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THE EU APPROACH TO INTERNATIONAL INVESTMENT POLICY AFTER THE LISBON TREATY

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DIRECTORATE-GENERAL FOR EXTERNAL POLICIES OF THE UNION

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STUDY

THE EU APPROACH TO INTERNATIONAL INVESTMENT POLICY AFTER THE LISBON TREATY

Abstract

The Lisbon Treaty extends exclusive European Union competence to foreign direct investment (FDI). After a transition period this should enable the EU to conclude either international investment agreements or comprehensive trade and investment agreements with third parties. This extension of the EU's competence offers the opportunity of promoting EU competitiveness in global markets through increased investment and better access to key third country markets. It also facilitates a greater European influence over international investment agreements a key instrument in any response to globalisation.

The EU will need to develop a coherent and balanced approach to investment if it is to make the most of these opportunities. In this the EU needs to address four major issues. First, the treaty provides no definition of FDI and thus the scope of EU exclusive competence. The EU institutions must therefore work towards a consensus on the scope of competence or how to manage mixed competence negotiations. Second, there is a need to define the main elements of an EU investment policy. This will involve agreement on standards for investment protection, dispute settlement and arbitral procedures as well as what the EU aims should be in terms of promoting 'sustainable investment.' Third, it will be necessary to decide on the basis of clear and objective criteria, which third countries should be given priority when it comes to negotiating EU level investment agreements. Finally, agreement must be found on how to manage the transition from member state bilateral investment treaties (BITs) to EU level investment agreements.

This study provides background on the nature of these challenges and discusses the options for EU policy.

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List of Abbreviations:

BIT	Bilateral Investment Treaty
CCP	Common Commercial Policy
COM	Commission
CONV	Convention on the Future of Europe
DG	Directorate General
EU	European Union
ECJ	European Court of Justice
FDI	Foreign Direct Investment
FTA	Free Trade Agreement
GATT	General Agreement on Tariffs and Trade
GATS	General Agreement on Trade in Services
IMF	International Monetary Fund
IIA	International Investment Agreement
IMF	International Monetary Fund
MNC	Multinational company
NAFTA	North American Free Trade Agreement
OECD	Organisation for Economic Cooperation and Development
TEU	Treaty on the European Union
TFEU	Treaty on the Functioning of the European Union
TRIMs	Trade Related Investment Measures
WTO	World Trade Organisation

EXECUTIVE SUMMARY

The Lisbon treaty's extension of EU exclusive competence to cover foreign direct investment (FDI) should enable the EU to conclude comprehensive trade and investment agreements, where in the past its coverage of investment has been only very partial. This should in turn strengthen the EU's ability to shape international investment policy. The greater negotiating leverage gained from negotiating comprehensive trade and investment agreements should also enable the EU to gain improved market access for EU investors in key target markets. Increase EU competence also means the EU will be able to establish uniform provisions for investors throughout the EU, in contrast to the current position in which investors in some member states have better protection in some markets than others.

The Lisbon Treaty extension of EU competence to cover investment will not however, bring about major changes in the short term. Change is likely to be progressive rather than dramatic with the EU progressively extending the number of EU investment agreements. In the interim member state bilateral investment treaties are likely to continue to remain in force.

- The European Parliament needs to consider two central issues:
- what should be the EU approach to international investment policy; and
- how can the transition from the current position with many member state bilateral investment treaties (BITs) to a common EU approach be managed?

Although the transitional arrangements are more short term, hence the more concrete nature of the proposed Regulation and the immediacy of the need for the European Parliament to reach a position, they cannot be separated from the question of what the EU approach should be. This is clear from the fact that the Commission intends already to seek a negotiating mandate to cover the inclusion of investment in the Comprehensive Economic and Trade Agreement it is negotiating with Canada.

The Lisbon Treaty does not define foreign direct investment. There is however a broad understanding that FDI implies control and is therefore different from portfolio investment, which is not covered by EU exclusive competence. The absence of a clear definition means that the scope of EU exclusive competence remains a potentially contentious issue. This situation is not new. The Treaty of Rome never defined the Common Commercial Policy with the result that the scope of EC de jure competence in the field of trade remained contentious. But disagreements over the scope of competence did not prevent the EC negotiating effectively on issues such as TBTs, procurement and services. This was possible because mutual trust and confidence between the Commission and the Council allowed the Commission to negotiate for the EC and member states on mixed agreements in consultation with the member states. The difference between the establishment of the CCP from the 1960s onwards and investment today is that the member states have existing investment policies in place with third countries. This was not the case for the mixed competence topics of the 1970s and 1980s. Nevertheless, the key to effective EU investment policy would still seem to be more likely found in the establishment of mutual trust and cooperation between the EU institutions, now including the European Parliament than in any specific text.

The approach to EU investment proposed by the Commission in its Communication appears to be in line with the stated aims of EU policy, such as in the form of the Global Europe Policy of 2006. In terms of the focus of EU initiatives, in other words the countries with which the EU should negotiate its first investment agreements, the approach proposed by the Commission appears to be in line with the criteria chosen. China, Russia and India represent countries with which the EU should consider negotiating comprehensive agreements, because of the need to gain access as well as strengthen and extend protection for EU investors in these markets. Canada and Singapore are already both relatively open and provide a high level of investor confidence, but with these countries the Commission proposes negotiating investment as part of wider agreements including market access and rules in trade topics. The Commission's proposed criteria also suggest a case for negotiating with some other countries such as the members of the GCC, Malaysia and South Africa.

The inclusion of FDI in exclusive EU competence should help to promote EU competitiveness in the sense that increased inward and outward investment can be expected to improve competitiveness. In an increasingly interdependent international economy characterised by global production and value chains, increased FDI is a means of ensuring that EU firms and the European economy as a whole can remain competitive in the face of shifting comparative advantage. The employment effects of such increased investment flows should, according to available research, be neutral. But the adjustment costs are likely to fall disproportionately on the low skilled. This raises the question of what can be done to provide adjustment assistance for this group of workers.

With regard to the standards of investment protection the existing EU member state BITs are less detailed in their definitions of scope of investment protection offered then in some more developed investment agreements. This appears to hold across the board for investment protection provisions, including core issues such as the scope for national treatment, MFN and fair and equitable treatment. The European agreements are also less precise in defining the scope for arbitration procedures and do not include provision for review of the decisions of arbitral tribunals.

- The options for an EU policy on investment protection standards are therefore broadly threefold:
- to retain the broad definitions of the existing member state BITs. This arguably provides for more investor protection, but leaves scope for arbitral tribunals to interpret and define the scope of the provisions.
- to argue for a comprehensive EU investment agreement that defines standards of protection and expectations of investors that reflect European norms; or
- to examine the various standards of protection and methods of dispute settlement and arbitration in detail and identify areas of best practice that best serve the interests of all EU stakeholders. Such an approach would include consideration of how a measure of public control over international investment law and arbitration could be re-established.

Coherence between EU investment policy and other policy areas such as sustainable development will also need careful consideration. Only one member state has included sustainable development provisions in its bilateral investment policy.

In terms of the transitional arrangements questions arise with regard to the compatibility of the existing member state BITs with; (a) the EU exclusive competence for FDI, (b) existing EU law and (c) the Union's future international investment policy. All translate into a non-negligible degree of legal uncertainty and might have repercussions on the confidence in the effectiveness of the existing BITs. The Commission's proposed Regulation purports to avoid legal uncertainty and reduce the risk of erosion of the present level of protection.

The proposed general authorisation of existing BITs would enhance legal certainty. But it is more questionable whether the proposed procedure allowing the Commission to scrutinize member state BITs, and if incompatible with EU law, direct Member States to amend or terminate them, would achieve this aim. The proposed publication of a list of authorised BITs whose authorisation could subsequently be withdrawn does not promise to enhance legal certainty. Similarly the proposed powers for the Commission to withdraw authorisation on the grounds that a BIT constitutes an obstacle to the development of the Union's policies in the field, will tend to add to rather than reduce the degree uncertainty. It is not clear what criteria would be used to justify withdrawal of authorisation in the latter case except for some clear statement of EU policy on IIAs and there is unlikely to be an EU model BIT to provide such criteria.

However, the proposed Regulation is legitimate in the sense that without a means of ensuring the transition from member state to EU exclusive competence as provided in the TFEU, member state reluctance to give up national BITs could block the evolution of EU policy. In turn, the absence of clear provisions for the transition could result in a default option of increased litigation by the Commission over the Member State's duty of loyal co-operation, which would be costly, time consuming and not provide the legal certainty sought by investors and member state governments. The option of setting a time limit on the life of member state BITs would need to consider how long it would take to negotiate EU agreements if these are to replace the member state BITs. Under international law, parties would, in any case, retain rights under member state BITs for anything up to 20 years. A third option would focus on process. Drawing on the experience with EC/EU external trade, EU policy on international investment will only be effective if the EU institutions, Commission, Council and Parliament, have trust in, and are content with, the decision making procedures for the pursuit of a common EU investment policy. Again drawing on the experience with trade, such trust can probably only be established over time and in the course of policy developments. The process option would therefore focus on who should make decisions on how to manage the transition from member states BITs with a third party to an EU agreement. This would involve a comitology procedure that would allow both the Council and the Parliament to intervene where they suspect an excess of powers by the Commission.

To sum up the options for the EU on transition are:

- to reject the project as granting the Commission too much and unchecked power in shaping the future investment policy of the Union;
- to support the Commission's project so as ensure that the Union's exclusive competence is effectively developed and implemented despite potential – and expected – resistance by numerous Member States; or
- to work towards an intermediate solution that would favour the development of the Union's policy on foreign investment by accepting the principle of a procedural framework as proposed by the Commission but with a modification that would allow the Council to retain the control over critical issues while, at the same time, ensuring a transparent public debate in the Parliament.

Part I Towards a European Union policy on foreign direct investment

1 THE IMPACT OF THE TREATY OF LISBON ON EU INVESTMENT POLICY: HOW TO MANAGE THE EVOLUTION?

The Treaty of Lisbon has extended the scope of the Common Commercial Policy (CCP) (Art. 206-207 TFEU) to the regulation of 'foreign direct investment' (FDI). This inclusion of FDI in exclusive EU competence is arguable long overdue. For many years it has been clear that investment has been as important if not more important than trade in goods and services in shaping how the EU engages with global markets. It has therefore been an anomaly that the EU has had no common approach to investment. Extending EU exclusive competence to include FDI now provides an opportunity to develop a common, comprehensive European Union approach to investment policy that can improve EU competitiveness and help obtain better access for EU investors in third markets; extend the protection afforded to EU outward investors beyond the existing member state bilateral investment treaties (BITs) and promote EU norms in the field of sustainable investment. These goals are however, unlikely to be achieved in the short term and will only be achieved if domestic (EU) stakeholders, member states and EU institutions can define common aims and cooperate in a genuine common policy. In some respects the addition of EU exclusive competence is analogous to the progressive extension of the CCP to cover more trade-related topics that were when negotiated as mixed competence agreements. But one important distinction is that in trade-related topics such as government procurement or trade in services, there were no well-developed external policies of the member states. In the case of investment, particularly with regard to investment protection, there are such well-established external policies of the member states. In addition to the question of the content of EU investment policy there is therefore an issue of the time scale and method of managing the transition from member state investment policies to a common EU investment policy.

Evolution not revolution: FDI regulation in the European Union

Prior to the entry into force of the Treaty of Lisbon on 1 December 2009 there was EU competence for some aspects of cross border investment. Since at least the mid-1980s the EC/EU has negotiated on market access for trade in services, in which establishment or investment in the service sector was a central feature. The EC/EU also negotiated on trade related investment measures (TRIMs) during the Uruguay Round of the GATT that led to the introduction of discipline on a number of performance requirements. EU competence for services investment was also codified in the Treaty of Nice.

