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Bilateral Investment Treaties and the EU Legal Order: Implications of the Lisbon Treaty

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BILATERAL INVESTMENT TREATIES AND THE EU LEGAL ORDER: IMPLICATIONS OF THE LISBON TREATY

INTRODUCTION

Foreign direct investment ("FDI")[1] is the "lifeblood of the global economy."[2] Foreign investors of developed, capital-exporting countries pursue opportunities abroad in efforts to obtain the highest returns on their investments, as well as to solidify positions in emerging markets.[3] Meanwhile, developing, capital-importing countries seek to attract capital flows and new technologies in efforts to enhance their economies and improve their competitive standing in the global marketplace.[4] In recent decades FDI flows dramatically surged,[5] a trend that is

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1. The International Monetary Fund and the Organisation for Economic Co-operation and Development define direct "foreign investment" as cross-border investment made by a resident entity in one economy (the "direct investor" or "multinational enterprise") with the objective of establishing a lasting interest in an enterprise resident in an economy other than that of the direct investor (the "foreign affiliate"). *See* International Monetary Fund [IMF], *Balance of Payments Manual*, at 86, (5th ed. 1993); *see also* Organization for Economic Co-operation and Development [OECD], *Detailed Benchmark Definition of Foreign Direct Investment*, at 7–8, (3d ed. 1996).

2. *See* Bernardo M. Cremades & David J. A. Cairns, *Contract and Treaty Claims and Choice of Forum in Foreign Investment Disputes*, *in* ARBITRATING FOREIGN INVESTMENT DISPUTES 325, 325 (Norbert Horn & Stefan Kroll, eds., 2004); *see also* Karl P. Sauvant & Lisa E. Sachs, THE EFFECT OF TREATIES ON FOREIGN DIRECT INVESTMENT: BILATERAL INVESTMENT TREATIES, DOUBLE TAXATION TREATIES, AND INVESTMENT FLOWS lx (2009) (stating that "[o]ne uncontroversial truth is that virtually all countries value FDI as a means to advance their economic development" and thus "compete with each other to attract investment").

3. *See* U.N. Conference on Trade and Dev. [UNCTAD], *World Investment Report 2003: FDI Policies for Development; National and International Perspectives*, xv, U.N. Doc. UNCTAD/WIR/2003 (Sept. 4, 2003) (stating that "intense competition continues to force [transnational corporations] to invest in new markets and to seek access to low-cost resources and factors of production").

4. *See id.* at iii (stating that due to its "enormous potential to create jobs, raise productivity, enhance exports and transfer technology, foreign direct investment is a vital factor in the long-term economic development of the world's developing countries").

5. *See* MIRIAN KENE OMALU, NAFTA AND THE ENERGY CHARTER TREATY: COMPLIANCE WITH, IMPLEMENTATION, AND EFFECTIVENESS OF INTERNATIONAL INVESTMENT AGREEMENTS 1–2 (NAFTA Law and Policy Series vol. 5, 1998) (stating that in 1980, FDI was estimated at $40 billion; in 1994 it jumped to $222 billion; by 1995 it had reached $315 billion); *see also* UNCTAD, *Assessing the Impact of the Current Financial and Economic Crisis on Global FDI Flows*, 3, U.N. Doc. UNCTAD/DIAE/IA/2009/3 (Jan. 19, 2009) (stating that the year 2007 saw unprecedented levels of FDI flows, "reaching a historic record of $1.8 trillion"); Jeswald W. Salacuse & Nicholas P. Sullivan, *Do BITs Really Work?: An Evaluation of Bilateral Investment*

expected to continue.[6] Coinciding with this surge is the proliferation of a dense network of international agreements pertaining to the protection of foreign investment,[7] most notably bilateral investment treaties ("BITs").[8] BITs are agreements between two countries that provide substantive standards for the protection of foreign investment, as well as procedures for dispute settlement.[9] In the absence of a comprehensive international legal framework or general customary international law governing foreign investment,[10] BITs have become the "dominant international vehicle through which investment is regulated."[11] In recent decades, BITs have flourished to unprecedented levels.[12]

While the legal infrastructure created by the BIT network operates on an international scale, BITs have become especially prevalent in the Eu-

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Treaties and Their Grand Bargain 46 HARV. INT'L L. J. 67, 71 (2005) (stating that between 1973 and 2000, FDI growth exceeded that of international trade twelvefold).

6. *See* UNCTAD, *World Investment Prospects Survey 2009–2011*, 9, U.N. Doc. UNCTAD/DIAE/IA/2009/8 (2009) (stating that while the global economic and financial crisis caused significant declines in global FDI flows in 2008 and 2009, a recovery is expected beginning in 2010 and will continue to gain momentum through 2011).

7. *See* Kenneth J. Vandevelde, *A Brief History of International Investment Agreements*, 12 U.C. DAVIS J. INT'L L. & POL'Y 157, 157 (2005).

8. *See* Efraim Chalamish, *The Future of Bilateral Investment Treaties: A De Facto Multilateral Agreement?,* 34 BROOK. J. INT'L L. 303, 305 (2009). BITs are part of the larger category of international investment agreements (IIAs), which also includes free trade agreements (FTAs) and regional trade agreements. FTAs and regional trade agreement contain foreign investment-related provisions, but such provisions are not their primary focus. This Note is concerned only with BITs, which typically deal exclusively with foreign investment and are the most proliferated type of IIA.

9. *See* Stephen M. Schwebel, *The Overwhelming Merits of Bilateral Investment Agreements*, 32 SUFFOLK TRANSNAT'L L. REV. 263, 263 (2009).

10. *See infra* Part I.A; *see also* Kelly Connolly, Note, *Say What You Mean: Improved Drafting Resources as a Means for Increasing the Consistency of Interpretation of Bilateral Investment Treaties*, 40 VAND. J. TRANSNAT'L L. 1579, 1609–1610 (2007).

11. Andrew T. Guzman, *Explaining the Popularity of Bilateral Investment Treaties*, *in* THE EFFECT OF TREATIES ON FOREIGN DIRECT INVESTMENT: BILATERAL INVESTMENT TREATIES, DOUBLE TAXATION TREATIES, AND INVESTMENT FLOWS 73 (2009).

12. *See* Salacuse & Sullivan, *supra* note 5, at 75 (stating that the impetus of this proliferation is the "desire of companies of industrialized states to invest safely and securely in developing countries, as well as the consequent need to create a stable international legal framework to facilitate and protect those investments"); *see also* ANDREW NEWCOMBE & LLUIS PARADELL, LAW AND PRACTICE OF INVESTMENT TREATIES 46–48 (2009) (By 1979, states had entered into approximately 100 BITs, by 1987, 265 BITs had been concluded, and by the end of the 1990s, 1,857 BITs had been concluded); Press Release, UNCTAD, *Bilateral Investment Treaties Quintupled During the 1990s*, U.N. Doc. TAD/INF/2877 (Dec. 15, 2000) (stating that there were 1,857 BITs by the end of the 1990s, while there had only been 385 at the end of the 1980s).

ropean Union ("EU").[13] The modern BIT originated in Europe when the first BIT was concluded[14] between the Federal Republic of Germany and Pakistan on November 25, 1959.[15] Since that time, EU Member States have constituted a majority of the most prolific negotiators of these treaties.[16] Central and Eastern European countries in particular have concluded a large number of BITs[17] and continue to be considered attractive locations for FDI by foreign investors.[18]

As the number of BITs concluded by EU Member States continues to grow, the nature of the relationship between these treaties and the EU legal order garners increasing attention.[19] This is because the relatively recent accession of many Central and Eastern European countries implicates the potential for conflict between EU legal requirements and BITs both between EU Member States (hereinafter, intra-EU BITs) and between EU Member States and non-EU Member States (hereinafter, extra-EU BITs).[20] In the context of BITs between Member States, the obligations under these BITs may be inconsistent with or superseded by EU law and, therefore, should be terminated.[21] With respect to BITs between

13. Seventy new BITs were concluded between June 2005 and June 2006. Of those seventy, EU Member States (excluding South-East Europe and the Commonwealth of Independent States) concluded the highest number of BITs, with forty-nine new agreements during this time period. UNCTAD, *International Investment Rule-Setting: Trends, Emerging Issues and Implications*, 3, 5, U.N. Doc. TD/B/COM.2/73 (Jan. 5, 2007).

14. To conclude a treaty is to ratify or formalize it. BLACK'S LAW DICTIONARY 126 (3d ed. 2006).

15. *See* Treaty for the Promotion and Protection of Investments, Pak.−F.R.G. Nov. 25, 1959, 457 U.N.T.S. 23 [hereinafter Pak.−F.R.G. BIT].

16. Germany, Switzerland, the UK, Italy, France, the Netherlands, and Belgium Luxembourg were seven among the top ten signatories of BITs up until 2008. UNCTAD, *Recent Developments in International Investment Agreements*, 3, U.N. Doc. UNCTAD/WEB/DIAE/IA/2009/8 (2008).

17. *See* Anca Radu, *Foreign Investors in the EU—Which 'Best Treatment'? Interactions Between Bilateral Investment Treaties and EU Law*, 14 EUR. L. J. 237, 238 (Mar. 2008).

18. *See* Stanimir Alexandrov, *The Future of Investment Treaty Protection in Eastern Europe*, EUR. & MIDDLE E. ARB. REV. (2009), *available at* http://www.globalarbitrationreview.com/reviews/14/sections/53/chapters/511/the-future-investment-treaty-protection-eastern-europe/, for a description of the recent, dramatic increase in FDI in Eastern Europe.

19. *See* Michele Potesta, *Bilateral Investment Treaties and the European Union. Recent Developments in Arbitration and Before the ECJ*, 8 LAW AND PRACTICE OF INTL. COURTS AND TRIBUNALS 225, 230 (2009).

20. *See* Thomas Eilmansberger, *Bilateral Investment Treaties and EU Law*, 46 COMM. MKT. L. REV. 383, 387 (2009).

21. *See* Christer Soderlund, *Intra-EU Investment Protection and the EC Treaty*, 24 J. INT'L. ARB. 455, 455 (2007).

