and one private individual on the other.”⁸³ Thus, whether ISDS provisions in intra-EU BITs violate Article 344 is far from a closed question.

The second conflict arises with TFEU Article 267, which provides that, whenever a question of interpretation of the EU treaties must be ruled on in order for a “court or tribunal of a Member State” to render a judgment, it may, and if a court of last resort, it must, request the CJEU for a preliminary ruling on the question.⁸⁴ This provision,

79. Reinisch, *supra* note 2, at 121.

80. TFEU, *supra* note 1, art 344.

81. Reinisch, *supra* note 2, at 152, *citing* Case C-459/03, *Commission v. Ireland (Mox Plant)*, 2006 E.C.R. I-4635, para. 125 *et seq.*

82. *Id.*

83. 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, COMMON MARKET L. R. 11 (forthcoming), available at <http://ssrn.com/abstract=2267045>.

84. TFEU, *supra* note 1, art. 267 (“The Court of Justice of the European Union shall have jurisdiction to give preliminary rulings concerning:
(a) the interpretation of the Treaties;
(b) the validity and interpretation of acts of the institutions, bodies, offices or agencies of

together with Article 344, aims to avoid divergences in the interpretation of EU law and to ensure that EU law is given its full effect within the framework of the judicial systems of the Member States. Because investor-State tribunals, to whom Member States submit *via* their BITs questions of EU law, are not “courts or tribunals” of Member States, they deprive Member State courts themselves from exercising their role in the important control function of Article 267.

It was on this basis that, in its *Opinion 1/09 on the European and Community Patents Courts*, the CJEU struck down the disputes procedures proposed in a draft agreement developed by the Council to be entered into by the EU and by Member States and third countries who are parties to the 1973 European Patent Convention.⁸⁵ Under those procedures, a specialized court system, with both first instance and appellate courts, would have had jurisdiction to hear disputes between individuals related to European and Community patents under the Convention and proposed EU legislation.⁸⁶ The CJEU observed that the envisaged patent court system would be called upon, *inter alia*, to interpret and apply provisions of EU law, effectively stripping Member States courts of their jurisdiction over the same disputes. In doing so, it would:

[D]eprive courts of Member States of their powers [provided in Article 267] in relation to the interpretation and application of European Union law and the Court of its powers to reply, by preliminary ruling, to questions referred by those courts, and, consequently, would alter the essential character of the powers which the Treaties confer on the institutions of the European Union and on the Member States and which are indispensable to the preservation of the very nature of European Union law.⁸⁷

Thus, it was not the inability of the special patent courts themselves to refer questions of EU law to the CJEU that caused the problem – contrary to what Prof. Reinisch could be read as suggesting, they would in fact have been empowered to do so under language virtually identical to Article 267⁸⁸ – it was the displacement of the ability of Member State courts to do so that made the scheme incompatible with the EU treaties.⁸⁹

the Union;

Where such a question is raised before any court or tribunal of a Member State, that court or tribunal may, if it considers that a decision on the question is necessary to enable it to give judgment, request the Court to give a ruling thereon.

Where any such question is raised in a case pending before a court or tribunal of a Member State against whose decisions there is no judicial remedy under national law, that court or tribunal shall bring the matter before the Court.”)

85. See *Opinion 1/09, Creation of a Unified Patent Litigation 2011 E.C.R. I-0137, available at* <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:62009CV0001:EN:PDF> ECR I-0137 (Mar. 8, 2011).

86. *Id.* ¶¶ 3-12.

87. *Id.* ¶ 89.

88. “Article 48 of the draft agreement states: 1. When a question of interpretation of the [EC Treaty] or the validity and interpretation of acts of the institutions of the European Community is raised before the Court of First Instance, it may, if it considers this necessary to enable it to give a

Under this same reasoning, investor-State treaty tribunals similarly deprive Member State courts from playing their role on questions of EU law before them and would therefore similarly be in violation of EU law; the conferral of jurisdiction upon investor-State tribunals by intra-EU BITs is in the same sense incompatible with the exclusive jurisdiction of the EU judicial system. Certainly, *Opinion 1/09* casts serious doubt as to whether the CJEU would be prepared to consider such tribunals as compatible with Article 267.⁹⁰