For some time the EU and member states have also shared competence for the regulation of capital flows under the chapter on the free movement of capital, now Articles 62 to 66 TFEU. This affects many aspects of investment including in particular the transfer of funds and the repatriation of earnings and therefore touches on both FDI flows as well as portfolio investment. The Treaty provisions generally prohibit restrictions on capital flows both within the EU AND between the EU and third countries. But there are provisions enabling a 'step back' from liberalisation or restrictions on capital flows if, for instance, macroeconomic stability is at risk or on the security grounds. The EU's competences in this field are mostly internal. These internal competences provide the EU with implicit external competences enabling for instance the conclusion of international agreements in this field. However, the scope of these implicit external competences is too limited for the development and implementation of a proper European investment policy and the conclusion of bilateral investment treaties (BITs) (Herrmann 2010; Eilmansberger 2009). Until the entry into force of the Treaty of Lisbon the Member States therefore remained generally competent to conclude BITs and to regulate investment protection and post-establishment treatment. The EU was generally competent with regard to market access of investment (Ceyssens 2005), but the EU was not able to develop a comprehensive approach to international investment (Herrmann, 2010).

This fragmented approach to investment policy can be seen as sub-optimal for a number of reasons. First, as noted above, over the past 30 years the conviction has grown that FDI is intimately linked to trade in goods and services. FDI is today considered as a complement to traditional forms of trade (e.g. through building commercial presence in order to supply post-purchase services) and as a substitute (e.g. through building production sites in third countries instead of exporting). Consequently, support for a more active role for the EU in investment has grown among stakeholders.

Second, the lack of a common position on investment has arguably undermined the EU's ability to articulate and pursue international negotiations on investment, whether in the OECD, WTO or in bilateral and regional trade agreements (Bungenberg 2010). Thus even though the EU accounts for more FDI (inward and outward) than any other trading entity, other countries have led in shaping investment regimes. For example, led by the US, the NAFTA states started concluding ambitious, comprehensive investment agreements with third countries in the 1990s. The emulation of such comprehensive agreements by other countries such as Singapore and Chile in comprehensive trade and investment agreements has led to the creation of what might be seen as *de facto* global standards for investment agreements. The EU's difficulties to negotiate matching agreements also translates into a relative loss of competitiveness for European investors and the European economy in the world (Commission 2006).

Fourth, the latest enlargement rounds of the EU have created the problem of intra-EU BITs, because most acceding countries concluded BITs with existing member states. These intra-EU BITs pose manifold legal questions. See section 11. They provide the possibility of 'treaty/forum shopping' for investors in that arbitral tribunals interpret provisions in the BITs that are also covered by EU law establishing the Single Market. It is unclear whether an EU investment policy would overcome these problems. For example, EU law does not offer investors access to arbitration in the case of disputes only recourse to EU law via the member state legal systems. Intra-EU BITs have therefore drawn attention to the problematic interaction between Member State investment policies and the Single Market regime (Eilmansberger 2009).

Finally, Member State investment policies and BITs have created inequality among European investors (Commission 2010). Whereas some member states (such as Germany, Britain, France, The Netherlands and Italy) have been very active in negotiating BITs with a wide range of countries, others have remained inactive. Obviously, this favours the investors and the economies of active member states, with those investors in non-active member states losing in competitiveness. European and foreign investors try to at least partially offset this inequality by creating special purpose investment vehicles in member states that provide a particularly conducive legal environment for their investment thanks in part to the existence of BIT. The uneven distribution of BITs among EU member states could therefore distort investment flows within the Single Market.

These manifestations of fragmented investment policy within the EU explain why cross border investment has been on the agenda of almost all intergovernmental conferences IGCs on treaty reform for the last 20 years. However, this was without success before the Convention on the future of Europe in 2002/2003, which finally introduced changes in this field. The treaty draft elaborated by the Convention provided for an extension of the CCP to cover FDI although several Member States (France, Germany, Ireland, Spain and the United Kingdom) had opposed such a reform. It was reported that the intergovernmental conferences following the Convention adopted the extended CCP provisions as part of a final package concluding the negotiations on the Treaty. The constitutional treaty never entered into force, but the modified chapter on the CCP was integrated into the Lisbon Treaty.

Exclusive competence for FDI: but what is included in 'FDI'?

Articles 206 and 207 TFEU bring 'foreign direct investment' under exclusive EU competence as part of the CCP. The Treaty of Lisbon, however, does not define FDI leaving open the actual scope of the new EU competence. The entry into force of the Lisbon Treaty has therefore triggered a legal and political debate on the definition and interpretation of the term FDI.

There is no consensus on an exact definition of FDI within the EU or at the international level. Broadly defined, FDI is capital flowing from an investor based in one country to an enterprise based in another country. Furthermore, there is general agreement on the two core characteristics of FDI. First, FDI manifests a long-lasting interest of an investor in the enterprise abroad. Second, FDI provides the investor with a certain degree of managerial control. The figure of 10% of the affiliated company's shares is often used as a measure of control (Herrmann, 2010), although there is no one metric that can be used. FDI is however defined in opposition to the term portfolio investment, which describes short-term investments with a narrow focus on the rate of return, no managerial control and a partly speculative character (Wolf 2008).

The existing member state BITs normally do not define the term FDI nor make a distinction between it and portfolio investment, but enumerate in more concrete terms the financial and legal titles and transactions, which are considered as cross-border investment under the respective agreement. The EU, however, has generally distinguished between FDI and portfolio investment in its publications, such as in its position papers regarding negotiations on investment in the Doha Round of the WTO (Herrmann 2010) and indeed in the Commission's Communication (European Commission, 2010). The ECJ has also specified its understanding of the term FDI in recent years[1] according to which FDI should be considered as a long-lasting investment, representing at least 10% of the affiliated company's equity capital / shares and providing the investor with 'managerial control'[2] over the affiliated company's operations. If an investor holds less than 10% of shares of an affiliated company, it can still qualify as FDI provided the investor has 'managerial control' over the affiliated company. As comprehensive investment agreements and standard BITs normally not only cover FDI, but also portfolio investment,

[1] Notably, ECJ judgement C-446/04 has elaborated the court's understanding of the term FDI. In judgement C-446/04 the court argues that directive 88/361/EEC on the free movement of capital on the Single Market should be invoked for the interpretation of the term. Directive 88/361/EEC defines the term *direct investment* as any investment by a legal person or individual establishing an enterprise or extending its capital and thereby building a durable, direct and managerial relation between investor and the enterprise. Consequently, *foreign direct investment* should establish such a relation between one actor being located within the EU and the other being located in a third country. Furthermore, the argumentation of the ECJ clarifies that the percentage of ordinary shares or equity capital provided/held by an investor is an indicator for the qualification of an investment as either FDI or portfolio investment. Several ECJ judgements as well as secondary EU law provide different possible threshold percentages for distinguishing between FDI and portfolio investment (Johannsen 2009).

[2] The EU working group on the Doha Round investment negotiations published a position paper, which helps to substantiate the vague term 'managerial control'. According to this paper a capital placement qualifies as FDI, if the investor is represented on the board of directors, sends managerial staff and participates in the decision-making of the affiliated company (see Krenzler, Pitschas 2005).

payments and legal titles (e.g. intellectual property rights), the ECJ's definition sets limits on the new EU competence (Herrmann 2010. The ECJ's definition largely corresponds to those developed by the IMF and the OECD. These consider FDI to be a long-term placement of capital, representing at least 10% of ordinary shares, equity capital or 10% of votes in the firm's decision-making (Johannsen 2009). But the ECJ's definition of FDI remains imprecise for several reasons. First, it does not specify what 'long term' means. Second, the ECJ has argued in its judgement C-446/04 that the calculation of the percentage of ordinary shares or equity capital held by an investor should be based on national law of the host country. Hence, a theoretically identical capital placement might be considered as portfolio investment in one state and as FDI in another.

This lack of a clear definition of FDI has significant consequences for its regulation. Art. 63 – 66 TFEU on free movement of capital provide for exclusive competence and OLP for 'measures on the movement of capital to or from third countries involving *direct investment',* although there are exceptions granting member state competence on such issues as prudential supervision and tax, which imply portfolio investment comes under the shared competence of the EU and Member States.

Given the emergence of global value chains and production, it is not surprising that it is difficult to make a clear distinction between FDI and portfolio investment. Any attempt at a rigid legal definition is likely to be difficult to apply to real world investment practices. There are therefore advantages in not trying to come up with a precise definition. An imprecise and evolving definition of FDI in the EU would allow for a continuous adaptation of the term and thus of the CCP to changing economic realities and the content of international negotiations. This might be positive for the EU – notably for the Commission – as it increases its potential room for manoeuvre in policy-making. Theoretically, it might also be of benefit for investors, who can challenge existing definitions in order to improve and adapt the regulatory context for their investments.

On the other hand, an imprecise and evolving definition of FDI creates legal uncertainty and economic risks for investors. The EU investment policy is likely to distinguish between FDI and portfolio investment. Whereas FDI is exclusive EU competence under the CCP administered by the DG Trade, portfolio investment is a field of shared competence and administered by DG Internal Market and Services (Tietje 2010). The diverging governance structures might therefore result in different market access, post-establishment and protection standards and procedures for FDI and portfolio investment. As the boundaries between both types of investment are fluid, this situation might increase the complexity and uncertainty for investors regarding the proper rules and procedures concerning their investment.

2 WHAT ARE THE BENEFITS OF EXCLUSIVE EU COMPETENCE FOR FDI?

Exclusive competence should result in the EU becoming a more important actor,

The extension of EU exclusive competence to FDI should give the EU a greater capability to shape international investment policy thanks to an ability to conclude comprehensive and up-to-date investment agreements with partner countries (Bungenberg 2010). Since the 1990s the NAFTA countries have shaped international investment rulemaking by concluding comprehensive investment agreements covering investment liberalisation (market access and pre-establishment treatment of investors) and post-establishment treatment (i.e. investment protection). Before the Lisbon Treaty neither the EU nor the Member States were competent to individually conclude comparable agreements and were unable or unwilling to coordinate their efforts and conclude 'mixed agreements' of an equivalent standard. This resulted in a loss of EU influence and - in so far as investment agreements ease market access and promote competitiveness – a loss of competitiveness for European investors vis-à-vis some of their main competitors on third markets. EU exclusive competence remains too narrow for the EU to conclude comprehensive investment agreements, but subject to any transitional arrangements (see part II) the member states are not allowed to conclude any more agreements (Herrmann 2010). Greater EU competence therefore makes coordination of efforts to conclude 'mixed agreements' a necessity. Mixed but comprehensive agreements on investment will enhance the EU's external representation by increasing the EU's bargaining power in international investment relations with third countries. The new competence should facilitate the EU speaking with one voice in investment as it does in trade. As the EU and its Member States are by far the world's most important destination and exporters of FDI, the EU as a single actor negotiating on the basis of a common policy plateform on investment should increases the EU's influence.

.. enable better access for EU investors in third markets.

The enhanced bargaining power of a single EU policy on trade and investment should enable the EU to gain better access to key third country markets while protecting EU investors, thus enhancing Europe's international competitiveness. Furthermore the EU and its member states should gain influence in a key area of globalisation. Some observers even speculate that a common policy might revive chances of the EU succeeding in its aim of negotiating a multilateral framework for investment in the WTO.

… promote European values,

The Treaty on the European Union (TEU) and the Treaty on the Functioning of the European Union (TFEU) enumerate a number of objectives for the EU's external actions including the CCP. Arts 206 and 207 TFEU call on the EU to contribute to a harmonious development and liberalisation of world trade, Arts 205 TFEU states that the CCP should be guided by the general principles of the EU's external action, including the promotion of democracy, the rule of law, further the respect of human rights and contribute to sustainable economic, social and environmental development of developing countries (etc.) (Vedder 2010; Bungenberg 2010).[3] While some stake holders will welcome the possibility of

[3] Elaborated in title V, chapter I, TEU. Already before the Lisbon Treaty most of these objectives applied to the international actions of the European Community, EU and CCP due to manifold international agreements. The Lisbon Treaty now codifies these obligations/objectives in the EU's primary law. This reinforces their political importance, but does not considerably change the legal context and purpose of the CCP.

promoting such broader European values, European investors and many member state governments fear a politicisation of investment protection, promotion and liberalisation. Their concern is that EU investment agreements with such political clauses will reduce the level of protection for EU investments abroad. Investors are in particular concerned that the inclusion of social or environmental clauses will be invoked by host states or arbitral bodies to justify indirect expropriation by host countries thereby weakening investor protection or increasing uncertainty for investors. European firms and investors therefore argue that they are likely to carry the costs of such a 'humanitarian' investment policy. Until now the Commission has not elaborated how it is planning to balance the economic and these broader political objectives of the CCP with regard to investment (Tietje 2010).