Member States and Non-Member States, the potential exists for direct conflict between BITs and EU law, since EU law requires Member States to take all necessary steps to eliminate incompatibility between the EC Treaty and any other agreements to which they are a party.[22]

While the current interface between BITs and the EU legal order reveals a degree of legal uncertainty in need of reconciliation, the individual EU Member States have retained jurisdiction over foreign investment, and thus the ability to negotiate and conclude international investment agreements.[23] However, this may change now that the Lisbon Treaty entered into force on December 1, 2009.[24] The Lisbon Treaty is an international agreement between EU Member States that amends the current sources of EU law, namely the EU Treaty and the EC Treaty.[25] Its provisions seek to "enhanc[e] the efficiency and democratic legitimacy of the Union and to improv[e] the coherence of its action."[26] In one of its most novel provisions, the Lisbon Treaty transfers competence[27] over FDI from the Member States to the EU by bringing it under the ambit of the EU's Common Commercial Policy ("CCP").[28] While the treaty's language with respect to FDI appears unequivocal, it is nevertheless unclear how it will be interpreted and applied, and therefore, the practical effects it will have on the current EU BIT network. Many questions remain unanswered:

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22. *See* Treaty Establishing the European Economic Community, 25 March 1957, 298 U.N.T.S. 3 [hereinafter EC Treaty]; *see also* Radu, *supra* note 17, at 238.

23. *See* Radu, *supra* note 17, at 238.

24. All 27 Member States ratified the Lisbon Treaty. The treaty passed by referendum in Ireland, and on November 3, 2009, it was signed by the president of the Czech Republic, the final country to sign on. *Lisbon Treaty*, N.Y. TIMES (Feb. 25, 2010), *available at* http://www.nytimes.com/info/treaty-of-lisbon/.

25. *See generally* Treaty of Lisbon Amending the Treaty on European Union and the Treaty Establishing the European Community, Dec. 3, 2007, 2007 O.J. (C 306) 1 [hereinafter Lisbon Treaty].

26. *See* Lisbon Treaty, *supra* note 25, at 3 (preamble); *see also* Dr. Simon Duke, *The Lisbon Treaty and External Relations*, Bulletin of the European Institute of Public Administrations No. 2008/01, 13 ("[T]he Lisbon Treaty holds enormous potential for a more coherent Union on the international stage).

27. Competence is akin to sovereignty. *See* DANIEL C. K. CHOW & THOMAS J. SCHOENBAUM, INTERNATIONAL TRADE LAW: PROBLEMS, CASES AND MATERIALS 124 (2008) (stating that the "debate over the external relations power in the EC/EU concerns primarily whether the EC/EU has exclusive competence to negotiate and conclude international treaties binding upon its member states or whether there is a shared competence with its member states allowing the states to participate in the negotiations and conclusion of the agreements").

28. *See* Marc Bungenberg *Going Global? The EU Common Commercial Policy After Lisbon in* EUROPEAN YEARBOOK OF INTERNATIONAL LAW 124 (C. Herrmann & J.P. Terhechte eds., 2009).

- Will EU Member States retain the competence to negotiate and conclude BITs in the future?
- What is the legal status of existing BITs concluded by EU Member States?
- Is the EU capable of concluding international investment agreements comparable to BITs?

This Note argues that the EU's current system of BITs should remain intact in the short term because it provides for investment protection and arbitral dispute mechanisms of which there are no viable equivalents under the Lisbon Treaty. Part I provides a brief history of the development of the modern BIT. Part II offers an overview of the current, well-established system of both intra-EU BITs and extra-EU BITs. Part III describes the changes pertaining to FDI introduced by the Lisbon Treaty. Part IV examines the problems that will likely arise as a result of these changes and proposes the implementation of interim measures to facilitate the gradual transition from a system of Member States mixed competence to a system of EU exclusive competence. This Note concludes that while EU competence over FDI is a logical step in the movement toward a more streamlined, comprehensive, multilateral EU trade and investment system, an expedited overhaul of the current legal structure would foster uncertainty and be detrimental to the EU's continued ability to attract FDI and manage foreign-investor expectations.

I. Bilateral Investment Treaties and the EU Legal Order

A. A Brief History of BITs Concluded by EU Member States

The development of the modern BIT originated in Europe in the period following World War II,[29] at which time individual European countries began to negotiate treaties dealing exclusively with foreign investment.[30] The objective of these treaties was to protect foreign investors against uncompensated expropriation,[31] an area not covered by customary inter-

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29. *See* Salacuse & Sullivan, *supra* note 5, at 68 (stating that in the period after World War II, "foreign investors who sought the protection of international investment law encountered an ephemeral structure consisting largely of scattered treaty provisions, a few questionable customs, and contested general principles of law").

30. *See* Rudolf Dolzer & Margaret Stevens, Bilateral Investment Treaties 10–11 (1995) (providing a historical context of BITs as an outgrowth of FCNs).

31. *See* Rodney Neufeld, *Trade and Investment, in* The Oxford Handbook of International Investment Law 636-637 (Daniel Bethlehem et al. eds., 2009) (stating that "direct expropriation involves the taking of an investment by the host State through

national law.[32] The first BIT was concluded between the Federal Republic of Germany and Pakistan in 1959,[33] after which several other European countries followed suit.[34] In the late 1980s, in efforts to attract foreign investment and to encourage economic development, several of the countries that now comprise Central and Eastern Europe concluded BITs with developed countries.[35] European countries alone concluded forty-seven BITs between January 2005 and June 2006.[36] While less than five hundred BITs were in force in the 1990s,[37] there are currently more than 2,600 in force.[38] BITs were initially concluded asymmetrically between a developed and a developing country,[39] but this arrangement is slowly

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seizure of the property or interest, or through its compulsory transfer, for example, to a state-owned enterprise or domestic investor . . . an indirect expropriation often consists of a series of government acts that has the effect of rendering the investor's property rights useless").

32. *See* NEWCOMBE & PARADELL, *supra* note 12, at 41 (stating that the development of international investment agreements "was primarily a response to the uncertainties and inadequacies of the customary international law of state responsibility for injuries to aliens and their property"); *see also* M. SORNARAJAH, THE INTERNATIONAL LAW ON FOREIGN INVESTMENT 89 (2d ed. 2004) (stating that while it is a principle of customary law that when a host country unlawfully takes the property of the foreign investor it must compensate the foreign investor for this taking, there is considerable disagreement on this standard of compensation and how it should be calculated); Andrew T. Guzman, *Why LDCs Sign Treaties That Hurt Them: Explaining the Popularity of Bilateral Investment Treaties,* 38 VA. J. INT'L L. 639, 641 (1998) (Prior to WWII, expropriation of a foreign investor's property was governed by the "Hull Rule" under customary international law, which required that compensation for expropriation be "prompt, adequate, and effective." However, this rule fell out of favor following WWII).

33. *See* Pak.–F.R.G. BIT, *supra* note 15; *see also* UNCTAD, *Bilateral Investment Treaties in the Mid–1990s*, 177–179, U.N. Doc. UNCTAD/ITE/IIT/7 (1998) (reporting historical statistics of all of the BITs entered into by Germany); UNCTC, *Bilateral Investment Treaties*, 7, U.N. Doc. ST/CTC/65 (stating that Germany was particularly concerned with the future protection of its foreign investments, as it had lost all of its foreign assets following WWI and WWII).

34. *See* NEWCOMBE & LLUIS PARADELL, *supra* note 12, at 42–43 (stating that the capital-exporting states of Switzerland, the Netherlands, Italy, the Belgo-Luxembourg Economic Union (BLEU), Sweden, Denmark, Norway, France, and the UK began to conclude BITs soon after Germany).

35. *See* UNCTAD, *International Investment Rule-making: Stocktaking, Challenges and the Way Forward*, 15, U.N. Doc. UNCTAD/ITE/IIT/2007/3 (2008).

36. *See* Radu, *supra* note 17, at 238.

37. *See id.* at 237.

38. 2,676 BITs were in effect as of 2009. UNCTAD, *World Investment Report 2009: Transnational Corporations, Agricultural Development and Development*, xxii, U.N. Doc. UNCTAD/WIR/2009 (2009).

39. *See* UNCTAD, *Bilateral Investment Treaties 1959–1999*, 1–2, U.N. Doc. UNCTAD/ITE/IIA/2 (2000) (stating that BITs were initially concluded between a developed, capital-exporting country and a developing, capital-importing country. Developing

eroding as developing countries enter into BITs with other developing countries and transition economies pursue BITs on their own.[40]

This expansive and growing network of BITs is a by-product of repeatedly failed efforts to establish an international investment framework.[41] In 1995, the Organisation for Economic Co-operation and Development ("OECD")[42] attempted to negotiate the Multilateral Agreement on Investment ("MAI").[43] The MAI sought to consolidate rules on international foreign investment into a single legal instrument that would be open to accession by both OECD and non-OECD members.[44] However, this agreement met a great deal of opposition and was consequently abandoned in 1998.[45] The objective of the MAI was resurrected in 2001 when the WTO Doha Ministerial Conference agreed to take up negotiations on trade and investment beginning in 2003, and established a negotiating group on trade and investment.[46] This plan was similarly abandoned in 2004.[47] Due to the lack of an international framework governing FDI, the dense network of BITs "[f]or all practical purposes . . . has become the fundamental source of international law in the area of foreign investment."[48]

B. The Basic Features of BITs

BITs contain substantive provisions for the protection of foreign investment as well as procedural provisions for investment dispute resolution.[49] In terms of substantive provisions, the vast majority of BITs iden-

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countries entered into BITs in order to attract foreign investors and reap the benefits of FDI. However, beginning in the late 1980s, this paradigm shifted and BITs were increasingly concluded between two developing countries).

40. *See* Andrea K. Bjorklund, *Reconciling State Sovereignty and Investor Protection in Denial of Justice Claims* 45 VA. J. INT'L L. 809, 832 (2005).

41. *See* UNCTAD, *Lessons from the MAI*, U.N. Doc. No. UNCTAD/ITE/ITT/Misc.22 (1999).

42. The OECD, "based in Paris, is an organization of thirty leading industrialized countries that deals with economic and social issues of concern to its members." It works with the Bretton Woods institutions and the WTO. CHOW & SCHOENBAUM, *supra* note 27, at 20–21.

43. *See* SORNARAJAH, *supra* note 32, at 291.

44. *See* Alfred Escher, *The Multilateral Investment Treaty, in* LEGAL ASPECTS OF FOREIGN DIRECT INVESTMENT 69 (Daniel D. Bradlow & Alfred Escher, eds. 1999).