Finally, not only are there serious questions about the compatibility of the arbitration provisions of intra-EU BITs with the exclusive jurisdiction of the EU judicial system, but those provisions are inherently discriminatory with regard to Member States which are not party to any particular BIT, and with regard to their nationals. Both the arbitration provisions and the substantive standards/treatment provisions of such BITs are available only to the State parties to the BIT and their investors. But, according to TFEU Article 18, discrimination on grounds of nationality is prohibited.⁹¹ The case law of the CJEU establishes that a breach of the legal duty of non-discrimination flows from the *mere existence* of the discriminating provision in the international instrument in question, and a breach exists until a remedy is employed.⁹²

In the view of some, this conclusion does not mean the BITs' arbitration provisions should be considered inoperative, since these discriminatory effects can be cured by each offending State by extending the obligations it owes to the other State and to its investors to all Member States and their investors.⁹³ However, quite apart from the practical and legal obstacles to unilateral extension – which, as established in the jurisprudence of the

decision, request the Court of Justice . . . to decide on the question. Where such question is raised before the Court of Appeal, it shall request the Court of Justice . . . to decide on the question." *Id.* ¶ 12.

89. "The draft agreement provides for a preliminary ruling mechanism which reserves, within the scope of that agreement, the power to refer questions for a preliminary ruling to the [special patent courts] *while removing that power from the national courts.*" (emphasis added.) *Id.* ¶ 81.
90. *Cf. Reinisch, supra* note 2, at 153 ("It cannot be excluded that the CJEU would consider investor-state arbitration incompatible with such a far-reading interpretation of its own interpret prerogatives [as is found in *Opinion 1/09*].").
91. TFEU, *supra* note 1, art. 18 ("Within the scope of application of the Treaties, and without prejudice to any special provisions contained therein, any discrimination on grounds of nationality shall be prohibited.").
92. Case C-471/98, *Commission of the European Communities v. Kingdom of Belgium* [2002] ECR I-9681, ¶¶ 141, 143 (" . . . the direct source of that discrimination is not the possible conduct of the United States of America but Article 5 of the Bermuda II Agreement, which specifically acknowledges the right of the United States of America to act in that way The efforts made by the Kingdom of Belgium to eliminate the incompatibility of the clause with Article 52 of the Treaty, however commendable, are clearly insufficient to disturb the finding made in the preceding paragraph.").
93. *See, e.g., Eastern Sugar B.V. (Netherlands) v. The Czech Republic*, Case No. 088/2004, Partial Award, at para. 170 (Arbitration Institute of the Stockholm Chamber of Commerce 2007), http://www.iisd.org/pdf/2007/itn_eastern_sugar.pdf.

ECJ, would not undo the incompatibility in the meantime⁹⁴ – the extension of dispute settlement mechanisms would certainly aggravate the concerns regarding the preservation of the nature of EU law.

Thus, despite the lack of success such arguments have had to date before investor-State tribunals, it is clear, as Prof. Reinisch acknowledges, that there are significant problems with the existence of a parallel system involving Member State parties capable of interpreting and applying EU law.

IV. Conclusion

The introduction of the EU as a major player in the field of investment protection and ISDS portend, in my view, significant changes in direction from the patterns established by previous Member State BIT practice. The issues raised by the traditional statements of State party obligations found in most BITs, and more than fifteen years of troubling experience with the ISDS system, have already led to a substantial re-appraisal of some of the most important underpinnings of the existing system. The fact that Canada, the US and China are among the countries first up for EU consideration has highlighted the tremendous stakes at issue. And the deviations from previous patterns that we will likely see in EU BITs in expressing standards of conduct and treatment, and in the providing for ISDS (if it is provided for at all), will together also accentuate the uncomfortable place that existing intra-EU BITs occupy in the EU legal system.

94. *See, e.g.*, “Contrary to what the Kingdom of Belgium maintains, the direct source of that discrimination is not the possible conduct of the United States of America but Article 5 of the Bermuda II Agreement, which specifically acknowledges the right of the United States of America to act in that way. 142. It follows that the clause on the ownership and control of airlines is contrary to Article 52 of the Treaty. 143. The efforts made by the Kingdom of Belgium in 1995 to eliminate the incompatibility of the clause with Article 52 of the Treaty, however commendable, are clearly insufficient to disturb the finding made in the preceding paragraph.” Case C-471/98, *Commission of the European Communities v. Kingdom of Belgium*, 2002 ECR I-9681, ¶¶ 141-143.