.. establish unified standards and procedures,

Member state policies and BITs have established diverse standards, rules and procedures in the field of investment protection and post-establishment treatment. The new EU competence over FDI regulation should facilitate a harmonisation of these standards and procedures. This would lower the costs for European and foreign investors and free resources for value-adding operations. However, the Commission does not intend to develop a model investment agreement, but proposes to adapt investment provisions to the negotiation context and partner country. Without some degree of uniformity in a standard platform for investment the benefits from unified EU standards will not be achieved.

…and re-establish equality among European investors;

Some member states have concluded many more BITs than others and the standards of investment protection in the member state BITs vary (Commission 2010). Thus, European investors do not enjoy the same level of protection and support. An EU investment policy leading to the conclusion of EU investment agreements should re-establish equality among European investors in the long run. As a shorter term means of establishing equality among European investors in third markets the Commission has proposed including an MFN clause in existing member state BITs that would extend the protection to all EU investors. Third countries are unlikely to accept such a clause as it would extend the protection under one member state BIT to the whole EU, whereas investors from the third country would only benefit from protection in the individual member state.[4] Furthermore, it is unclear how such a renegotiation of BITs between member states and third countries should proceed given that the EU is now exclusively competent for FDI (Tietje 2010).

.. but there remains uncertainty about the transition to a more unified EU policy;

An evolutionary process inevitably requires transitional measures and currently, EU and foreign investors are waiting for a clarification from the EU on regarding the current validity and future of existing member state BITs. On 7 July 2010, the Commission published a proposed Regulation setting out transition rules on existing BITs in order to end this phase of uncertainty (COM(2010)344), see part II which addresses the question of whether the proposed approach reduces uncertainty. European investors are also wondering about the investment protection and promotion standards of future EU investment agreements. In particular investors in member states with numerous BITs, like Germany, France, Great Britain, the Netherlands and Belgium, fear that new EU investment agreements may fail to deliver a comparable level of protection. Commission documents COM(2010)343 and COM(2010)344 have tried to reduce this uncertainty among European investors by presenting the general plans of the Commission for this field. But not surprisingly the most essential questions regarding pre- and post-

[4] All member state BITs include a provision that prevents third countries benefiting from such an MFN and gaining rights throughout the entire EU thanks to a BIT with one member state.

establishment treatment, arbitration procedures and compensation rules remain the subject of debate (Tietje 2010).

…..about inflexibility or delay with a common EU policy,

European investors also fear that the EU will be less responsive to their demands regarding new BITs than member state governments or that negotiations at the EU level will take much longer. National business and industry confederations are therefore seeking authority for member states to continue to conclude new BITs, if there is a strong national, but no Europe-wide interest in a BIT (CBI 2003). The Commission in its Communication has provided for such authorisation. See part II again on this issue. But there is also concern that EU negotiations may also be held up by resistance or opposition from member state governments. As future EU BITs or comprehensive trade and investment agreements are likely to be 'mixed agreements' requiring national ratification and unanimous support in the Council of Ministers (Herrmann 2010b), there will be ample opportunities for one or more member states to hold up or block EU level agreements. This concern has also been addressed in the Commission's proposed Regulation on transitional measures. [5]

.. and the risk of politicisation of investment policy.

Despite some heated political debate on international or multilateral agreements on investment, bilateral investment agreements have remained largely a 'technical issue' dealt with by government officials and investment lawyers. The debate on what should constitute an EU investment policy is seen by some EU investors and governments as risking a politicisation of investment protection for the sake of general humanitarian, socio-economic or environmental foreign policy considerations. The judgement that must be made here is whether and if so how much the inclusion of the broader objectives will reduce the economic benefits of any agreement. Another issue is whether inclusion of such broad objectives in BITs is the best means of promoting sustainable development, and if included should there be a general reference to sustainable development in the preamble of any EU agreement or in a substantive article? Finally, there is a question as to the effectiveness of provisions on labour and environmental standards that have been included in some investment agreements such as those concluded by the USA and Canada? These issues are covered in sections 8 and 9 of part I.

Some, national business and industry associations have also come out against inclusion of investment protection in free trade agreements (FTA) on the grounds that FTAs are the product of bargaining and inclusion of investment protection within such agreements risks compromising investor protection in the interests of, for example, improved market access. (BDI 2010). Integrating investment protection into FTAs could thus politicise negotiations and agreement provisions on investment protection.

Separating investment protection from broad issues of investment liberalisation or market access in general would however, reduce any enhanced leverage the EU will gain from an ability to negotiate comprehensive trade and investment agreements.

Conclusions on the scope of EU competence.

The impact of the Treaty of Lisbon on cross-border investment regulation and the external economic regime of the EU seem likely to remain uncertain in at least the short term. Questions remain regarding

[5] Art 9 of the regulation on transitional arrangements would give the Commission power to block any bilateral BIT negotiation by a member state if this would 'undermine the objectives of negotiations underway or imminent between the Union and (a) third country'. More controvertially, Art 6 of the proposed regulation would also give the Commission power to withdraw authorization of a member state BIT if it feels a member state is blocking EU negotiations.

the scope of the new EU competence, the future of existing member state BITs and the nature of future EU investment policy. The theoretical advantages and disadvantages of an exclusive EU competence over FDI regulations will only materialise over the coming years and after legal and political debates between the Member States, the European institutions and stakeholders.

3 DOES FDI ENHANCE EU COMPETITIVENESS?

.. the economic arguments all point to both inward and outward FDI enhancing competitiveness;

There is consensus that the competitiveness and productivity[6] of firms and thus of national economies are related to FDI. Inward and outward FDI have manifold direct and indirect effects on firms, economic growth and development as well as potential political and social consequences for host and home economies.

Today, most economists and governments consider *inward FDI* as beneficial for host economies. Inward FDI creates employment within the international firms that establish in the host country as well as firms supplying goods and services to these operations. Inward investment also promotes the transfer of innovative technology and managerial skills to the host economy as well as migration of highly skilled staff. It also fosters competition within the host economy thereby promoting innovation, enhancing the business climate reducing consumer prices and increasing welfare. Finally, it further integrates the host country into the world economy. (Hjälmroth, Westerberg 2009).

Economic analysis of outward FDI furthermore indicate that a firms' productivity and competitiveness gains attained by outward FDI vary across time, economic sector and country (Sunesen et al. 2010). In other words not all firms gain in equal measure. Nevertheless, one can identify three general causal channels between outward FDI, competitiveness and productivity gains for firms:

- setting up or buying an affiliated company in a third market can help the parent company to exploit economies of scale (efficiency-seeking FDI), to unlock new and bigger markets (market-seeking FDI) and to get closer to customers and their needs thereby potentially increasing sales (strategic FDI). These three aspects of outward FDI enhance firms' overall competitiveness and productivity (Dunning 1993).
- parent companies can source input factors (natural resources, labour, expertise, technology) through affiliated companies in third countries (resource-seeking FDI) thus lower costs through input factor prices and thereby increasing the parent company's competitiveness on home and international markets (Dunning 1993).
- significant FDI activity by national firms can function as an economic incubator for the national economy in that such firms often set new standards in productivity thereby forcing the rest of the economy to innovate in order to compete. This in turn leads to a fall of consumer prices and finally a spillover of technical and managerial skills from successful MNCs to other firms and sectors. In the long run, FDI activity thereby contributes to the economic development of firms and economies (Fu 2008; Hjälmroth, Westerberg 2009).

[6] Productivity signifies the efficient use of input factors for the production of goods or provision of services. The less input factors are needed for the production of a specific good or service (output), the more productive a firm is. Productivity and competitiveness are closely related.

…improved market access in markets with growth potential helps EU firms to remain competitive in global markets;

As discussed above the conclusion of more comprehensive EU investment agreements should improve market access conditions for European firms and investors on third markets (Herrmann 2010). Many emerging markets maintain market access restrictions for inward FDI for instance by protecting state monopolies (OECD 2006). The new EU competence could help to provide European MNCs and investors with new investment opportunities in such key markets of the world economy and therefore support European firms and investors in fully exploiting the advantages of globalisation. Stronger EU agreements will in particular help to nullify the competitive advantages that Northern American and Japanese MNCs/investors have on certain third markets vis-à-vis European firms/investors. (Commission 2006).

…an enhanced aggregate level of protection for EU investors could contribute to competitiveness;

The best available standards of protection will facilitate EU firms to engage fully in the international division of labour and thus enhance competitiveness (see discussion of these below). Firms throughout the EU will benefit from at least the level of the most protected firms under member state BITs. The increased aggregate protection level should lower investment risks and hence costs for business ventures abroad. Lower costs should then free additional resources for value-adding business operations and increase productivity.

…cost reductions thanks to standardised rules;

A more coherent set of common rules should lower the administrative costs of investing in target markets for European firms thus releasing resources for further value-adding business operations. At present some firms in member states without BITs establish a presence in member states that have such BITs in order to benefit from investment protection. Common rules would remove the need for such activity and thus save costs. The scope for such savings will depend on how standardised EU investment agreements are. Given the diversity of potential negotiating partners for the EU (from Canada and Singapore to China and LDCs) investment provisions appear likely to vary from partner to partner. Diversity between EU agreements will therefore mean fewer gains from reduced transaction costs.

.. enhanced attractiveness of the European Union for foreign investors;

EU investment agreements should also increase the competitiveness of the EU as host economy for inward FDI. Until now, investors from third countries have had to base their investment activities in the EU on a specific BIT and member state. EU investment agreements should make the Single Market as a whole more accessible and attractive for foreign investors. As explained-above inward FDI can promote the competitiveness in a number of ways. Common standards for inward FDI would also help limit distortions to competition within the EU market resulting from competition between member states to attract investment.

.. but with sector and national variations;

Economic research indicates that the impact of FDI on the productivity and competitiveness of international firms and investors can vary across economic sectors and countries. Firm-level studies suggest that the manufacturing firms may stand to benefit quicker from foreign affiliates (by serving foreign markets or sourcing intermediate inputs) than service firms with affiliates. First, manufacturing firms may draw from market-seeking foreign affiliates more enduring productivity gains than service sector firms. Service sector firms must wait about three years before their affiliates contribute to their productivity and competitiveness (Hijzen et al. 2009). Second, manufacturing firms sourcing input material from affiliated companies abroad should see a higher – although in absolute terms small – increases in their productivity, than service sector firms sourcing intermediate services from affiliated companies abroad. This is probably linked to the impossibility of storing services and the thereby resulting high coordination costs for sourcing intermediate services (Anderson et al. 2008).

On the other hand, establishment (the ability to invest in target market) is often essential for service sector access to export markets. Although market access for services is already EU competence and forms part of market access negotiations in the GATS and in bilateral trade agreements, the extension of EU competence should increase the EU's negotiating leverage and thus improve access to some key services markets.

The impact of FDI on the productivity of European extractive industries has not been object to empirical studies. Extractive industries often encounter market access, post-establishment and also protection problems (e.g. European oil and gas companies in Russia). The considerably increased bargaining power of the EU in the field of investment could thus facilitate improved access and possibly more effective enforcement of EU firm's investment protection in raw materials and energy thereby contributing to Europe's resource and energy security.

Finally, Bitzer and Görg (2009) find variations in the impact of FDI on the productivity and competitiveness of entire countries. With regard to OECD countries they find that inward FDI in general leads to an increase of productivity and competitiveness of the host economy. Outward FDI effects, however, are found to vary with France, Poland, Sweden, the United Kingdom and the USA gaining in productivity from outward FDI, whereas Germany, Spain, Italy and Norway on average seem to lose productivity due to increasing outward FDI stocks.

.. probably neutral in terms of net employment but exacerbates adjustment costs for low skilled workers.

While outward FDI is often considered to promote competitiveness and productivity there is also a belief that it destroys domestic jobs and reduces domestic investment activity. Empirical studies of the employment effects of outward FDI suggest that it does not have much of a net effect, but probably promotes a shift from low skilled to higher skilled employment. While this should be seen as a positive factor for the EU's position in global competition, it would clearly mean that the adjustment costs will tend to be carried by the lower skilled. (Sunesen et al 2010)

There is evidence that firms engaging in outward investment also invest at home. FDI and domestic direct investment are thus complementary rather than substitutes (Desai, Foley, Hines 2005). Other studies have demonstrated that investing at home or abroad are generally not mutually exclusive. Firms that refrain from investing abroad do not necessarily invest at home. In some cases, investing abroad may be necessary to remain competitive and thus maintain some operations at home (e.g. textile industry relocating some production abroad in order to survive). There is some empirical work suggesting firms with investment in third countries (i.e. outside the EU) grow faster (some 5% more) than their 'purely domestic' counterparts and are thus likelier to re-invest at home (Navaretti, Castellani 2004). Most empirical studies of the employment effects of outward investment conclude that outward FDI is not a substitute for, but complementary to domestic investment. Companies relocating production abroad lay off workers, but create directly or indirectly nearly as many new jobs at home.