45. *See* UNCTAD, *Lessons from the MAI*, *supra* note 41.

46. *See* CHOW & SCHOENBAUM, *supra* note 27, at 324.

47. *Id.*

48. SALACUSE & SULLIVAN, *supra* note 5, at 70.

49. *See* Theresa McGhie, *Bilateral and Multilateral Investment Treaties, in* LEGAL ASPECTS OF FOREIGN DIRECT INVESTMENT 109 (Daniel D. Bradlow & Alfred Escher eds., 1999).

tify the scope of investments covered under the respective treaty.[50] The very first BIT, between Germany and Pakistan, provided for a broad definition of "investment."[51] This inclusiveness is characteristic of the BITs concluded over the past fifty years.[52] While the breadth of coverage of investment articulated in a BIT can vary based upon the intentions of the negotiating parties,[53] the prevailing definition adopted by BITs concluded by EU Member States describes "investment" as including "every kind of asset."[54] This encompassing definition, thus, goes beyond the coverage of FDI[55] and can even extend protection to portfolio investments.[56]

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50. *See* DOLZER AND STEVENS, *supra* note 30, at 25–26.

51. *See* Pak.−F.R.G. BIT, *supra* note 15, art. 8 (stating that the term "investment shall comprise capital brought into the territory of the other Party for investment in various forms in the shape of assets such as foreign exchange, goods, property rights, patents and technical knowledge. The term "investment" shall also include the returns derived from and ploughed back into such "investment" . . . Any partnerships, companies or assets of similar kind, created by the utilization of the above-mentioned assets shall be regarded as "investment").

52. "Investment" is typically defined very broadly in BITs, and includes both the tangible and intangible assets of the foreign investor. *See* SORNARAHAH, *supra* note 32, at 220–221.

53. *See* UNCTAD, *Bilateral Investment Treaties 1995–2006: Trends in Investment Rulemaking*, 7, U.N. Doc. UNCTAD/ITE/IIA/2006/5 (2007) [hereinafter UNCTAD, *BITs 1995–2006*] (stating that some BITs define "investment" broadly, but additionally provide for a list of clarifications limiting or excluding particular kinds of investments).

54. DOLZER AND STEVENS, *supra* note 30, at 27; *see also* UNCTAD, *BITs 1995–2006, supra* note 53, at 8 (stating that the "asset-based" definition of "investment" usually includes "five categories of assets: first, movable and immovable property and any related property rights such as mortgages, liens or pledges, second, various types of interests in companies, such as shares, stock, bonds, debentures or any other form of participation in a company, business enterprise or joint venture; third, claims to money and claims under a contract having a financial value and loans directly related to a specific investment; fourth, intellectual property rights; and fifth, business concessions, that is rights conferred by law or under contracts").

55. *See* UNCTAD, *BITs 1995–2006, supra* note 53, at 8; *see also* Neufeld, *supra* note 31, at 621 ("To 'invest' means to expend money, effort, or time into an undertaking with the intention of deriving profit. However, 'foreign direct investment' (FDI) implies something more than the mere purchase of shares for the sake of the interest, dividends or profits. Traditionally, States have distinguished FDI from other investment . . . FDI distinguishes itself from portfolio investment in that it 'consists of a transaction made by a foreigner in a host state which is intended to set up a long term relationship with a party in the host state'").

56. *See* Neufeld, *supra* note 31, at 622 (stating that portfolio investment is any type of foreign investment that is not classified as FDI); *see also* SORNARAHAH, *supra* note 32, at 227 (describing portfolio investment as "[investment] instruments connected with companies like shares or unconnected with them like promissory notes and bonds").

BITs can vary in substantive detail, but their structure and general composition are relatively uniform.[57] They contain preliminary statements that articulate their purpose and aim, typically the "reciprocal encouragement and protection of investment flows between the two states."[58] They provide for core protections including national treatment,[59] most favored nation ("MFN") treatment,[60] compensation for expropriation,[61] and rights to transfer capital and returns.[62] Due to this protective framework for substantive rights, BITs play an important role in alleviating the concerns and vulnerabilities of foreign investors who assume the inherent risks associated with FDI.[63]

In the event that a party to a BIT does not comply with its treaty obligations, BITs also contain provisions for investment dispute resolution.[64] Arguably, the most significant facet of BITs is their provision for investor-state dispute settlement, in which foreign investors may directly sub-

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57. *See* SORNARAHAH, *supra* note 32, at 89.

58. *Id.* at 217.

59. In the context of BITs, national treatment refers to the "obligation of contracting parties to grant investors of the other contracting party treatment no less favourable than the treatment they grant to investments of their own investors. The effect is to create a level playing field between foreign and domestic investors in the relevant market." UNCTAD, *BITs 1995–2006, supra* note 53, at 33.

60. In the context of BITs, the MFN treatment standard "means that investments or investors of one contracting party are entitled to treatment by the other contracting party that is no less favourable than the treatment the latter grants to investments or investors of any other third country." *See id.* at 38.

61. J. Frederick Truitt, *Expropriation of Foreign Investment: Summary of the Post World War II Experience of American and British Investors in Less Developed Countries*, 1 J. INT'L BUS. STUDIES 21, 24 (1970) (defining expropriation as "an official taking by a sovereign state of the tangible property of alien corporate ownership with a view toward the continued exploitation of that property for the public utility of the expropriating state in lieu of continued ownership and control by private foreign enterprise"); *see also* Schwebel, *supra* note 9, at 265–266 ("If there is a taking by the state of the foreign investment, by means direct or indirect, the state is treaty-bound to pay prompt, adequate and effective compensation").

62. *See* NEWCOMBE & PARADELL, *supra* note 12, at 43; *see also* Press Release, UNCTAD, Analysis of Bilateral Investment Treaties Finds Growth in Agreements, New Areas of Focus, UNCTAD/PRESS/IN/2007/014 (Dec. 4, 2007), *available at* http://www.unctad.org/templates/Webflyer.asp?docID=8270&intItemID=1528&lang=1 (report concludes that "more countries concluding these treaties are placing greater emphasis on public concerns such as health, environment, core labour rights, national security, transparency in information exchange and rulemaking").

63. The "basic assumptions behind BITs are that a bilateral treaty with clear and enforceable rules to protect and facilitate foreign investment reduces risks that the investor would otherwise face and that such reductions in risks, all things being equal, encourage investment." Salacuse & Sullivan, *supra* note 5, at 77.

64. *See id.* at 87.

mit violations of BITs by a host state to international arbitration.[65] Foreign investors consider these arbitration proceedings, which are outside the jurisdiction of the host state, preferable to filing a claim against the host state in its domestic courts.[66] This is because this system prevents the host state from enjoying a "home court advantage."[67]

The main forum chosen for dispute settlement is the International Centre for Settlement of Investment Disputes ("ICSID"),[68] which was formally established in 1965 for the primary purpose of resolving disputes between host countries and foreign private investors.[69] Other forums for dispute arbitration include the International Center for Dispute Resolution, the International Chamber of Commerce, and the Arbitration Institute of the Stockholm Chamber of Commerce.[70] According to statistics from the United Nations Conference on Trade and Development, by the end of 2007, there were two hundred and ninety known investment treaty arbitrations, the majority of which were commenced under BITs.[71] While

65. *See* Alexandrov, *supra* note 18. (The judgments awarded in these arbitrations are binding, and may require that the host state "pay substantial monetary damages to the injured investor"); *see also* Jarrod Wong, *Umbrella Clauses in Bilateral Investment Treaties: Of Breaching of Contract, Treaty Violations, and the Divide Between Developing and Developed Countries in Foreign Investment Disputes*, 14 GEO. MASON L. REV. 135, 142 (2006). Wong explains: "[s]ignificantly, only states (and not the investors) enter into BITs. Notwithstanding, the investor is able to enforce directly its rights under the BIT through the BIT's dispute settlement provisions." *Id.* at 142; Salacuse & Sullivan, *supra* note 5, at 88 (stating that "granting a private party the right to bring an action in an international tribunal against a sovereign state with respect to an investment dispute is a revolutionary innovation that now seems to be taken for granted"); Schwebel, *supra* note 9, at 267 (stating that "[t]his extraordinary innovation displaces the uneven intervention of states in exercise of their right of diplomatic protection of the interests of their nationals by according the foreign investor standing under international law, by virtue of the treaty, to pursue arbitration against the host state").

66. *See* Schwebel, *supra* note 9, at 263 (Foreign investors seeking legal recourse for the violation of BIT provisions may consider the domestic courts to be biased against them. The foreign investor could alternatively seek legal intervention from the country of which they were a national, but this too was not always an effective route for the foreign investor).

67. George M. von Mehren, *Navigating Through Investor-State Arbitrations – An Overview of Bilateral Investment Treaty Claims,* 59 DISP. RESOL. J. 69, 70 (1994).

68. Convention on the Settlement of Investment Disputes Between States and Nationals of Other States, Mar. 18, 1965, 17 U.S.T. 1270, 575, U.N.T.S. 159 [hereinafter ICSID Convention].

69. *See* SORNARAJAH, *supra* note 32, at 250.

70. *See* von Mehren, *supra* note 67, at 70.

71. Between 1987 and 2007, seventy-eight percent of investment treaty arbitrations were brought on allegations of the violation of a BIT. *See* UNCTAD, *Latest Developments in Investor-State Dispute Settlement*, 1, U.N. Doc. UNCTAD/WEB/IIA/2008/3 (2008).

these arbitrations have been criticized for their lack of uniformity and transparency in decision-making,[72] they nevertheless offer benefits to host countries and investors.[73] Dispute settlement provisions in BITs providing for this type of arbitration enable host countries to attract foreign investment, and allow foreign investors to "manage the risk associated with investing in a foreign country."[74]

II. THE RELATIONSHIP BETWEEN BITS AND THE PRE-LISBON EU LEGAL ORDER

A. The Division of Competences

The structure of the EU legal order is quite complex, consisting of a supranational legal system which coexists alongside the legal systems of the individual Member States.[75] Under this arrangement, Member States transfer some of their national sovereignty to the European Community ("EC"),[76] and in effect become governed by Community law.[77] Up until the passage of the Lisbon Treaty, the primary sources of Community law were a set of treaties which formed the basis for "everything the EU does."[78] The most important of these treaties are the EC Treaty[79] (also

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72. For an in-depth discussion of the negative impact of inconsistent interpretations of BITs by ad hoc arbitration panels, see CONNOLLY, *supra* note 10. *See generally* Susan Franck, *The Legitimacy Crisis in Investment Treaty Arbitration: Privatizing Public International Law Through Inconsistent Decisions,* 73 FORDHAM L. REV. 1521 (2005).