4 IS THE EU'S APPROACH TO INVESTMENT POLICY COMPATIBLE WITH THE GLOBAL EUROPE STRATEGY AND THE EUROPE 2020 VISION?

The Global Europe strategy of 2006 had the central aims of promoting EU international competitiveness in the global economy, and enhancing market access for EU firms in countries and regions with growth potential (.e.g. India, ASEAN, China and The Republic of Korea, Canada etc.) in order to maintain or strengthen the EU's relative position in the global economy despite the structural changes in demand in recent years. To this end it was envisaged that preferential trade agreements would be negotiated with a number of targeted countries, but not China. The return to an active EU policy on free trade/preferential trade agreements was to be conducted in parallel with multilateral efforts to bring about the progressive removal of barriers to trade. Preferential agreements were therefore to be compatible with the longer term aim of continuing to promote multilateralism. Since the mid to late 1990s it could be argued that the EU has been the major driver behind efforts to negotiate multilateral trade agreements, including those with investment. There were also a number of other objectives of the Global Europe strategy, such as the more effective enforcement of existing trade agreements including in particular intellectual property right provisions.

… increased inward and outward investment promotes EU competitiveness

An EU approach to investment policy that strengthens the EU competitive position in international competition would therefore be in line with the Global Europe aims. As discussed above increasing both inward and outward investment should promote EU competitiveness. Given the EU's factor endowments compared to the large emerging markets this is the best strategy to retain EU competitiveness and wealth creation. Adjustment assistance should be considered for those sections of the labour force that have to carry a disproportionate share of adjustment costs.

… a comprehensive trade and investment policy enhances EU negotiating leverage;

Arguably one of the reasons the EU and other developed economies have resorted to preferential trade negotiations is because of a relative decline in their negotiating leverage. In reciprocity based international negotiations such as those that still determine international trade and investment, economic power is measured by how much parties can 'give' in terms of concessions. Through successive rounds of tariff negotiations and internal policies that have led to a liberalization of the European Single Market, also with regard to third countries, the EU has seen this negotiating coinage steadily eroded. In comparison the major emerging markets have both relatively higher growth and thus relatively greater market potential than many OECD economies as well as higher levels of protection in terms of tariffs, regulatory barriers to trade and controls on inward investment. The addition of exclusive competence for FDI should facilitate comprehensive trade and investment negotiations between the EU and the major emerging markets. Such a comprehensive approach will go some way to compensating for the relative decline in the EU's negotiating leverage.

… this will enable the EU to negotiate more effectively with the target markets identified in Global Europe..

Access to markets, including in particular those such as China, Brazil and India will in future be more concerned with investment than trade issues. Trade and investment have for many decades been complementary. So if the EU wishes to ensure effective market access to the major areas of economic growth, a central aim of the Global Europe Strategy, it will need to include investment in its bilateral relations with these markets.

…. extending investment protection measures for EU investors can improve enforcement of intellectual property rights..

Another aim of the Global Europe Strategy was to promote more effective enforcement of intellectual property rights. Through multilateral as well as bilateral means the EU has been pursuing this aim. By negotiating investment agreements with third countries that include investment protection the EU can also enhance the enforcement of property rights. This will depend on the definition of investment included in any agreements, but a broad definition of investment could cover all assets including intellectual property.

… bilateral agreement on investment will undermine the pursuit of multilateral agreement..

Global Europe stressed that preferential agreements are/should be compatible with multilateralism. In the past the EU has favoured multilateral approaches to investment rather than the plurilateral and bilateral route favoured by the United States. In the mid-1990s it was the EU that pushed for the inclusion of investment in WTO negotiations and it was the EU that was one of the few promoters of investment as one of the Singapore issues in the Doha Development Round. Before the OECD negotiation on a plurilateral 'Multilateral' Agreement on Investment (MAI) the EU favoured the WTO over the OECD as a more inclusive forum for negotiation because future investment issues were clearly going to concern the developing countries more than the OECD countries. There was always a tension in the Global Europe strategy between the pursuit of preferential trade agreements and this commitment to multilateralism. When the EU negotiates preferential, comprehensive trade and investment agreements this could undermine the prospects of reaching agreement at a multilateral level on investment.

…but then the prospects of a meaningful multilateral agreement on investment are remote.

5 DOES THE EU'S STRATEGY HAVE THE RIGHT FOCUS?

In its Communication on the future of EU international investment policy the Commission has identified a number of priority partners, i.e. Canada China, India, Mercosur, Russian Federation and Singapore. The Commission identifies several 'determinants' according to which the focus of the strategy was defined: the 'magnitude of investment flows', 'market potential for future investments', and 'stability and predictability of investment climate.' The Commission has also expressed its willingness to engage in investment protection negotiations with its trading partners if they wish to do so. In this context, this study does not attempt to judge whether the selection criteria is 'right' or 'wrong'. Rather, it investigates whether and to what extent the selection criteria have been applied in an objective basis across potential partner countries. By using various analytical indicators and indices, it evaluates the extent to which the priority countries fulfill the objective criteria. It also probes if there are other countries that could be identified as potential partners for investment protection negotiations.

Criterion 1: Magnitude of investment flows

The EU has a diverse set of investment partners in relation to both its outward investment flows/stocks and its inward flows/stocks by country of destination and origin. This section examines the recent trends in EU27 investment stocks - which show the accumulated value of all investments for a reference period - and investment flows in order to determine the EU's major partners in this field.

Looking at the data on investment flows accumulated between 2004 (the earliest data available for the EU-27) and 2008, the EU's top three partners in both outward and inward stocks are the United States (US), Offshore Financial Centres and Switzerland, respectively. See tables 1 and 2.

In outward stocks, Canada, ACP countries (as a group), China (including Hong Kong), the Russian Federation, Turkey, Singapore and Brazil are among the EU's top 10 investment destinations. As for the EU priority countries as identified by the Commission, the majority are important partners accumulating substantial stocks of investment coming from the EU. Canada holds a share of 5 per cent of all extra-EU27 outward stocks. The share of China (including Hong Kong) is slightly more than 4 percent, while the shares of Russian Federation and Singapore are 4 per cent and 2 percent respectively. As part of Mercosur, the share of Brazil is 2 per cent, while other members of Mercosur do not have stocks of significant magnitude invested by EU27.

For inward investment stocks, on the other hand, Gulf states (group of eight countries), Japan, Brazil, Canada, ACP countries, Australia and Singapore are among the top 10 extra-EU27 countries (and country groups) investing in the EU. Among the EU priority countries, Brazil and Canada have the highest share of investment stocks in the EU, both holding 4 per cent of all investment by extra-EU27 countries. The share of Russian Federation is 2 per cent, followed by China (including Hong Kong) holding approximately 2 per cent and India holding 1 per cent of all investment stocks by extra-EU27 investing countries.

Table. 1 EU-27 outward and inward investment stocks (2004-2008) by extra-EU 27 country of origin and destination

	Outward stocks		Inward stocks	
Rank	**Country of destination**	**Share in total extra-EU27**	**Country of origin**	**Share in total extra-EU27**
1	United States	28%	United States	38%
2	Offshore financial centers	21%	Offshore financial centers	23%
3	Switzerland	10%	Switzerland	10%
4	Canada	5%	Gulf states*	7%
5	African, Caribbean and Pacific countries	5%	Japan	4%
6	Russian Federation	4%	Brazil	4%
7	Turkey	3%	Canada	4%
8	Singapore	2%	African, Caribbean and Pacific countries	3%
9	Brazil	2%	Australia	2%
10	Japan	2%	Singapore	2%
11	Hong Kong	2%	Russian Federation	2%
12	Gulf Arabian Countries*	2%	Norway	2%
13	China (excl. Hong Kong)	2%	Hong Kong	1%
14	Australia	2%	Iceland	1%
15	Mexico	2%	India	1%
16	Norway	2%	Mexico	<1%
17	South Africa	2%	Uruguay	<1%
18	Egypt	1%	South Africa	<1%
19	Ukraine	1%	Egypt	<1%
20	India	1%	China (excl. Hong Kong)	<1%

Source. Eurostat

*Gulf states: (AE, BH, IQ, KW, OM, QA, SA, YE)

Table. 2 EU-27 outward and inward investment flows by extra-EU 27 country of origin and destination, 2008

	Outward flows		Inward flows	
Rank	**Country of Destination**	**Share in total extra EU27**	**Country of origin**	**Share in total extra EU27**
1	United States	35%	Gulf states*	32%
2	Offshore financial centers	11%	United States	25%
3	Switzerland	10%	Offshore financial centers	10%
4	Russian Federation	7%	Canada	8%
5	Gulf states*	5%	Brazil	5%
6	Singapore	4%	Switzerland	5%
7	Australia	4%	Japan	4%
8	Egypt	3%	India	2%
9	Canada	2%	Norway	2%
10	African, Caribbean and Pacific countries	2%	Egypt	2%
11	Turkey	2%	African, Caribbean and Pacific countries	2%
12	Hong Kong	2%	Singapore	1%
13	Japan	2%	Russian Federation	1%
14	Mexico	2%	Hong Kong	1%
15	Ukraine	1%	Uruguay	1%
16	China (excl. Hong Kong)	1%	Mexico	<1%
17	Norway	1%	Venezuela	<1%
18	Argentina	1%	Israel	<1%
19	India	1%	Ukraine	<1%
20	South Africa	1%	South Africa	<1%

Source. Eurostat

*Gulf Arabian Countries: (AE, BH, IQ, KW, OM, QA, SA, YE)

If one examines the most recent data on investment flows (2008), which had been affected by the financial crisis, the picture is slightly different. In particular, Gulf Arabian Countries (group of eight countries) have become the top investor in EU in 2008, overtaking both the US and Offshore Financial Centres. This group has also become the fifth largest destination of EU27 outward investment flows. There have been significant changes in the investment flows of the priority countries too. For example, EU27 investment flows to Russian Federation have increased significantly, making it the fourth largest investment destination of EU outward flows in 2008 (after US, Offshore Financial Centres and Switzerland). In the same year, the share of India in EU inward investment has increased too, placing it among the EU27's top 10 investing countries. On the other hand, the share of ACP countries has fallen in terms of both EU inward and outward investment flows. It must be born in mind that investment flows can fluctuate significantly due to short term economic factors. This is of course, particularly the case with the recent financial crisis.

Criterion 2: Market potential for future investments

Various indicators, such as growth rate, production and consumption capacity, can be used to assess market potential for investment. There are also composite indexes ranking countries based on their performance in various indicators. This section compares the market potential of EU investment partners by using such indices. For this purpose, we rely on the 'Market Potential Index for Emerging Markets' developed by the Michigan State University. This ranks countries according to eight dimensions – namely market size, market growth rate, market intensity, market consumption capacity, commercial infrastructure, economic freedom, market receptivity, and country risk. These dimensions represent the market potential of a country (over a scale of 1 to 100) and each of them is measured and weighted, which then determine the ranking of a country in the Overall Market Potential Index.

In 2009, Singapore ranked 1st in this list, indicating that it offers a substantial market potential for investment. See table 3. It was followed by China and Hong Kong ranking second and third respectively. South Korea, Israel, Russian Federation and Malaysia are also among the top 10 (non-EU) countries offering significant market potential. Among the priority countries identified by the Commission, India ranks 11th, Brazil (member of Mercosur) ranks 16th, and Argentina (member of Mercosur) ranks 18th. There are also non-priority countries, some of which the EU has trade agreements with, ranking high in the market potential index. Most notably, South Korea, Israel, Malaysia, Mexico and Saudi Arabia offer substantial market potential for future investments. Among those, however, currently only Saudi Arabia and Mexico have some significant investment flows with the EU27.

Table 3. Overall Market Potential Index (emerging economies), 2009

Countries	Market potential rank	Market potential rank (Excluding EU) Countries)
Singapore	1	1
China	2	2
Hong Kong	3	3
Korea, South	4	4
Czech Rep.	5	-
Israel	6	5
Poland	7	-
Hungary	8	-
Russia	9	6
Malaysia	10	7
India	11	8
Turkey	12	9
Chile	13	10
Mexico	14	11
Saudi Arabia	15	12
Brazil	16	13
Egypt	17	14
Argentina	18	15
Thailand	19	16
Pakistan	20	17
Peru	21	18
Indonesia	22	19
Philippines	23	20

Source.Michigan State University

Criteria 3. Stability and predictability of investment climate

Various indicators and indices could be used to evaluate the stability and predictability of investment and political environment in a given country. The World Bank's 'Ease of doing business index' is generally considered to be an advanced index that ranks countries according to how favourable the regulatory environment is for business activity. This multidimensional index also includes a specific 'investment protection' dimension, which is particularly relevant for assessing the stability of the investment climate in a given country. See table 4. A low ranking in such an ease of doing business index would justify inclusion in an EU list of priorities, especially if the host country concerned is a major destination for EU investors.

The ease of doing business index ranks countries according to 10 equally weighted dimensions – namely; starting a business, dealing with construction permits, employing workers, registering property, getting credit, protecting investors, paying taxes, trading across borders, enforcing contracts, closing a business. Country performances are measured based on a list of indicators developed for each dimension. According to the Doing Business 2010 Report, covering the period between June 2008 and May 2009, Singapore, New Zealand and Hong Kong rank as the top three countries respectively. The US ranks the 4th and Canada is the 5th both of which are major investment partners for the EU. Saudi Arabia, which is also an important investor in the EU, ranks the 9th. As for the priority countries, China (excluding Hong Kong) ranks the 89th, Russian Federation ranks the 120th, Argentina (as a member of

Mercosur) ranks the 118th, Brazil (as a member of Mercosur) ranks the 129th, and India ranks the 133rd among the 183 countries listed in the index. As such, apart from Singapore and Canada (and Hong Kong), none of the other priority countries offers a favourable regulatory environment for the operation of business.

Table 4. Ease of Doing Business Index

	Ease of Doing Business Rank	Ease of Doing Business Rank (excluding EU countries)
Singapore	1	1
New Zealand	2	2
Hong Kong SAR, China	3	3
United States	4	4
United Kingdom	5	-
Denmark	6	-
Ireland	7	-
Canada	8	5
Australia	9	9
Norway	10	6
Georgia	11	7
Thailand	12	8
Saudi Arabia	13	9
Iceland	14	10
Japan	15	11
Finland	16	-
Mauritius	17	12
Sweden	18	-
Korea, Rep.	19	13
Bahrain	20	14
Switzerland	21	15
Belgium	22	-
Malaysia	23	16
Estonia	24	-
Germany	25	-
Lithuania	26	-
Latvia	27	-
Austria	28	-
Israel	29	17
Netherlands	30	-
France	31	-
Macedonia, FYR	32	18
United Arab Emirates	33	19
South Africa	34	20

Source. World Bank

Based on the 'protecting investors methodology',[7] the indicator, called 'protecting investors', ranks countries based on three areas of investment protection: 'transparency of transactions', 'liability for self-dealing and shareholders' ability to sue officers and directors for misconduct'. Each of these areas gets a score based on a survey of 'corporate lawyers, the country's securities regulations, company laws and court rules of evidence' (World Bank, 2010).[8] Countries are than ranked according to the average of their scores in these three areas of investment protection. Although investment protection is part of the 'Ease of doing business index' it is useful to cover it separately given its relevance for this study.

Similar to the 'ease of doing business index', among the priority countries only Singapore, Hong Kong and Canada score high on investment protection. However, the scores for India, Brazil, Russian Federation and China are quite low, ranging from the 41st (India) to the 93rd (Russian Federation and China), which indicates that these countries do not offer high degree of investment protection. Among non-priority countries, on the other hand, Malaysia, Israel and South Africa, and Saudi Arabia score relatively high on the ranking.

[7] The methodology was developed by Djankov, La Porta, Lopez-de-Silanes, and Schleifer (2008). Available at: <http://www.doingbusiness.org/documents/Protecting-Investors-Self-Dealing.pdf>

[8]Available at: <http://www.doingbusiness.org/MethodologySurveys/ProtectingInvestors.aspx>

Table 5. Protecting investors ranking

	Protecting investors ranking	Protecting investors ranking (excluding EU countries)
New Zealand	1	1
Singapore	2	2
Hong Kong, China	3	3
Malaysia	4	4
United States	5	5
Ireland	5	-
Canada	5	5
Israel	5	5
Colombia	5	5
United Kingdom	10	-
South Africa	10	10
Thailand	12	11
Mauritius	12	11
Kyrgyz Republic	12	11
Albania	15	14
Saudi Arabia	16	15
Japan	16	15
Belgium	16	-
Puerto Rico	16	16
Norway	20	17
Macedonia, FYR	20	17
Azerbaijan	20	17
Slovenia	20	-
Peru	20	17
Trinidad and Tobago	20	17
Bangladesh	20	17

Source. World Bank

In summary, it is clear that the Commission's strategy to choose priority partners, i.e. Canada China, India, Mercosur, Russian Federation and Singapore, appears to have been informed by their performances in relation to the selected criteria, namely 'magnitude of investment flows', 'market potential for future investments', and 'stability and predictability of investment climate'. Table 6 below summarises the ranking of the priority countries for the selected indices used in this study. In order to assess EU priorities it is perhaps useful to differentiate between comprehensive investment agreements covering both access for EU investors and investment protection (in other words pre and post establishment national treatment), investment liberalization agreements (pre establishment national treatment) and investment protection agreements (post-establishment). See the following section for details on the various elements of investment protection. Target countries should be near the top of the chart in terms of existing investment stocks (current importance) and market potential as far as market access/liberalization of investment is concerned, but nearer the bottom of the investment protection chart. Agreements focusing on investment liberalization should clearly focus on partners with market potential as those countries that already figure high in the rankings for investment stock are clearly already largely open for EU outward investors.

Singapore and Canada are near the top of the indicators for investment stocks and Singapore for market potential, but both also offer high standards of investment protection, which suggests that other less well performing countries should be the priority for EU investment protection agreements. China, excluding Hong Kong scores very high on the market potential index, not especially high in terms of investment stock (in fact China is still small in terms of EU investment stock) and low in terms of the stability and predictability of its investment climate. China therefore appears to fit the bill for a comprehensive agreement covering liberalization and investment protection. Similarly, Russian Federation and Brazil (member of Mercosur) are quite important for EU27 outward and inward investment, offer substantial market potential and come a good way down the list in terms of investment protection. Argentina (member of Mercosur) has similar characteristics but a lower potential. Russia, Brazil therefore also appear to fit the bill for comprehensive investment agreements. India also falls into this category as having market potential, but relatively poor ratings on investment protection. The distinction between market potential and investment protection should not be overplayed however, since company's willingness to invest also depends on the investment protection.

In terms of countries not listed in the Commission's priorities the Gulf states have rapidly increased their share in EU27 inward and outward investment flows over the recent years, but they already offer relatively stable and predictable investment climates for EU outward investors. Malaysia, Israel, Mexico and South Africa are other countries that offer market potential, although not as great as the leading emerging markets, and offer rather better investment protection (except for South Africa).

Table 6. Ranking of priority and non-priority countries according to selected indicators

	EU27 Outward stocks	EU27 Inward stocks	Market potential	Ease of Doing Business Rank	Protecting investors ranking
Priority countries	Rank	Rank	Rank	Rank	Rank
Singapore	8	10	1	1	2
Canada	4	7	-	8	5
China (exl. Hong Kong)	13	20	2	<20	<20
Hong Kong	11	13	3	3	3
Russian Federation	6	11	9	<20	<20
Brazil	9	6	16	<20	<20
Argentina	<20	<20	18	<20	<20
India	20	15	11	<20	<20
Non-priority countries					
Gulf Countries*	12	4	15 (SA)	13 (SA)	16 (SA)
Malaysia	<20	<20	10	<20	4
Israel	<20	<20	6	<20	5
Mexico	15	16	14	<20	10
South Africa	<20	18	<20	<20	<20

*Gulf states: (AE, BH, IQ, KW, OM, QA, SA, YE)

**SA: Saudi Arabia

Conclusions on focus

The above analysis suggests that the priority negotiating partners for EU investment agreements identified in the Communication are broadly in line with the criteria analysed here. These suggest that negotiations with China (excluding Hong Kong), India and Russia should aim at comprehensive investment agreements. In the case of Canada and Singapore the focus should be on market access. But even here the fact that these countries are already major investment partners with the EU suggests that there are no major impediments to outward EU investment.

6 WHAT ARE THE BEST AVAILABLE STANDARDS FOR INVESTOR PROTECTION?

The rationale for International Investment Agreements (IIAs) [9]

Of primary importance to EU international investment policy, as outlined in the 2010 Communication from the Commission are the objectives of investment *promotion, protection* and *liberalization*. International Investment Agreements (IIAs), BITs and comprehensive trade and investment agreements, represent one visible component of an overall investment policy as well as a potential tool for achieving these triple objectives. IIAs have evolved historically as a government response to investor concern about enforcing their property rights in the developing host countries in which they were investing, particularly in situations where host legal systems were weak. Since the first BIT was signed between Germany and Pakistan in 1959, developed country governments have sought to protect their investors just as developing countries have sought to attract investment. While the empirical data is mixed regarding the effectiveness of IIAs at promoting investment into developing countries[10], the case is stronger regarding the effectiveness of IIAs in investor protection. Close to 3000 IIAs had been signed by 2009, many with comprehensive investor protection provisions backed by strong enforcement mechanisms. The EU member states' dominance is clear with Germany, UK, Italy, France, Netherlands, Belgium and Luxemburg among the top ten signatories[11], and EU member state BITs totaling over 1300.

What do modern IIAs contain?

While IIAs have evolved greatly since 1959, today's modern agreements are broadly aimed at 1) ensuring non-discriminatory treatment for foreign investors, 2) securing for investors appropriate levels of protection and operating flexibility as well as 3) providing a means of enforcing such commitments. The following sections looks at each of these components of IIAs in turn with a view to highlighting recent developments or 'best' practice in order to inform the debate on future EU international investment policy.

Non-discriminatory treatment of investors

One of the key components of IIAs is the substantive provisions dealing with the treatment of investors and their investments. Most agreements will seek to ensure non-discriminatory treatment for investors while often also ensuring that treatment does not fall below an internationally understood minimum standard of treatment. General standards of treatment include *national treatment*, *most favoured national treatment* and *fair and equitable treatment*.

National Treatment

Virtually all IIAs will seek to ensure *national treatment* for investors. *National treatment* 'requires that foreign investors should receive treatment no less favourable than that accorded to nationals of the host country engaged in similar business activity.'[12] This is a key aspect of any investment agreement

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[9] The Abbreviation IIAs is used to refer to both Preferential Trade and Investment Agreements (PTIAs) containing substantive investor protection provisions and Bilateral Investment Treaties (BITs).
[10] Studies by UNCTAD (1989), (Lesher and Miroudot (2007), Selacuse and Sullivan (2005), Neumayer and Spess (2004), Tobin and Rose-Ackerman (2004), Eggar and Pfaffermayr (2003), Hallward-Dreimeier (2003) , Buthe and Milner (2004), Gross and Trevino (2006), Egger and Marlo (2007), Swenson (2005), Yackee (2007), Aisbett (2007) and Rose-Ackerman (2008) have looked at this issue and shown mixed results regarding the correlation between BITs and levels of FDI within developing countries
[11] UNCTAD – Recent Developments in International Investment agreements (2008-June 2009)pp. 2-7.
[12] Muchlinski, Peter. The Framework of Investment Protection: The Content of BITs - derived from Peter T. Muchlinkski *Multinational Enterprises and the Law* (Oxford, Oxford University Press, 2nd Ed, 2007). Reprinted as Chapter 2 in: Sachs, Lisa and Karl P. Sauvant. 2009. *The Effect of Treaties on Foreign Direct Investment: Bilateral Investment Treaties, Double Taxation Treaties, and Investment Flows*. Oxford University Press

and crucial for ensuring that a country's investors do not face discrimination vis-à-vis local businesses. Because *national treatment* involves a comparison between the treatment of domestic and foreign investors, there are often issues regarding how to determine an appropriate comparator. Many EU IIAs are silent on this issue, even such recent agreements as the 2009 BIT between Germany and Pakistan. Others make reference to a comparator as illustrated by the 2005 BIT between the US and Uruguay which states that:

'Each Party shall accord to investors of the other Party, treatment no less favourable than that it accords in like circumstances, to its own investors…'

While arguably greater specificity provides guidance to tribunals hearing investor-state disputes on this issue, difficulties still exist in establishing what *like circumstances* mean in practice and whether the parties are referring to the same industry, a similar company or some other like circumstance. See figure 7 for a comparison of national treatment provisions in various agreements.