73. *See von* Mehren, *supra* note 67, at 76.

74. *Id.*

75. *See* Matej Avbelj, *The EU and the Many Faces of Legal Pluralism. Toward a Coherent or Uniform EU Legal Order?,* 2 CROATION YEARBOOK OF EUROPEAN LAW AND POLICY 377, 380 (2006).

76. *See* DERRICK WYATT & ALAN ASHWOOD, EUROPEAN UNION LAW 125 (5th ed. 2006); *see also* Case 26/62, Van Gend en Loos V. Nederlanse Administratie det Melastingen, 1963 E.C.R. 3, Summary ¶ 3 (stating that "the European Economic Community constitutes a new legal order of international law for the benefit of which the states have limited their sovereign rights, albeit within limited fields, and the subjects of which comprise not only the Member States but also their nationals"); CHOW & SCHOENBAUM, *supra* note 27, at 124 (stating that the EU's structure consists of "three pillars," one of which is the EC which carries out the legal functions of the EU).

77. *See* JEAN-VICTOR LOUIS, THE COMMUNITY LEGAL ORDER 11 (European Communities 2d ed. 1990).

78. The Lisbon Treaty amends, but does not replace these treaties. To avoid confusion, Part II.C of this Note discusses the EC Treaty and the EU Treaty in the present tense, as the majority of their provisions remain intact; *see also* KAREN DAVIES, UNDERSTANDING EUROPEAN UNION LAW 48 (3rd ed. 2007) (stating that these treaties include the Treaty establishing the European Coal and Steel Community 1951; the Treaty establishing the European Atomic Energy Community 1957; the Treaty establishing the European Economic Community 1957; the Merger Treaty 1965; the Budgetary Treaties

known as the Treaty of Rome or the Treaty establishing the European Economic Community) and the EU Treaty[80] (also known as the Maastricht Treaty or the Treaty on the European Union). The EC Treaty is the major governing instrument in the EU, regarded as a kind of constitution.[81] Its scope includes economic, social, environmental, and regional policies.[82] The EC Treaty seeks "to lay the foundation of an ever closer union among the peoples of Europe," and to "strengthen the unity" of the Member State economies.[83] The EU Treaty, which entered into force in 1994, created the "three pillar" structure that forms the basis of the "European Union."[84] In its preamble, the EU Treaty sets as its objective the "strengthening and the convergence" of the Member State economies.[85] Thus, together these treaties set forth the broad goals of integrating the EU Member States and facilitating cooperation at the political, social, and in particular, economic level.

Despite the EU's broad goal of an integrated Europe, it may only act within the confines of the powers attributed to it by Community law under various treaties.[86] Community competence, or sovereignty, is divided into three principal categories: exclusive, shared, and supporting.[87] In areas of exclusive Community competence, power is held solely by the

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1970 and 1975; the Single European Union Act 1986; the Treaty on European Union 1992; the Treaty of Amsterdam 1997; the Treaty of Nice 2000.)

79. *See* EC Treaty, *supra* note 22.

80. *See* Treaty on European Union (EU), 7 February 1992, 1992 O.J. (C 191) 1, 31 I.L.M. 253 [hereinafter EU Treaty].

81. LINDA SENDEN, SOFT LAW IN EUROPEAN COMMUNITY LAW 37 (2004). Because the EC Treaty is the most comprehensive treaty governing the EU, the EU law discussed in this Note relies predominantly on the EC Treaty.

82. *See Id.*

83. EC Treaty, *supra* note 22, at preamble.

84. *See How the European Union Works: Your Guide to the EU Institutions*, E.U. Commission, http://www.eurunion.org/infores/HowEUWorks072007.doc (last visited June 2010).

85. *See* EU Treaty, *supra* note 80, at preamble. For the sake of avoiding confusion, this Note refers to the European Union to mean both the European Economic Community created by the EC Treaty and the European Union as it stands today.

86. *See e.g.,* EC Treaty, *supra* note 22, art. 5(1) (stating that the Community "shall act within the limits of the powers conferred upon it by this Treaty and all of the objectives assigned to it herein"); *see also* EC Treaty, *supra* note 22, art. 5(2) (stating that "in areas which do not fall within its exclusive competence, the Community shall take action, in accordance with the principle of subsidiarity, only if and in so far as the objectives if the proposed action cannot be sufficiently achieved by the Member States and can therefore, by reason of the scale or effects of the proposed action, be better achieved by the Community; EC Treaty, *supra* note 22, art. 5(3) (stating that "any action by the Community shall not go beyond what is necessary to achieve the objectives of this Treaty").

87. *See* WYATT & ASHWOOD, *supra* note 76, at 91–97.

Community.[88] Member States cannot act autonomously, but rather, can only act if authorized by the Community.[89] In the category of shared competence, both the Community and the Member States are competent to exercise their shared regulatory power in a given area.[90] However, in exercising this power, Member States must concurrently comply with their obligations under the provisions of the various treaties.[91] Finally, under the category of supporting competence, the Community establishes broad goals in a field, but the Member States retain exclusive regulatory power to act.[92] In summary, the Community cannot act unless it has the authority to do so under the Treaties; Member States retain competence in areas that have not been specifically delegated to the EC.[93]

Based on the division of competences under the EC Treaty, both the EU and the Member States retain regulatory control over different aspects of foreign investment.[94] The EU can exercise its competence by adopting measures relating to foreign investment to the extent that it acts "within the limits of the power conferred upon it" by the EC Treaty.[95] The EC Treaty contains a number of provisions relating to foreign investment. Under Articles 43 and 48 through 56, the Treaty provides for rights of establishment.[96] Articles 56 through 60 deal with movement of capital.[97] Under Article 310, the Treaty gives the Community the power to conclude agreements relating to reciprocal rights and obligations.[98] Finally, under Article 181, the EU can conclude agreements with developing countries.[99] Thus, all of these provisions touch upon the EU's internal and external competence relating to foreign investments. For that reason, these provisions are coterminous with BITs.[100] However, while

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88. *See* DAVIES, *supra* note 78, at 25; *see also* WYATT & ASHWOOD, *supra* note 76, at 91–92 (Under the EC Treaty, exclusive competence has been uncontroversial in only three cases: the regulation of external trade under the common commercial policy, which is based upon Article 133 EC; the conservation of marine biological resources; and monetary policy for those Member States which have adopted the euro).

89. *See* WYATT & ASHWOOD, *supra* note 76, at 91.

90. *Id.* at 92.

91. *Id.*

92. *Id.* at 95.

93. *Id.*

94. *See* Eilmansberger, *supra* note 20, at 389.

95. *See* EC Treaty, *supra* note 22, art. 5(1); *see also* Jan Ceyssens, *Towards a Common Investment Policy? – Foreign Investment in the European Constitution,* 32 LEGAL ISSUES OF ECON. INTEGRATION 260 (2005).

96. EC Treaty, *supra* note 22, art. 43–48.

97. *Id.* art. 56–60.

98. *Id.* art. 310.

99. *Id.* art. 181.

100. *See supra* Part I.B.

the EC Treaty contains investment-related provisions, because it does not confer exclusive competence over foreign investment upon the EU, nor does it confer upon the EU the power to conclude international investment agreements with non-EU countries, these areas fall within the competence of the EU Member States.[101]

Since the EU has limited powers to adopt measures pertaining to foreign investment under the EC Treaty, EU Member States predominantly exercise competence in this field.[102] Member States have largely implemented this power through the negotiation and conclusion of BITs.[103] However, the interaction between provisions contained in BITs and the EU legal order can lead to overlap and incompatibility issues.[104] The interface between BITs entered into by EU Member States and the EU legal order is significant in two contexts: intra-EU BITs, and extra-EU BITs.[105]

B. Intra-EU BITs

The majority of intra-EU BITs resulted from the relatively recent accession of twelve Central and Eastern European nations to the European Union.[106] These countries entered into BITs with EU Member States prior to their accession, creating the current situation in which both parties to the BIT are now Member States.[107] The number of intra-EU BITs is quite significant;[108] approximately 190 BITs of this nature are current-

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101. *See* WYATT & ASHWOOD, *supra* note 76, at 91–97.

102. *See* Ceyssens, *supra* note 95, at 259; *see also* Soderlund, *supra* note 21, at 461.

103. *See* Ceyssens, *supra* note 95, at 268.

104. *See* Radu, *supra* note 17, at 238 (explaining the difficulty encountered by EU Member States in concluding BITs that do not conflict with EU law and that do not prejudice foreign investors).

105. *See* Potesta, *supra* note 19, at 225.

106. In 2004, 10 countries acceded to the EU, including Malta, Cyprus, Slovenia, Estonia, Latvia, Lithuania, Poland, the Czech Republic, Slovakia, and Hungary. Most recently, Bulgaria and Romania acceded in January 2007. *2000-Today: A Decade of Further Expansion*, EUROPA.EU, http://europa.eu/abc/history/2000_today/index_en.htm (last visited Dec. 21, 2009); *see also* Soderlund, *supra* note 21, at 455 (stating that there are two BITs concluded between "old" EU Member States. Germany concluded BITs with Portugal and Greece prior to their accession to the EU in 1980 and 1986, respectively. However, no foreign investor has invoked either of these BITs in bringing an investment dispute against one of these countries).

107. *See* Soderlund, *supra* note 21, at 455.