Figure 7 EU and North American Model Agreements – Provisions on Pre and Post Establishment

	Pre Establishment Coverage			Post Establishment Coverage		
	NT	MFN	PR*	NT	MFN	PR
German Model				+	+	+
French Model				+	+	+
Belgium/ Luxembourg Model				+	+	+
Canadian Model	+	+	+	+	+	+
US Model	+	+	+	+	+	+

***PR= Performance Requirements see discussion on this below.**

Based on 2005 OECD Report entitled 'Novel Features in OECD Countries' Recent Investment Agreements: An Overview

While most IIAs include provisions on *national treatment*, there are also differences in the way they are dealt with both within existing EU member state BITs and IIAs in other regions, particularly North America. There are three key things that need to be considered when considering the EU policy on *national treatment* protection:

– ***To what extent should EU investment policy seek to secure market access for investors?*** Where market access or investment liberalization is the goal pre-establishment national treatment is key. Most North American IIAs provide for *national treatment* in the 'establishment, acquisition and expansion'[13] of the investment and not only the 'management, use, enjoyment and disposal' of the investment which is the case in EU member state BITs. The more liberalising approach is that of NAFTA because it includes non-discriminatory treatment of investors at the pre-establishment phase and therefore the unhindered entry of foreign direct investment into all sectors of the host economy. When *national treatment* is provided for at the pre-establishment phase, countries will

[13] See the 'Treaty Between the United States of America and Republic of Uruguay Concerning the Encouragement and Reciprocal Protection of Investment' 2005 Article 3 and the 'North American Free Trade Agreement' 1992 Article 1102

however, generally identify non-conforming measures or exceptions or reservations to the application of *national treatment* obligations. In this way they determine which industries are open to foreign investment and which sectors or activities are to be excluded, often for reasons of national political sensitivity or for development considerations.[14] General EU level exclusions from liberalizing pre-establishment national treatment would therefore be in line with international practice, but would clearly open up the possibility of similar exclusions by the EU's negotiating partners.

– ***Should national treatment requirements apply to all levels of government****?* IIAs generally allow investors to 'hold the host state liable for breaches committed by any branch of government (executive, legislative, or judicial) and at any level of government (federal, state, provincial, or local).[15] Internally the EU generally liberalizes all levels of government and also seeks similar coverage of sub-national government in international agreements (such as on technical barriers to trade, government procurement, services trade etc.). Federal states, such as all the NAFTA parties, do not always extend the reach of international agreements to the sub-central level. This is also likely to be an issue in negotiations with states such as India and China where investment policy is shaped by policies at the sub-central level. It is important to be aware of this from a policy perspective and to understand both the implications of such commitments and how they are best communicated to those levels of government covered by the scope of the agreements.
– ***Should the EU approach specify the basis for comparison for non-discrimination?*** Most EU member state BITs appear to be silent on the basis for comparison in the application of *national treatment*. Some newer member state BITs such as the 2009 revised BITs between Canada and Latvia, Slovakia, Czech and Romania provide for such a comparator. Possibly because this is Canadian rather than EU member state practices. This obviously provides greater power of interpretation to tribunals while allowing for case by case interpretation. As mentioned earlier where IIAs specify a comparator such as '*in like circumstances*', there still remains some difficulty in interpreting what this means in practice.
– ***Should there be exceptions to national treatment for issues such as 'national security, public health or industry specific development exceptions'****?* Many countries feel that these types of exceptions are crucial for retaining their ability to set public policy in areas of social sensitivity. Again it is the NAFTA parties that have the more extensive provisions here. EU member state BITs are required to provide for exceptions in order to comply with the provisions of Art 64 (3) TFEU that allow the EU to take 'a step backwards' as regards liberalization of the movement of capital, and Art 66 TFEU in the case of 'serious difficulties for the operation of economic and monetary union.'

Most Favoured Nation Treatment (MFN)

As with national treatment, most modern day IIAs provide for *most favoured nation treatment*. The MFN standard ensures that investors are treated as favourably within the host country as any other third party with whom that country has an agreement. This form of treatment allows for the 'equality of competitive conditions'. In other words 'States have traditionally used MFN clauses in trade treaties to ensure that they obtain any advantages, privileges and concessions that the granting state has accorded or accords in the future to third parties.'[16]

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[14] Exceptions are often specified for the protection of cultural industries such as in the case of Canada or to carve out existing discriminatory policies aimed at protecting or developing sensitive industries such as air transport, energy, telecommunications or defence.
[15] Finizio, Steven P, Ethan G. Shenkman and Julian Davis Mortenson. *Recent developments in investor-state arbitration: effective use of provisional measures*. Global Arbitration Review. ICSID. 2006
[16] Newcombe, Andrew and Lluis Paradell. 2009. *Law and Practice of Investment Treaties*. Kluwer Law International. p 195

As with *national* treatment, the questions for the EU are:

- ***To what can and should the EU seek to secure market access for investors vis-à-vis those of third countries?*** The EU could seek MFN treatment with US or other national BITs and thus apply this clause to pre-establishment or post-establishment phase of the investment. Again EU member state and North American approaches have differed. There is also an MFN issue relating to member state BITs as discussed above, but this section is concerned with the content of common EU IIAs.
- ***Should the EU specify the basis for comparison?*** As with *national* treatment many BITs are silent on this while others such as NAFTA provide for comparison based on 'like circumstances'. Again, it will depend how much interpretive power one would like to bestow on tribunals as well as the level of confidence that such a comparator will assist in the specificity of the treatment.
- ***Should MFN be subject to exceptions*?** Member state BITs these are required to include an exclusion for member state commitments under EU law. In other words rights the benefits a third country has under a member state BIT cannot be extended throughout the EU. When negotiating with a country that is itself part of a regional grouping (e.g. Mercosur or ASEAN) the EU will need to consider the application of MFN to all members of such a region.

Fair and Equitable or Minimum Standard of Treatment

Unlike national treatment and MFN treatment, which are universally understood relative standards, *fair and equitable treatment* attempts to set out an absolute baseline standard of treatment for investors or a minimum standard below which treatment must not fall. 'Minimum standards of treatment serve a key role in promoting and protecting foreign investment by assessing government conduct based on internationally accepted standards of good governance.'[17]

Fair and equitable treatment is seen as an important and broad standard of treatment and it appears in most IIAs. It is however ill defined, with wide variations in how it is dealt with and understood within treaties. One approach provides for the *fair and equitable treatment* standard to be measured without limitation or reference to any other standard, while a second approach measures it against the *minimum standard of treatment* as defined in customary international law. The minimum standard of treatment, because it is grounded in customary international law is constantly in the process of developing, having continued to evolve since the 1926 landmark *Neer Claim*[18]. It is seen as a 'norm in customary international law which governs the treatment of aliens, by providing for a minimum set of principles that States, regardless of their domestic legislation and practices, must respect when dealing with foreign nationals and their property.'[19] It is furthermore seen as including such elements as the 'denial of justice, lack of due process, lack of due diligence, and instances of arbitrariness and discrimination.'

The confusion arises in that *fair and equitable treatment* (on its own - where it is not referenced against any other standard) is seen as requiring at least the minimum standard of treatment but may in fact go beyond such treatment. Given that the minimum standard of treatment is itself an evolving standard, the broader meaning of *fair and equitable treatment* is not concisely defined and is seen on its own, as providing tribunals a much more open-ended mandate of interpretation.

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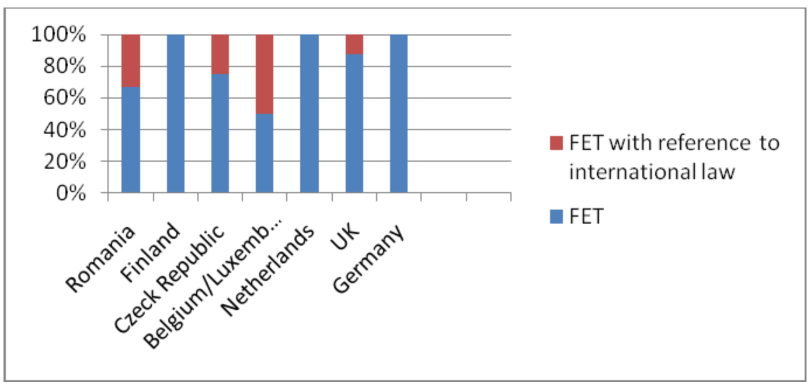
[17] Ibid. p. 234

[18] A landmark case for the international minimum standard was the 1926 decision on the Neer Claim in which the US Mexico Claim Commission stated that '...the treatment of an alien, in order to constitute an international delinquency should amount to an outrage, to bad faith, to wilful neglect of duty, or to an insufficiency of governmental action so far short of international standards that every reasonable and impartial man would readily recognize its insufficiency.' United Nations, Reports of International Arbitral Awards, 1926, IV, pp.60ff.

[19] OECD Working Papers on International Investment. ' Fair and Equitable Treatment Standard in International Investment Law'. September 2004

In practice EU member states have tended to provide for *fair and equitable treatment,* sometimes combined with other treatment standards such as 'full protection and security' in their IIAs. See table 8. While it has not been standard practice for EU member states, more and more are linking *fair and equitable treatment* to customary international law or the customary international law minimum standard of treatment. The recent BITs from Germany and those between Canada and Latvia, Slovakia, Czech and Romania have included such a reference, as have Canadian agreements with countries such as Columbia, Mexico, Peru and Venezuela. North America IIAs, most notably NAFTA and the model BITs of both Canada and the US contain provisions dealing with the Minimum Standard of Treatment (MST). These agreements have sought to anchor fair and equitable treatment and full protection and security in international legal minimum standard below which the treatment of investors should never fall and have argued that any interpretation of *fair and equitable treatment* not go beyond the minimum standard of treatment found in customary international law. A number of investor-state disputes have arisen under NAFTA on this issue and led the NAFTA Free Trade Commissions (FTC) to issue a clarification of the meaning of the MST provision.[20]

Table 8 EU member state BIT application of Fair and Equitable Treatment (FET) and customary international law



Based on a study of 51 recent EU member BITs – see Annex x for details of the sample

For more detail on the investment protection provisions in EU member state BITs see table 9 in the annex.

In deciding how to address the issue of *fair and equitable treatment*, the EU will need to consider:

– How important is it to ensure investors receive an absolute level of treatment irrespective of the relative treatment provided to host country nationals and third parties through national treatment and MFN treatment? While controversial and ill defined, this standard is seen as an important component of any IIA. Furthermore 'where there is no express fair and equitable treatment clause in the IIA, such as in the case of the 2007 German-Nigeria BIT or 1985 Italy-China BIT, the standard is likely to be applicable based on an MFN clause.'[21] In other words, if an

[20] The NAFTA Free Trade Commission issued a binding interpretation on July 21, 2001 which state that: *Article 1105 (1) prescribes the customary international law minimum standard of treatment of aliens as the minimum standard of treatment to be afforded to investments of investors of another Party. The concepts of 'fair and equitable treatment' and 'full protection and security' do not require treatment in addition to or beyond that which is required by the customary international law minimum standard of treatment of aliens. A determination that there has been a breach of another provision of the NAFTA, or of a separate international agreement, does not establish that there has been a breach of Article 11-5 (1)'*

[21] Newcombe, Andrew and Lluis Paradell. 2009. *Law and Practice of Investment Treaties*. Kluwer Law International. p 253

investment is already entitled to MFN treatment, investors will have access to fair and equitable treatment where it is available in a third state.

– To what extent should the fair and equitable treatment standard be grounded in the evolving yet more clearly bounded minimum standard of treatment? Once a decision has been made to provide investors with fair and equitable treatment, it is important to consider to what extent one may wish to bound or confine the meaning of such a standard and how it may reduce interpretive uncertainty under any future investor-state dispute settlement. As mentioned earlier, it is commonly agreed that fair and equitable treatment requires at least the minimum standard of treatment and 'no IIA awards nor any commentator have suggested that fair and equitable treatment provides less favourable treatment than the minimum standard of treatment.'[22] The larger question is whether and to what extent it goes beyond the minimum standard of treatment.

Protection of Investors

A core aim of comprehensive investment agreements is to both provide protection for investors and ensure they have operational flexibility in the countries in which they are investing. This will generally take the form of provisions ensuring the free transfer of funds in relation to the investment out of the host country and compensation for losses due to expropriation, armed conflict or internal disorder.

Should EU policy provide for the free transfer of funds?

Virtually all IIAs deal with the issue of the free transfer of funds. This is a crucial component of any investment agreement as it ensures that 'the investor can transfer the income from its investment out of the jurisdiction of the host country and repatriate its capital on termination of the investment'.[23] There are a number of things to consider with respect to the transfer of funds. 1) The scope of the transfer rights including limiting any 'domestic restrictions on the sale or disposition of the investment that prevent the investor form liquidating its investment'[24] 2) The type of funds covered by the transfer, with the preferred option in IIAs being to ensure coverage for as wide a variety of transfers as possible based on a non-exclusive illustrative list. 3) Convertibility rights both in terms of the type of foreign currency and the exchange rate applicable at transfer. 4) Permissible restrictions on transfers, where the goal is to minimise the scope and number of delays and restrictions that states may impose on transfer. 5) Express exceptions to transfer obligations such as in cases of balance of payment crisis.[25]

Compensation for losses due to armed conflict or internal disorder?

Compensation for losses due to armed conflict or internal disorder is frequently dealt with in IIAs and generally recommends that the investor be treated 'in accordance with *national treatment* and *MFN* standards in the matter of such compensation'.[26]

Should an EU investment agreement cover compensation for expropriation (both direct and indirect)?

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[22] Ibid. p277

[23] Muchlinski, Peter. The Framework of Investment Protection: The Content of BITs - derived from Peter T. Muchlinkski *Multinational Enterprises and the Law* (Oxford, Oxford University Press, 2nd Ed, 2007). Reprinted as Chapter 2 in: Sachs, Lisa and Karl P. Sauvant. 2009. *The Effect of Treaties on Foreign Direct Invesment: Bilateral Investment Treaties, Double Taxation Treaties, and Investment Flows*. Oxford University Press

[24] Newcombe, Andrew and Lluis Paradell. 2009. *Law and Practice of Investment Treaties*. Kluwer Law International. p 407

[25] Ibid pp406-416

[26] Ibid.

Customary international law allows host states to expropriate foreign investments assuming certain conditions are met including the provision of compensation. Expropriation can take the form of a direct expropriation, i.e. nationalisation involving either the 'formal transfer of title or outright physical seizure'[27] of assets. Expropriation can also occur however where there is a clear 'interference by the state in the use of that property or with the enjoyment of the benefits, even where the property is not seized and the legal title not affected.'[28] This type of action is often referred to as *indirect expropriation* or *measures tantamount to expropriation*. The difficulty arises in defining which measures taken by the host state that interfere with property should be considered indirect expropriation. Government measures for example such as non-discriminatory taxation, consumer protection initiatives or legitimate environmental regulations, which are considered 'essential to the efficient functioning of the state' are not considered expropriation and would therefore not be compensable.

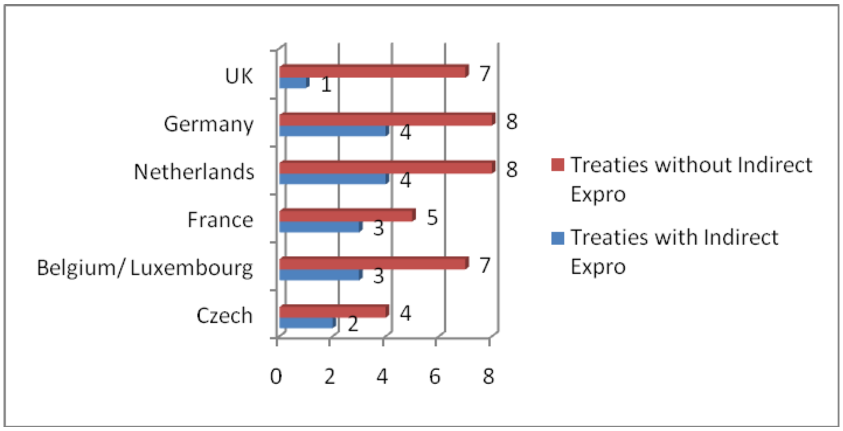
IIAs aimed at protecting investors including EU member state BITs, nearly always provide for compensation for expropriation. It also remains however, one of the most controversial provisions for the reasons mentioned above. The majority of IIAs cover expropriation and 'contain a provision that permits expropriation or nationalization of assets owned by the investor from the other contracting country only where this is done for a public purpose, under due process of law, without discrimination, and upon the payment of 'prompt, adequate and effective' compensation in accordance with the fair market value of assets immediately before expropriation'.[29]

Should the EU approach to investment seek to define indirect expropriation and non-compensable regulatory measures?

Many IIAs also cover the issue of *indirect expropriation* or measures tantamount to expropriation. In a study of 51 BITs completed by EU member states in the last 10 years we found a mixed record, with many countries such as Germany, France and the Netherlands providing protection against *indirect expropriation* in close to half of their agreements. Italy did not cover indirect expropriation in any of the BITs analyzed, while the UK dealt with it in only one out of seven. See table 10. Moreover in none of the 23 BITs where *indirect expropriation* was covered, was it clearly defined. The controversy arises in terms of how to deal with non-compensable regulatory issues and most IIAs are silent on this, with no distinction made between compensable and non-compensable regulatory actions. French BITs refer to 'measures of expropriation or nationalisation or any other measures the effect of which would be direct or indirect dispossession'. UK BITs cover measures 'having effect equivalent to nationalisation or expropriation', while some agreements concluded by Sweden refer to 'any direct or indirect measure'. [30]

Table 10 EU countries' inclusion of indirect expropriation provisions in recent BITs

[27] OECD "Indirect expropriation and the right to regulate in international investment law', OECD working paper on International Investment
[28] Ibid
[29] Ibid.
[30] OECD Working Papers on International Investment. 'Indirect Expropriation' and the 'Right to Regulate' in International Investment Law. 2004



Based on a study of 51 recent EU member BITs – see Annex x for details of the sample

Some North American IIAs have tried to define the issue of non-compensable regulation explicitly. NAFTA and both the 2004 Canadian and US model BITs do this in great detail. The inclusion of such a definition followed extensive investor-state litigation aimed at challenging the legitimacy of government regulation. Both the 2004 Canadian Model Foreign Investment Promotion and Protection Agreement and the 2004 US Model BIT address the issue of indirect expropriation and the right to regulate in a similar way. The US Model BIT states that:

'Except in rare circumstances, non-discriminatory regulatory actions by a Party that are designed and applied to protect legitimate public welfare objectives, such as public health, safety and the environment, do not constitute indirect expropriations.'

With cases slowly making their way through the arbitral process, this clarification has arguably provided guidance to tribunals in their deliberations.

The issues for the EU approach to investment can be summed up as follows:

– ***Should protection for investors extend to both direct and indirect expropriation?*** Discrimination can often take the form of indirect expropriation disguised as legitimate taxation or regulation. EU investors in third markets will expect protection against such measures under any EU agreement to match those under member state BITs. On the other hand, concerns obviously exist that the inclusion of indirect expropriation in IIAs could lead to challenges of legitimate EU regulation in the areas of health, safety and the environment.
– ***Should indirect expropriation be clearly defined or left to the discretion of tribunals?*** Current international standards of definition exist in the context of IIAs signed by countries such as Canada, the US and some recent EU member state BITs such as between Canada and Latvia, Czech Republic, Slovak Republic and Romania. These definitions have sought to lay out what constitutes legitimate government measures that are *designed and applied to protect legitimate public welfare objectives, such as public health, safety and the environment, and do not constitute indirect expropriations.* To date it appears that tribunals have taken on board this interpretation. It is worth considering whether such specificity will preserve EU government's right to regulate while still ensuring the appropriate protection for investors against a very real form of creeping expropriation.

Other important provisions found in IIAs

A number of other provisions have emerged in IIAs signed within the last ten years. These include provisions that prohibit the imposition of performance requirements on investors by host countries, similar to the WTO agreement on Trade Related Investment Measures (TRIMs) and requirements regarding senior management and boards of directors. Such provisions prohibiting the use of performance requirements (such as the requirement to export a given percentage of goods or services, achieve a certain percentage of domestic content in their production or to transfer a particular technology) are found in many North American IIAs, though not currently espoused by EU member states and reflects the desire of governments to protect their investors against requirements linked to the establishment or operation of their investment.

Provisions related to *senior management and boards of directors* prohibit the requirement by host countries that senior management positions or a majority of the boards of directors be of a particular nationality. While arguments have been made that countries have already made similar commitments as signatories of the TRIMs agreement, the IIAs cover more performance requirements and – a key difference - provide access to investor-state dispute settlement at both the pre and post establishment phases and thus much better enforcement. These provisions where they exist are generally subject to a carve-out or set of exceptions for each Party's existing non-conforming government measures as is the case with *national treatment* and *MFN*.

Should the EU approach to investment agreements include investor-state dispute settlement?

Virtually all modern day IIAs have provisions dealing with the settlement of disputes both those arising between the contracting parties and disputes between the host state and the investor.

State-to-State dispute settlement

Generally when disputes arise between the contracting parties, the 'usual procedure is for a dispute to be settled by negotiation between the contracting countries, or, if this is not possible, to go to arbitration.'[31] The types of disputes most likely to arise between states would be more procedural in nature and in practice disputes of this nature have rarely gone to international arbitration, but are settled through diplomatic means.

Investor-State dispute settlement

The more contentious disputes are those that arise between host country governments and foreign investors. The issue of enforcement and dispute settlement provisions is dealt with in more detail in the next section, including trends in investor-state dispute settlement such as greater transparency in arbitral proceedings, as well as concerns raised by recent litigation. The absence of investor-state dispute settlement in an EU approach would imply much less effective enforcement than available under member state BITs and seems certain to make any such EU agreement more or less irrelevant.

Final issues for consideration

There are a number of more general issues that need to be considered when determining the most appropriate standards for investor protection.

Should the EU approach to IIAs address labour, environment and health and safety?

Recently a number of countries have led the way in establishing provisions in IIAs aimed at preventing parties from lowering environmental and labour standards and general exception clauses aimed at protecting the right of parties to regulate in the public interest. With the exception of Belgium-Luxembourg, EU member state BITs have not included such provisions while North American BITs have,

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[31] Muchlinski, Peter. The Framework of Investment Projection: The Content of BITS – derived from Peter T. Muchlinkski *Multinational Enterprises and the Law* (Oxford, Oxford University Press, 2nd Ed, 2007). Reprinted as Chapter 2 in: Sachs, Lisa and Karl P. Sauvant. 2009. *The Effect of Treaties on Foreign Direct Invesment: Bilateral Investment Treaties, Double Taxation Treaties, and Investment Flows*. Oxford University Press

see table 11. Where included these provisions have gone some way to reassuring those concerned with labour and environmental standards, that IIAs are seeking an appropriate balance between the rights of investors and the public interest. Generally these provisions have taken the form of best endeavor clauses aimed at ensuring that countries do not lower environmental and labour standards in order to encourage investment and have not been subject to dispute settlement provisions. Calls for reciprocal requirements to be placed on investors to operate responsibly in developing countries have continued to be made. Some have suggested providing links to the OECD Guidelines on Multinational Enterprises. The Guidelines represent recommendations to multinational enterprises (MNEs) by the Governments of the OECD member countries aimed at ensuring MNEs act responsibly and according to the laws of the countries in which they operate. While voluntary and not legally enforceable they represent commitments to building an atmosphere of confidence and predictability between business government and labour.