108. "The top signatories – Germany, UK France, Italy, The Netherlands, Belgium and Luxembourg – count more than 500 BITs. From January 2005 to June 2006 only, European countries concluded 47 BITs." Radu, *supra* note 17, at 237.

ly in force.[109] The recent influx of intra-EU BITs has generated a number of questions concerning the relationship between EU law and the obligations these countries have undertaken through BITs.[110] These questions include whether intra-EU investment issues are governed by EC law or the domestic law of the Member States, whether intra-EU BITs are superseded by EC law, and whether intra-EU investor-state arbitration mechanisms conflict with the EC legal order.[111]

These uncertainties were recently addressed through arbitral proceedings in *Eastern Sugar B.V. v. Czech Republic*.[112] In 1991, the Czech and Slovak Federal Republic, seeking to attract FDI to its newly established free market economy, entered into a BIT with the Netherlands.[113] In 1993, the Czech and Slovak Federal Republic separated into two sovereign states, and the Czech Republic assumed the international obligations arising from the BIT concluded with the Netherlands.[114] In 2003, an investment dispute arose between Dutch sugar producer Eastern Sugar B.V. and the Czech Republic.[115] In December 2003, the dispute was submitted to an ad hoc arbitral tribunal of the United Nations Commission on International Trade Law ("UNCITRAL") pursuant to Article 8 of the BIT.[116] Article 8 provides in pertinent part that "[e]ach Contracting Party hereby consents to submit a dispute . . . to an arbitral tribunal . . . [which] shall determine its own procedure applying the arbitration rules of UNCITRAL."[117] Subsequently, in 2004, the Czech Republic acceded to the EU pursuant to the Accession Treaty of April 16, 2003.[118] Because

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109. For figures on BITs entered into by each EU Member State, see Country-Specific Lists of BITs, UNCTAD, http://www.unctad.org/Templates/Page.asp?intItemID=2344&lang=1 (last visited Dec. 22, 2009); *see also* Radu, *supra* note 17, at 238 (stating that the proliferation of BITs between countries in the Eastern bloc exceeded 150 prior to these countries acceding to the EU).

110. *See* Alexandrov, *supra* note 18.

111. *See* Soderlund, *supra* note 21, at 460.

112. Eastern Sugar B.V. v. Czech Republic, Partial Award, SCC No. 088/2004, UNCITRAL (Mar. 27, 2007) [hereinafter Eastern Sugar].

113. Agreement on Encouragement of Reciprocal Protection of Investments Between the Kingdom of the Netherlands and the Czech and Slovak Federal Republic, Neth.-Czech Rep.-Slovk., Apr. 24, 1991. *See also* Eastern Sugar, *supra* note 112, ¶ 2 (stating that until 2002, the Czech Republic had concluded BITs with all countries that are currently EU Member States).

114. *See* Eastern Sugar, *supra* note 112, ¶ 5.

115. *See id.* ¶ 12.

116. *See id.* ¶ 13.

117. *See* Agreement on encouragement and protection of investments, Czech Republic-Netherlands, *supra* note 112, art. 8.

118. *See* Eastern Sugar, *supra* note 112, ¶ 14.

the Netherlands was already an EU Member State, the BIT effectively became an intra-EU BIT.

In this investment dispute, the foreign investor of Eastern Sugar B.V. alleged that Czech authorities discriminated against him by issuing three decrees that adversely affected Eastern Sugar.[119] The tribunal found that the Czech Republic had violated the fair and equitable treatment standard set forth in Article 3(1) of the BIT because one of the decrees that it issued unduly "targeted" Eastern Sugar and constituted a "discriminatory and unreasonable measure,"[120] and awarded 25 million Euros in damages to Eastern Sugar.[121] While this award was substantial, the tribunal's decision is particularly significant for its discussion of intra-EU BITs and the tribunal's holding that the mere fact of accession of a country to the EU does not render an intra-EU BIT irrelevant or invalid.[122]

The Czech Republic argued that the arbitral tribunal lacked jurisdiction over claims brought by Eastern Sugar to the extent that they pertained to a time subsequent to the Czech Republic's accession to the EU.[123] According to the Czech Republic, when it became an EU Member State, "this changed the relationship that it had with the Netherlands sufficiently to terminate or limit the application of the BIT implicitly, and as a result, to put an end to the benefits and protection enjoyed under the BIT by a Dutch investor such as Eastern Sugar."[124]

Pursuant to the UNCITRAL Arbitration Rules, it was the role of the arbitral tribunal to determine on its own whether or not it had jurisdiction over the dispute.[125] The tribunal noted that neither the Europe Agreement, under which the Czech Republic became a candidate for EU accession, nor the Accession Treaty, pursuant to which the Czech Republic ultimately acceded to the EU, "provide *expressly*" that the BIT would be terminated.[126] Furthermore, the BIT itself did not state that it would be

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119. *See* Potesta, *supra* note 19, at 227.

120. *See* Eastern Sugar, *supra* note 112, ¶¶ 335–338. *See also* Agreement on encouragement and protection of investments, Czech Republic-Netherlands, *supra* note 113, art. 3(1) (stating that "[e]ach Contracting Party shall ensure fair and equitable treatment to the investors of the other Contracting Party and shall not impair, by unreasonable or discriminatory measures, the operation, management, maintenance, use, enjoyment or disposal thereof by those investors").

121. *See* Eastern Sugar, *supra* note 112, ¶ 368.

122. *See* Marek Wierzbowski & Aleksander Gubrynowicz, *Conflict of Norms Stemming from Intra-EU BITs and EU Legal Obligations: Some Remarks on Possible Solutions in* INTERNATIONAL INVESTMENT LAW FOR THE 21ST CENTURY 552–553 (2009).

123. *See* Eastern Sugar, *supra* note 112, ¶ 112.

124. *Id.* ¶ 117.

125. *Id.* ¶ 116.

126. *Id.* ¶ 143.

terminated in the case that both parties became EU Member States.[127] The arbitral tribunal proceeded to analyze the relationship between the Czech Republic-Netherlands BIT and the EC Treaty under the Vienna Convention on the Law of Treaties ("VCLT").[128]

Under Article 42 of the VCLT, a treaty is only terminated according to its own terms, or the terms of the VCLT.[129] Article 59 of the VCLT provides that a treaty is terminated if 1) all the parties to it conclude a later treaty relating to the "same subject matter," 2) the later treaty established that the parties "intended to be governed by that treaty," or 3) 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."[130] The arbitrators concluded that none of these conditions were

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127. *See* Agreement on Encouragement and Protection of Investments, Czech Republic-Netherlands, *supra* note 113, art. 13(2) ("Unless notice of termination has been given by either Contracting Party at least six months before the date of the expiry of its validity, the present Agreement shall be extended tacitly for periods of ten years, each Contracting Party reserving the right to terminate the Agreement upon notice of at least six months before the date of expiry of the current period of validity").

128. Vienna Convention on the Law of Treaties, *opened for signature* May 23, 1969, 115 U.N.T.S 331 (entered into force on Jan. 27, 1980) [hereinafter Vienna Convention]. The Vienna Convention is a treaty concerning customary international law on treaties between states, and is binding upon its signatories. As of May 2009, it has been ratified by 109 parties, including the Czech Republic and the Netherlands. The treaty provides the general rules for treaty interpretation.

129. Vienna Convention, *supra* note 128, art. 42. Article 42 of the Vienna Convention, *Validity and continuance in force of treaties*, reads in its entirety:

> (1) The validity of a treaty or of the consent of a State to be bound by a treaty may be impeached only through the application of the present Convention.
>
> (2) The termination of a treaty, its denunciation or the withdrawal of a party, may take place only as a result of the application of the provisions of the treaty or of the present Convention. The same rule applies to suspension of the operation of a treaty.

130. Vienna Convention, *supra* note 128, art. 59. Article 59 of the Vienna Convention, *Termination or suspension of the operation of a treaty implied by conclusion of a later treaty*, reads in its entirety:

> (1) A treaty shall be considered 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;

met, and affirmed the tribunal's jurisdiction over the proceedings.[131] Thus, the tribunal held that "EU law has not *automatically* superseded the BIT as a result of the accession of the Czech Republic to the EU."[132]

Considering the number of intra-EU BITs currently in force and the potential for the interaction between those BITs and the EU legal order to be a factor raised in future arbitral proceedings, the *Eastern Sugar* decision is significant beyond this particular tribunal's decision. The EC Commission has pressured the Member States to terminate, or at the very least to renegotiate, the BITs to which they are a party in order to avoid the disparate obligations that stem from the BITs and EU Law.[133] The Commission takes the position that "there appears to be no need for agreements of this kind in the single market" because "it would appear that their content is superseded by Community law."[134] Some countries have followed this suggestion.[135] For example, in 2008, the BIT between Italy and Hungary was terminated, and in 2009, the Czech Republic initiated the termination process for 23 BITs it had concluded with EU Member States prior to its EU-accession.[136]

However, the majority of Member States believe that the existing BIT framework should be maintained.[137] According to their position, Member States should be able to conclude treaties amongst themselves, and those

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> (2) The earlier treaty shall be considered as only suspended in operation if it appears from the later treaty or is otherwise established that such was the intentions of the parties.

131. *See* Eastern Sugar, *supra* note 112, ¶¶ 159–171.

132. *See id.* ¶ 172; *see also* Soderlund, *supra* note 21, at 455 (stating that in future scenarios like that of *Eastern Sugar* in which host states raise the jurisdictional defense that a BIT is no longer operative because it became an intra-EU BIT, these foreign investors will be likely unsuccessful in invoking this defense).

133. *See* Wierzbowski, *supra* note 122, at 555.

134. EU Members Review Intra-European BITs in Light of Potential Overlap with EU Law, INVESTMENT TREATY NEWS, 20 June 2007.

135. *See id*; *see also* Alfred Escher, *Current Developments, Legal Challenges an Definition of FDI, in* LEGAL ASPECTS OF FOREIGN DIRECT INVESTMENT 16–19 (Daniel D. Bradlow & Alfred Escher eds., 1999) for a brief discussion of the EU's goal of "furtherance of economic integration and the facilitation of cross-border investments within the EU." *Id.* at 18.

136. *See* UNCTAD, *Recent Developments in International Investment Agreements, supra* note 16, at 5; *see also Bilateral Investment Treaties and the EU*, http://www.cms-aacs.com/bilateral-investment-treaties-and-the-eu-05-26-2009 (last visited Dec. 16, 2009) (stating that despite a degree of uncertainty regarding the interface between intra-EU BITs and the EU legal order, the Czech Republic should reconsider its plans to terminate its intra-EU BITs, as they provide comfort to foreign investors).

137. *See EU Member States Reject the Call to Terminate Intra-EU Bilateral Investment Treaties,* INVESTMENT TREATY NEWS, 10 February 2009.

treaties currently in force between Member States should remain so as long as the Member States comply with their obligations under the EC Treaty.[138] At this time, the issue has not been brought to the European Court of Justice ("ECJ"),[139] and thus, the potential for inconsistent decisions by arbitral tribunals leaves the status of intra-EU BITs unclear.[140]

C. Extra-EU BITs

Incompatibility problems also arise in the context of extra-EU BITs. Under Article 307(2) of the EC Treaty, Member States "shall take all appropriate steps to eliminate the incompatibilities" between their treaty obligations with non-EU countries and their obligations under the EC Treaty.[141] This treaty provision suggests that recently acceded Member States must renegotiate their BITs with non-EU Member States in order to eliminate inconsistency with EU law.[142] However, under Article 307(1) of the EC Treaty, the "rights and obligations arising from agreements . . . or acceding States, before the date of their accession, between one or more Member State on the one hand, and one or more third countries on the other, shall not be affected by the provisions of this Treaty."[143] Nonetheless, several Member States have followed the suggestion of the Commission. For example, in 2003, the European Commission, the United States, and eight Central Eastern European Countries preparing to join the European Union, signed a Memorandum of Understanding (MOU), which ensured that the BITs concluded between the U.S. and these acceding countries were compatible with the EU's laws and regula-

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138. *See* Lorenza Mola, *Which Role for the EU in the Development of International Investment Law?* para. 5.1 (Soc'y of Int'l Econ. Law, Working Paper No. 27/08, 2008), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1154583.

139. The jurisdiction of the ECJ includes the power to bring enforcement actions against Member States. In the future the European Commission may bring a direct action against Member States that it deems are failing to fulfill its obligations under EU law by refusing to terminate intra-EU BITs. *See* DAVIES, *supra* note 78, at 40–41; *see also* CHOW & SCHOENBAUM, *supra* note 27, at 125 (stating that the ECJ consists of one judge from each EU Member State and has the final word in interpreting the EC Treaty).

140. *See* Potesta, *supra* note 19, at 238.

141. EC Treaty, *supra* note 22, art. 307.

142. *See* UNCTAD, *Recent Developments in International Investment Agreements, supra* note 16, at 5 (stating that "in 2008 the Czech Republic concluded five protocols on the amendment to originals BITs, a process reported as negotiations of BITs. These negotiations are in response to article 307 of the Treaty establishing the European Community (EC Treaty) and seek to bring the country's BITs into conformity with EU law"); *see also* UNCTAD, *World Investment Report 2003: FDI Policies for Development; National and International Perspectives, supra* note 3, at 59 (stating that "EU-accession countries will have to harmonize their FDI regimes with EU regulations").

143. EC Treaty, *supra* note 22, art. 307.

tions.[144] While the MOU represents forward progress in the elimination of existing incompatibilities, it does not have legal force and only applies to the specific BITs designated in the memorandum.[145] For that reason, all other extra-EU BITs remain susceptible to compatibility issues.[146]

The incompatibility problems arising from the relationship between the EU legal order and extra-EU BITs were recently addressed in *European Commission v. Republic of Austria*[147] and *European Commission v. Republic of Sweden*.[148] In these cases, the European Commission brought infringement proceedings under Article 307(2) of the EC Treaty against Austria and Sweden; the Commission alleged that the countries had failed to harmonize provisions contained in BITs with non-EU Member States negotiated prior to their accession to the EU with EU law.[149] Prior to their accession to the EU, Austria and Sweden entered into BITs with several non-European countries.[150] All of these BITs contained clauses "under which each party guarantee[d] to the investors of the other party . . . the free transfer . . . of payments connected with an investment."[151] In

144. *See Eight Acceding Countries and U.S. Sign Bilateral Investment Understanding,* EUR. UNION DELEGATION TO THE U.S.A. (Sept. 23, 2003), http://www.eurunion.org/eu/index.php?option=com_content&task=view&id=2079&Itemid=58 (stating that "A number of provisions in the BITs were contrary to the existing EU legislation and needed to be amended prior to accession. The acceding countries concerned are Bulgaria, Czech Republic, Estonia, Latvia, Lithuania, Poland, Romania and Slovakia. The European Commission is pleased that a satisfactory solution has been found, showing that EU enlargement can be beneficial to third countries").

145. *See* Radu, *supra* note 17, at 238.

146. *See id.*

147. *See* C-205/06, European Commission v. Republic of Austria, [2009] E.C.R. [hereinafter Austria Proceedings].

148. *See* C-249/06, European Commission v. Republic of Sweden, [2009] E.C.R. [hereinafter Sweden Proceedings].

149. *See* Austria Proceedings, *supra* note 147; Sweden Proceedings, *supra* note 148; *see also* EC Treaty, *supra* note 22, art. 226 (explaining that if the Commission believes that a Member State has failed to fulfill an obligation under the EC Treaty, it shall give the country formal notice of its opinion on the matter and provide the country with the opportunity to submit its own observations. If the country does not comply with the Commission's opinion, the Commission can commence infringement proceedings against a Member State which it believes has infringed upon Community law); EC Treaty, *supra* note 22, art. 230 (stating that the ECJ has jurisdiction over infringement proceedings brought by the European Commission against Member States); Potesta, *supra* note 19, at 238.

150. *See* Austria Proceedings, *supra* note 147, ¶ 1 (listing the countries that Austria entered into BITs with prior to its EU-accession); Sweden Proceedings, *supra* note 148, ¶ 1 (listing the countries that Sweden entered into BITs with prior to its EU-accession).

151. *See* Austria Proceedings, *supra* note 147, ¶ 3; Sweden Proceedings, *supra* note 148, ¶ 3.

both cases, the Commission objected to these clauses, maintaining that they precluded Austria and Sweden from complying with their obligations under the EC Treaty.[152] Because these EC Treaty provisions guaranteed the free transfer of capital, they clashed with Article 57(2),[153] Article 59,[154] and Article 60[155] of the EC Treaty, which enable the EU to regulate movement of capital between EU Member States and non-EU countries, as well as restrict the flow of capital in exceptional circumstances.[156] Thus, the Commission argued that Austria and Sweden failed to take appropriate steps to eliminate incompatibilities with their obligations under these BITs and under the EC Treaty.[157]

The major point of contention in *European Commission v. Republic of Austria* and *European Commission v. Republic of Sweden* was the extent to which Article 307(2) of the EC Treaty requires Member States to ensure that their BITs with non-EU countries comply with EU law.[158] In regards to the pertinent EC Treaty articles, the Commission had never before had the opportunity to exercise its powers.[159] In other words, no situation had ever arisen in which the Commission found it necessary to exercise its competence and adopt measures pursuant to Article 57(2), Article 59, or Article 60 of the EC Treaty. Therefore, the incompatibility alleged by the Commission was "merely hypothetical until the Council adopt[ed] the relevant provisions."[160] The Commission argued that the Member States were required to eliminate even potential compatibilities

152. *See* Austria Proceedings, *supra* note 147, ¶ 6; Sweden Proceedings, *supra* note 148, ¶ 6.

153. *See* EC Treaty, *supra* note 22, art. 57(2). Under Article 57(2), the European Council may adopt measures on the movement of capital to and from non-EU countries "which constitute a step back in Community law as regards the liberalisation of the movement of capital to or from third countries."

154. *See* EC Treaty, *supra* note 22, art. 59. Under Article 59, the Council may take safeguard measures restricting capital flows to non-EU countries in "exceptional circumstances" if it deems such measures to be "strictly necessary."

155. *See* EC Treaty, *supra* note 22, art. 60. Under Article 60, the Council may "take the necessary urgent measures on the movement of capital and on payments as regards the third countries concerned."

156. *See* Austria Proceedings, *supra* note 147, ¶ 11; Sweden Proceedings, *supra* note 148, ¶ 11.

157. *See* Austria Proceedings, *supra* note 147, ¶ 6; Sweden Proceedings, *supra* note 148, ¶ 6.

158. *See* Potesta, *supra* note 19, at 241.

159. *Id.* at 238.

160. *Id.* at 241.

when Article 307 is read in conjunction with Article 10 of the EC Treaty.[161] Article 10 sets forth a duty of loyalty and cooperation, under which:

> Member States shall take all appropriate measures, whether general or particular, to ensure fulfillment of the obligations arising out of this Treaty or resulting from action taken by the institutions of the Community. They shall facilitate the achievement of the Community's tasks. They shall abstain from any measure which could jeopardize the attainment of the objectives of this Treaty.[162]

While the ECJ did not adopt the Commission's reasoning, it nevertheless held that the Member States had breached their obligations under Article 307 of the EC Treaty.[163]

As was the case in *Eastern Sugar,* the implications of the court's decisions extend beyond the BITs concluded by Austria and Sweden, as other EU Member States are parties to hundreds of BITs with non-EU countries. In its judgments, the ECJ clarified that its holding does not apply only to Austrian and Swedish BITs entered into with non-EU countries, but to all Member States that are parties to BITs containing similar provisions.[164] In general, the judgments reflect a broad interpretation of Article 307, suggesting that Member States must eliminate even potential incompatibilities between the BITs and EC law.[165] In this way, endless scenarios for incompatibility can be envisioned.[166] Unless the Council takes it upon itself to bring infringement proceedings against Member States that are encroaching on EU law through their BITs, the individual Member States are unlikely to examine their BITs on their own accord, identify potential incompatibilities, and then work with the non-EU country to amend the treaty.[167]

III. BITS AND THE EU LEGAL ORDER POST-LISBON

On December 1, 2009, the Lisbon Treaty entered into effect.[168] The treaty amends the current principal sources of law of the EU, namely the

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161. *See* Austria Proceedings, *supra* note 147, ¶ 11; Sweden Proceedings, *supra* note 148, ¶ 11.

162. *See* EC Treaty, *supra* note 22, art. 10.

163. *See* Austria Proceedings, *supra* note 147, ¶ 45; Sweden Proceedings, *supra* note 148, ¶ 45.

164. *See* Austria Proceedings, *supra* note 147, ¶ 43; Sweden Proceedings, *supra* note 148, ¶ 43.

165. *See* Potesta, *supra* note 19, at 243.

166. *See id.*

167. *See id.* at 237.

168. *See Treaty of Lisbon: Taking Europe into the 21st Century*, EUROPA.EU, http://europa.eu/lisbon_treaty/index_en.htm (last visited June 1, 2010); *see also* Dan Bi-

EC Treaty and the EU Treaty.[169] After years of debate, the Lisbon Treaty extends EU competence to the fields of trade and services, trade related aspects of intellectual property, and, in a "major innovation, to foreign direct investment."[170] These fields are all brought within the ambit of the Common Commercial Policy ("CCP"), the section of the Lisbon Treaty which establishes the basis of the EU's legal position in its international economic relations, as well as one of the few areas in which the EU retains exclusive competence.[171] This marks a significant departure from the EC Treaty prior to the Lisbon amendments, under which the CCP only extended to the field of external trade.[172] In this way the Lisbon Treaty "reflects a new governance arrangement and legal order that was not contemplated by the current investment system."[173]

Because the Lisbon Treaty very recently entered into effect, it remains to be seen how its new provisions under the CCP will be interpreted and applied. However, the Lisbon Treaty certainly has the potential to present considerable implications for the relationship between the EU legal order and the system of BITs with respect to the contentious realm of FDI.[174] While neither the EC Treaty nor the EU Treaty contain provisions specifically referencing FDI, Article 206 and Article 207(1) of the Lisbon Treaty unequivocally bring FDI under the auspice of the CCP.[175] The

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lefsky & Stephen Castle, *Way is Clear to Centralize Europe's Power,* N.Y. TIMES, Nov. 4, 2009, at A6 (stating that on November 3, 2009, the Lisbon Treaty "cleared its last major hurdle," as the president of the Czech Republic was the last European leader to sign the treaty).

169. *See Treaty of Lisbon: Taking Europe into the 21st Century, supra* note 168.

170. *See* Stephen Woolcock, *The Potential Impact of the Lisbon Treaty on European Union External Trade Policy*, SWEDISH INST. FOR EUR. POL'Y ANALYSIS, June 2008, at 1.

171. *See* Bungenberg, *supra* note 28, at 124.

172. EC Treaty, *supra* note 22, art. 133.

173. *See* L. Yves Fortier, Chairman, Address at the British Institute of International and Comparative Law 50th Anniversary Series, Investment Protection and the Rule of Law: Change or Decline? (Mar. 17, 2009).

174. *See* Woolcock, *supra* note 170, at 4.

175. *See* Lisbon Treaty, *supra* note 25. The Lisbon Treaty inserts the new heading "External Action by the Union." Under this heading, Title II sets forth the "Common Commercial Policy." Article 131 of the EC Treaty, *supra* note 22, read: "By establishing a customs union between themselves Member States aim to contribute, in the common interest, to the harmonious development of world trade, the progressive abolition of restrictions on international trade and the lowering of customs barriers." Under the Lisbon Treaty, this wording is replaced by the following: "By establishing a customs union in accordance with Articles 23 to 27, the Union shall contribute, in the common interest, the harmonious development of world trade, the progressive abolition of restrictions on international trade and on *foreign direct investment*, and the lowering of customs and other barriers." Article 133(1) of the EC Treaty read: "The common commercial policy shall be based on uniform principles, particularly in regard to changes in tariff rates, the conclu-

Lisbon Treaty adds the term "foreign direct investment" within the scope of coverage of the CCP, but the intent of this language is ambiguous, and, thus, it remains unclear whether these FDI provisions in effect circumscribe the existing domestic competence of the Member States.[176] In other words, it is uncertain whether the Lisbon Treaty grants the EU exclusive competence over liberalization, protection, and promotion of FDI,[177] or only to the liberalization of FDI[178] in general.[179] At the same time, employing a strict textual reading, the language of the Lisbon Treaty now grants the EU exclusive power over the field of FDI, and does not cite any exceptions.[180]

IV. PROBLEMS ARISING FROM THE TRANSFER OF COMPETENCE OVER FDI AND SOME PROPOSED SOLUTIONS

The EU's objective in bringing FDI under the auspice of the CCP is to improve efficiency in foreign investment negotiations, and to eliminate the complications that arise from a system of intertwined competences.[181] However, this aim will be thwarted if there is an expedited overhaul of the current legal structure for the protection of foreign investment. If the EU seeks to improve its competitive position in the global economy as an

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sion of tariff and trade agreements, the achievement of uniformity in measures of liberalization, export policy and measures to protect trade such as those to be taken in the event of dumping or subsidies." Under the Lisbon Treaty, this is replaced as follows: "The common commercial policy shall be based on uniform principles, particularly with regard to changes in tariff rates, the conclusion of tariff and trade agreements relating to trade in goods and services, and the commercial aspects of intellectual property, *foreign direct investment*, the achievement of uniformity in measures of liberalization, export policy and measures to protect trade such as those to be taken in the event of dumping or subsidies. The common commercial policy shall be conducted in the context of the principles and objectives of the Union's external action." (emphasis added). Furthermore, the Lisbon Treaty adds the following language: "For the negotiation and conclusion of agreements in the field of trade in services and the commercial aspects of intellectual property, as well as *foreign direct investment*, the Council shall act unanimously where such agreements include provisions for which unanimity is required for the adoption of internal rules." (emphasis added).

176. *See* Eilmansberger, *supra* note 20, at 394.

177. Significantly, the liberalization, promotion and protection of FDI are considered the three fundamental goals of BITs. *See* Salacuse & Sullivan, *supra* note 5, at 68.

178. Investment liberalization generally refers to the creation of an investment climate in which foreign investors undertake investments that they judge to be in *their* interest rather than in the interest of the host country. *See id.* at 78–79.

179. *See* Mola *supra* note 138, para. 3.2.

180. Bungenberg, *supra* note 28.

181. *See supra* Part II; *see also* Ceyssens, *supra* note 95, at 269 ("[T]he current procedures involving both Member States and the EU in the conclusion and implementation of international agreements are excessively burdensome").

economic superpower, it needs to maintain a transparent, stable system for the regulation of foreign investment.[182] If foreign investors believe that the EU's system does not provide adequate protection, they may choose to retract their investments. This will make it difficult for the EU to attract new foreign investors who will likely forego opportunities in the EU to avoid the problems associated with an unstable investment regime. Furthermore, the BITs entered into by EU Member States are part of a dense international network of BITs, and a disruption of this system could be detrimental to the EU's foreign relations. Therefore, in responding to the challenges that lie ahead, it is crucial that the EU make a gradual, deliberate transition from a system in which Member States have the competence to conclude BITs, to a system in which the EU retains exclusive competence over FDI. While the transfer of competence over FDI from the individual EU Member States to the EU creates a number of problems, if these problems are adequately dealt with, then the changes to FDI embodied in the Lisbon Treaty will represent an improvement over the EU's prior international investment regime.

A. Will EU Member States Retain the Competence to Negotiate and Conclude BITs in the Future?

Article 207 of the Lisbon Treaty does not define the scope of the EU's authority over FDI, leaving the provision open to disparate interpretations.[183] According to Dr. Stephen Woolcock, some Member States interpret Article 207 to grant the EU exclusive competence over FDI only as it relates to investment liberalization.[184] Under this narrow interpretation, the EU would have exclusive power to negotiate and conclude international investment agreements providing for pre-establishment national treatment,[185] but not to the protection of foreign investment once it has entered the country.[186] Therefore, Member States would retain their competence to conclude BITs. Alternatively, some Member States, as

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182. *See* Bungenberg, *supra* note 28, at 125 ("Economic growth, employment and prosperity can only be achieved if the EU itself is competitive on the international level, which from a legal point of view is primarily determined by its constitutional basis and options").

183. *See* Woolcock, *supra* note 170, at 4; *see also* Alexandrov, *supra* note 18.

184. *See* Woolcock, *supra* note 170, at 4.

185. *See* OECD, STABILITY PACT: SOUTHEAST EUROPE COMPACT FOR REFORM, INVESTMENT, INTEGRITY AND GROWTH, 11 (Oct. 2003) ("National treatment in pre-establishment is the commitment of a (host) country to accord to the investment by non-resident enterprises in its territory, including the right of establishment, treatment no less favourable than that accorded in like situations to resident enterprises.")

186. *See* Woolcock, *supra* note 170*,* at 4.

well as the Commission, interpret Article 207 more broadly, so that FDI includes both investment liberalization and investment protection.[187] Under this broader interpretation, EU Member States would no longer be able to negotiate and conclude BITs on their own, as the substantive aspects of investment protection would fall exclusively under the competence of the EU.[188] Because these two interpretations have such different implications for the future of the EU's international investment policy, there is a need for legal certainty.

The EU must approach this issue pragmatically. If the EU adopts the narrow interpretation of Article 207, then it will not achieve its objectives in bringing FDI under the auspice of the CCP. This is because the EU would still need to deal with the incompatibility and inconsistency problems that arise from a system of shared competence.[189] On the other hand, the EU's adoption of the broader interpretation of Article 207 would entail an immediate, disruptive overhaul of the legal infrastructure created by the BIT network. In order to avoid these problems, the EU should adopt the broader interpretation so that both the liberalization and the protection of FDI fall under the competence of the EU, but the EU should exercise its newfound competence gradually.

While the Lisbon Treaty itself does not provide for any kind of transition period, this does not prevent the EU from establishing one. In *Donckerwolcke v. Procureur de la Republique,*[190] the ECJ held that even though the EU has exclusive competence with regard to the CCP, derogation is permitted where the EU specifically authorizes the Member States to act.[191] Thus, the EU could authorize the Member States to continue to negotiate and conclude BITs, but could establish a definitive timeline so that eventually the Member States will no longer have this power. This approach will enable the EU to articulate its long-term objective by stating that it retains the exclusive authority over all aspects of FDI, but is temporarily deviating from this policy in order to ensure a smoother transition to a system of exclusive competence. This type of transition period will make the policy clear to non-EU countries, prepare EU Member States and foreign investors for what is to come, and avoid an immediate overhaul of a well-established system. By gradually phas-

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187. *Id.*
188. *See supra* Part II.C.
189. *Id.*
190. *See* C-41/76, Donckerwolcke v. Procureur de la République [1976] E.C.R. 1921.
191. *See id.* ¶ 32 ("As full responsibility in the matter of the commercial policy was transferred to the Community by means of Article 113(1) measures of commercial policy of a national character are only permissible . . . by virtue of specific authorization by the Community").

ing out BITs, the EU will have the opportunity to further develop its own foreign investment policy and conclude international investment treaties that provide foreign investors with adequate protection.

Finally, the EU should also commence discussions on "portfolio investment," which is not encompassed by the EU's authority over FDI.[192] Many BITs provide for an expansive definition of "investment," which includes "portfolio investment."[193] Therefore, by explicitly referring only to FDI in the CCP, the Lisbon Treaty leaves some types of foreign investment outside the scope of the EU's exclusive competence. This will most likely permit individual Member States to continue to conclude BITs, albeit only in terms of the regulation of portfolio investment. While the Lisbon Treaty aims for a streamlined approach in the conclusion of these types of agreements, the EU's failure to conclude comprehensive agreements pertaining to foreign investment will certainly frustrate this objective by maintaining a fragmented system. Foreign investors will need to enter into investment agreements with the EU for the protection of FDI, and will separately need to enter into bilateral agreements with the individual Member States in order to protect their portfolio investments.

B. What is the Legal Status of Existing BITs Concluded by EU Member States?

Another problem arising from the transfer of competence over FDI from Member States to the EU is the unclear legal status of existing BITs between EU Member States and non-EU countries. Pursuant to Article 307(2) of the EC Treaty, EU Member States "shall take all appropriate steps to eliminate the incompatibilities" between their treaty obligations with non-EU countries and their obligations under the EC Treaty.[194] Article 351 of the Lisbon Treaty incorporates this exact language.[195] Therefore, EU Member States must ensure that incompatibilities stemming from their BIT obligations with non-EU countries conform to EU law now that the EU has been granted exclusive competence over FDI. If an expansive definition of FDI were adopted, then it would appear that in order to conform to Article 351, Member States must either terminate their BITs or dramatically amend their provisions, as they deal predomi-

192. See *supra* Part II.B.
193. *See id.*
194. *See* EC Treaty, *supra* note 22, art. 307(2).
195. *See* Lisbon Treaty, *supra* note 25, art. 351.

nantly with FDI. However, this is impractical given the number of BITs to which Member States are parties.[196]

Furthermore, requiring EU Member States to terminate their BITs is contrary to customary international law.[197] Under Article 27 of the VCLT, "a party may not invoke the provisions of its internal law as justification for its failure to perform a treaty."[198] Under Article 42 of the VCLT, "the termination of a treaty, its denunciation or the withdrawal of a party, may take place only as a result of the application of the provisions of the treaty or the present Convention."[199] Under Article 59 of the VCLT:

> [A] treaty shall be considered as terminated if all the parties to it conclude a later treaty relating to the same subject matter and . . . it appears from the later treaty or is otherwise established that the parties intended that the matter should be governed by that treaty . . . or the provisions of the later treaty are so far incompatible with those of the earlier one that the two parties are not capable of being applied at the same time.[200]

Based on these VCLT provisions, Member States cannot be legally forced to terminate their BITs.

The majority of BITs provide that the agreement shall remain in force for a period of ten years, and at the end of each ten-year period either party may choose to terminate the BIT by providing notice to the other party.[201] Furthermore, BITs often provide that if a party terminates a BIT according to its terms, the investments covered by its provisions will continue to be protected under the agreement for a specified number of years.[202] Forcing EU Member States to immediately terminate their BITs would be at odds with Article 42 of the VCLT because termination must be governed by the termination terms contained within each individual BIT. Furthermore, Article 59 is inapplicable because the non-EU Member States that are parties to the BITs with EU Member States are not

196. *See* Bungenberg, *supra* note 28, at 135 (Of the nearly 2,600 BITs concluded worldwide, the 27 EU Member States are parties to 1,300 of those treaties).

197. *See* Vienna Convention, *supra* note 128.

198. *Id.* art. 27.

199. *Id.* art. 42.

200. *Id.* art. 59.

201. For example, in the BIT concluded between Pakistan and Germany, the provision related to termination reads: "[This Agreement] shall remain in force for a period of ten years and shall continue in force thereafter for an unlimited period unless notice of termination is given in writing by either Party on year before it expiry." Pak.−F.R.G. BIT, *supra* note 15, art. 13(2).

202. *Id.* art. 13(3) ("In respect of investments made prior to the date of expiry of the present Treaty, the provisions of Articles 1 to 13 shall continue to be effective for a further period of ten years from the date of expiry to the present Treaty").

also parties to the Lisbon Treaty. While the Lisbon Treaty arguably covers the same subject matter, the Lisbon Treaty is not binding on these countries and, therefore, cannot supersede existing BITs.

Because it would be both impractical and contrary to international law to call for the immediate termination of extra-EU BITs, an interim system needs to be established in order to facilitate a gradual transition to exclusive EU competence over FDI. This could be accomplished by allowing the BITs to terminate according to their own terms. At the end of the ten-year periods, the EU Member States could give notice to the other party that they intend to terminate the respective treaty. As these BITs expire, they can then be replaced by agreements negotiated and concluded by the EU. At the same time, Member States must ensure, as is required by Article 307 of the EC Treaty and now Article 351 of the Lisbon Treaty, that their BITs comply with all other provisions of EU law.[203] If not, these EU Member States should renegotiate and amend these treaties.[204] This approach is in the best interest of the EU because it will reduce the likelihood that foreign investors withdraw their investments in EU countries out of the concern that these investments are not protected under an investment treaty. Furthermore, EU Member States will be complying with customary international law under the VCLT, and therefore will not be destroying their legitimacy and harming their relations with foreign countries.

C. Is the EU Capable of Concluding International Investment Agreements Comparable to BITs?

Prior to the Lisbon Treaty entering into force, the EU negotiated treaties addressing investment-related issues, but none which dealt exclusively and comprehensively with the liberalization and protection of a broad range of investments.[205] These EU treaties differ significantly from BITs which provide for both substantive and procedural protections of foreign investment.[206] Because the EU is not accustomed to negotiating and concluding BITs, it could take the transition period proposed in the previous two sections of this Note to further develop its investment policy platform. It could create a "Model International Investment Agreement" that contains provisions comparable to those contained in BITs.

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203. *See* EC Treaty, *supra* note 22, art. 307(2); *see also* Lisbon Treaty, *supra* note 25, art. 351.

204. *See supra* Part II.C. The ECJ Infringement Proceedings Brought Against Austria and Sweden did not only apply to those two particular countries, but rather the decision applies to all EU Member States.

205. *See supra* Part II.A.

206. *Id.*

This model agreement should provide for the main substantive protections afforded under BITs, including national treatment, most favored nation, compensation for expropriation, and rights to transfer capital and returns.[207] In particular, the EU should develop a procedural mechanism for the settlement of investment disputes that will likely arise under its newly negotiated and concluded agreements.[208] By taking these steps, the EU will be able to maintain a stable regime for the regulation of foreign investment. If not, foreign countries will be reluctant to enter into investment agreements with the EU that do not provide for conditions as favorable as those provided under BITs.

The EU does not currently have an international dispute settlement regime comparable to the ad hoc system prescribed in BITs.[209] Therefore, as the situation stands, foreign investors would need to bring their investment dispute claims against the EU before the ECJ.[210] According to Peter Ondrusek, a consultant for the United Nations Industrial Development Organization:

> [T]here are not necessarily any real obstacles in principle for the EC to become a party to an international investment-dispute arbitration system. However, there are some obstacles on the part of the current international investor-State arbitration system to be able to accommodate reliably the EC.[211]

The main forum chosen for dispute settlement under BITs is the International Centre for Settlement of Investment Disputes (ICSID).[212] However, the EU is not a party to the ISCID.[213] Under Article 67 of the ICSID Convention, the convention is open for signature on behalf of States that are members of the International Bank for Reconstruction and Development, as well as States that are parties to the Statute of the International Court of Justice and have been invited to sign the convention by the Administrative Council of the International Centre for Settlement of Investment Disputes.[214] While the EU is not a state, it should neverthe-

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207. *See supra* Part I.B.

208. *See* Wierzbowski, *supra* note 122, at 546 ("[I]n many ways a BIT, with its unique opportunity to force a host State to respond to arbitrators, is a clear advantage and no comparable mechanism is at investors' disposal under EC law rules").

209. Mola, *supra* note 138, at para. 1.5.

210. *Id.*

211. *See* Peter Ondruskek, *EC and Investor-State Dispute Settlement: Some Thoughts,* a paper delivered at the BIICL, Investment Treaty Forum: European Law and Investment Treaties: Exploring the Grey Areas, (Dec. 4, 2008).

212. *See* ICSID Convention, *supra* note 68.

213. *See id.* art. 25 for a list of all the parties to the ICSID Convention.

214. *Id.* art. 67.

less attempt to become a party to an impartial investment dispute forum.[215] This way, as BITs concluded by EU Member States are gradually phased out, foreign investors will still have access to the procedural mechanisms that make BITs such attractive agreements.

CONCLUSION

This Note has explored the nature of the relationship between BITs concluded by EU Member States and the EU legal order, and the potential impact on this interface now that the Lisbon Treaty has entered into force. It remains to be seen how the challenges of the EU's international investment system will be resolved in the future. Prior to the passage of the Lisbon Treaty, a system of shared competence in the realm of foreign investment led to incompatibility and overlap issues that made it difficult for the EU to act as a united front. At the same time, this BIT network has been in place for over five decades and provides benefits to countries seeking to attract foreign investors, as well as to foreign investors who seek protection against the inherent risks associated with their investments. While the Lisbon Treaty brings FDI under the auspice of the Common Commercial Policy, the simple addition of the term "foreign direct investment" does not indicate how the EU's exclusive competence over FDI will be interpreted and applied, and whether or not it is intended to completely displace the current BIT network.

Because of the need for legal certainty, the EU's current system of BITs should remain intact in the short term, as it provides for investment protection and arbitral dispute mechanisms of which there are no viable equivalents under the Lisbon Treaty. While the EU's exclusive competence over FDI is a logical step in the movement toward a more streamlined, comprehensive multilateral EU trade and investment system, an expedited overhaul of the current legal structure would foster uncertainty and be detrimental to the EU's continued ability to attract FDI and manage foreign-investor expectations. It would be imprudent to immediately do away with the standing BIT system until the EU is able to develop a stable and transparent international investment framework. Therefore, the EU should implement a transition period in which it can gradually adapt to its new, exclusive authority to negotiate and conclude international investment treaties. Dr. Stephen Woolcock states, "The inclusion of FDI in EU competence is an important step towards the creation of a comprehensive EU approach to trade and investment that reflects the nature of the international economy in which trade and investment are

215. *See supra* Part I.B.

inextricably linked."[216] The EU must take gradual and deliberate action in order to improve its international investment regime.

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216. Woolcock, *supra* note 170, at 5.

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