Table 11 Inclusion of 'sustainable development' provisions in EU member state and North American model IIAs

	Environment	Labour
German Model		
French Model		
Belgium/ Luxembourg Model	+	+
Canadian Model	+	+
US Model	+	+

Based on 2005 OECD Report entitled 'Novel Features in OECD Countries' Recent Investment Agreements: An Overview

Recent EU trade agreements, such as the EPA between the EU and CARIFORUM while not a traditional IIA, have attempted to address this issue through a commitment not to lower environmental or labour standards in order to attract investment, as well as through a provision on the *behaviour of investors*. Article 72 of the EPA commits the Parties to cooperate and take domestic action to ensure investors do not partake in bribery, that they act according to core international labour standards, do not circumvent environmental or labour obligations of the state and maintain appropriate liaisons within the communities in which they will be operating.[32] The commitments under this agreement are not subject to a binding international enforcement mechanism, but fall within the remit of the domestic legal systems. The challenge of addressing this issue in the context of a treaty between states is the inability to bind the actions of individual investors who are not signatories to the treaty. Additionally it has been argued that a right of action by the state against investors can already be upheld in host domestic courts. It is likely that pressure will continue to be placed on states to promote the responsible behaviour of its foreign investors. While it is difficult to imagine how this can be more than hortatory in nature, simply embedding commitments within IIAs will show the positive intent of the contracting parties. This issue is addressed more fully below in the context of policy coherence in EU investment policy.

[32] Economic Partnership Agreement between the CARIFORUM States and the European Union. 2008

7 HOW SHOULD THE EU HANDLE DISPUTE SETTLEMENT PROCEDURES, ESPECIALLY INVESTOR STATE DISPUTE SETTLEMENT?

History and purpose of dispute settlement provisions

Historically international investment disputes were settled through diplomacy or in rare cases through the intervention of states.[33] Prior and following WWII the use of international arbitration became more common for the settling of international investment disputes between states. The expansion of international business progressively led states to allow a more direct role for individuals in the process of international arbitration, though strictly for commercial disputes.[34] Investor-state arbitration as a means of resolving regulatory disputes between states and investors was first conceived under the Convention on the Settlement of Investment Disputes of 1965 which established the World Bank's Centre for Settlement of Investment disputes (ICSID). 'In the decades since the ICSID Convention was concluded states have ratified hundreds of investment treaties, all of which transplant the original model of consensual arbitration into the regulatory sphere.'[35]

What approach should the EU adopt to investor-state provisions?

Virtually all modern day IIAs have provisions dealing with the settlement of disputes under the agreement, both those arising between the contracting parties and disputes between the host state and the investor. Under IIAs, when disputes arise between the contracting parties, the 'usual procedure is for a dispute to be settled by negotiation between the contracting countries, or, if this is not possible, to go to arbitration.'[36] As mentioned previously, disputes of this nature have rarely gone to international arbitration, but are settled through diplomatic means. Most IIAs deal with state-to-state dispute settlement provisions in a similar manner. Provisions are generally short and concise and will provide choice of arbitration venue and arbitral rules.

The more contentious disputes are those that arise between host country governments and foreign investors. While most IIAs contain investor-state provisions, these provisions vary greatly in terms of their level of specificity, the nature of their application and the extent to which they have been used by investors. The unique nature of investor-state arbitration in international law has ensured that it remains controversial. 'According a private party the right to bring an action in an international tribunal against a sovereign country with respect to an investment dispute is a revolutionary innovation that now seems to be taken for granted.'[37]

IIAs that provide for investor-state dispute settlement generally take one of two forms, the EU style provisions, which are short and concise and the North American style provisions, which are quite comprehensive and prescriptive.[38] The different styles have evolved over time and are borne out of both regions' experiences with respect to investor-state litigation.

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[33] Salacuse, Jeswald and Nicholas P. Sullivan

[34] Van Harten, Gus. P 50

[35] Ibid. P. 57

[36] [36] Muchlinski, Peter. The Framework of Investment Projection: The Content of BITS – derived from Peter T. Muchlinkski *Multinational Enterprises and the Law* (Oxford, Oxford University Press, 2nd Ed, 2007). Reprinted as Chapter 2 in: Sachs, Lisa and Karl P. Sauvant. 2009. *The Effect of Treaties on Foreign Direct Investment: Bilateral Investment Treaties, Double Taxation Treaties, and Investment Flows*. Oxford University Press

[37] Salacuse, Jeswald and Nicholas P. Sullivan

[38] On average EU member IIAs have investor-state dispute provisions of one page in length while north American style provisions vary from 5-20 pates in length (including annexes).

The experience of EU member states as recipients of investor-state claims has been limited and perhaps explains the lack of specificity contained in investor-state provisions among EU member IIAs. As of 2009, roughly 55 investor-state claims had been launched against 14 countries. While the Czech Republic and Poland have received the most claims with 16 and 10 respectively, most EU member countries have not received more than 1 to 2 claims at most.[39] It is perhaps worth noting that as the discussion above shows the Czech Republic has gone further than many member states in its efforts to define more exactly standards of protection than other member states. The EU experience is in marked contrast to NAFTA countries, which faced a barrage of litigation in the 1990s, due in large part to the fact that NAFTA was the first IIA between developed countries. While the inclusion of investor-state dispute settlement provisions were originally intended to provide recourse for US and Canadian investors in their dealings with Mexico, many of the claims have been brought against these developed country governments.

For the EU there is therefore a question as to whether there will also be a growth in the number of cases brought against EU member states under the various BITs. If there were such a trend the case for an EU approach to more closely define the scope for dispute settlement would be greater. Table 12 below shows that it is Central and Eastern European member states that are the most subject to investor complaints, the Czech Republic and Poland leading the way.

Table 13 in the annex provides an overview of known cases since the mid-1990s involving EU Member states as respondents. The following observations can be made:

– Respondents tend to be Central and Eastern European member states brought into international arbitration proceedings by companies based in the older member states, generally using the BITs signed between these member states. Other litigants are companies from the United States, Canada and marginally Russia or Israel.

– The companies that litigate are frequently local companies who use headquarters in Western European countries or their strategic investor to litigate against actions taken by the state.

– Only rarely have Western European member states been respondents in investor-to-state arbitration cases. Two cases involve emerging market investors: Sancheti vs United Kingdom (Indian investor), and in the late 1990s, Emilio Agustin Maffezini, an Argentinian investor against Spain (ICSID Case No. ARB/97/7). Such cases could become more frequent in future as emerging market multinationals play an increasing role in the global economy. Yet, as the Mittal Steel case against the Czech Republic launched in 2005 shows, it is likely that these would use their EU headquarters to launch litigations.

– Government decisions questioned by investors in such cases are regularly upheld in such arbitration cases. Table 13 lists ten such cases, where the final outcome is known.

– The track record of known cases shows so far that application of public policies by EU member states is not infrequently upheld against investor claims.

[39]UNCTAD. Latest Developments in Investor State Dispute Settlement. IIA Issues note no. 1 (2010). United Nations

Table 12 Known International Arbitration Cases Against EU Member States

Czech Republic	16
Poland	10
Romania	7
Hungary	6
Slovakia	5
Estonia	3
Germany	2
Latvia	2
Lithuania	2
Slovenia	2
France	1
Portugal	1
Bulgaria	1
Spain	1
United Kingdom	1
Total	60
COMPARISON:	
United States	14
Canada	14
Source: UNCTAD	

Most EU member state BITs have been short and concise, with investor-state dispute settlement applying to all aspects of the agreement, choice of arbitration forum left to the discretion of the contracting parties, and generally with no provision made for appeals. Rules related to arbitral procedure both in terms of the selection and conduct of arbitration are based on the rules of the arbitral forum selected by the parties. In contrast the North American style investor-state dispute settlement provisions have become extremely lengthy and prescriptive. While also providing for choice of international arbitration forum they have sought to be specific on the process of submitting a claim, the selection of arbitrators and the conduct of arbitration. In addition many North American IIAs and particularly NAFTA and the model BIT of both the US and Canada provide for the possibility of establishing a bilateral appellate mechanism as well as provisions dealing with the consolidation of multiple claims. Reviews of arbitral panels are aimed to promote consistency and greater transparency in the interpretation of agreements. The North American approach have also included innovations in the shape of their treatment of transparency issues such as the publication of documents, the opening of arbitral proceedings to the public as well as granting the tribunal the authority to accept submissions from non-disputing parties or *amicus curiae*. The pros and cons of a number of these issues will be discussed in greater detail below.

Also of note is the fact that a number of IIAs make no provision for investor-state dispute settlement. It appears that some BITs signed between EU members such as Germany, France, Italy and the Netherlands and African, Middle East or Asian countries do not provide for such enforcement.[40] More

[40] See the 2005 German-Yeman BIT, 1985 France-China BIT and agreements between the Netherlands and Oman (2009) and Benin (2001) by way of example.

recently the US has pursued a FTA with Australia, which included a comprehensive investment chapter yet no provision for investor-state dispute settlement.

Arbitration venue

ICSID, while not a permanent tribunal, provides the main 'legal and organizational framework' for the disputes arising between investors and host states. It is the primary choice of arbitral body for the settlement of disputes alongside other bodies offering ad hoc arbitral proceedings such as the United Nations Commission on International Trade Law (UNCITRAL), the Stockholm Chamber of Commerce (SCC) and the International Chamber of Commerce (ICC). By 2009, there had been 357 known disputes and 63% or 225 of these were filed with ICSID or under the ICSID additional facility, 25% or 91 under UNCITRAL and 5% or 19 with the ICC. ICSID has also led the way in the area of transparency in arbitral proceeding as discussed below.[41]

While the majority of EU member states are signatories to the ICSID Convention and have enjoyed the use of its arbitration facilities in the context of their existing IIAs, the EU is not a member of the ICSID Convention and cannot at present become a member. This raises questions concerning the EU's relations and involvement in investor state dispute settlement cases. 'Unless the statue of the International Monetary Fund – which is also relevant for ICSID membership (only States can be signatories of the IMF statue) is modified, ICSID dispute resolution will remain no option for an EU agreements on investment.'[42]

Current trends with investor state dispute settlement

With the proliferation of investor-state arbitration cases, there are a number of trends and issues which impact upon EU thinking on how to handle dispute settlement procedures in the context of its international investment policy. Table 14 illustrates how the more detailed provisions on how investor – state arbitration are to be found in the North American BITs but absent from the EU approach.

Table 14 Detail on EU and North American model agreements' provisions on investor-state dispute settlement and arbitration

	Participation of non-disputing parties	Transparency	Open hearings	Amicus Curiae submissions	Consolidation of claims
German Model					
French Model					
Belgium/ Luxembourg Model					
Canadian Model	+	+	+	+	+
US Model	+	+	+	+	+

Based on 2005 OECD Report entitled 'Novel Features in OECD Countries' Recent Investment Agreements: An Overview

[41] UNCTAD. Latest Developments in Investor State Dispute Settlement. IIA Issues note no. 1 (2010). United Nations

[42] Herrmann, Christoph and Terhechte, Jorg Philipp. European Yearbook of International Economic Law 2010. Springer. P. 149

Should the EU favour transparency in arbitral proceedings and if so in what form?

While today's system of investor-state dispute settlement is grounded in the system of international commercial arbitration, it differs markedly due to the involvement of governments as a contracting party and the public policy content of the measures being challenged. In other words the concept that arbitrators rule on a purely commercial dispute behind closed doors may not offend in quite the same way as the same arbitrators deciding, in the same way, whether potentially sensitive public policy measures taken by a government are compatible with an investment treaty.[43] As such the confidential or *in camera* nature of proceedings has led to public concern, criticism and pressure for more openness, public access and transparency in the proceedings.

Generally most IIAs do not require public disclosure of information from the registration of the dispute through to the award itself, although existing arbitration rules differ on the issue of transparency depending on the forum. ICSID has a policy of registering disputes and where ICSID is providing administrative support for ad hoc arbitration under UNCITRAL rules this would also be the case. There is no publication or registration of disputes provided for in the cases of other fora such as the ICC or SCC. In 2006 ICSID implemented a number of key transparency amendments to its Convention. As a result ICSID has provided a right for non-parties to a dispute, such as public interest groups, to intervene in arbitration hearings through *amicus curiae* submissions, where the tribunal feels certain conditions have been met. While the parties to the dispute have no veto right over a tribunal's decision to accept these submissions, they do with respect to a non-parties' right to attend ICSID arbitration hearings. Transparency has been extended to make the publication of awards and the legal reasoning behind them mandatory.

More and more however, investment agreements are starting to provide for greater transparency. NAFTA led the way in 2001 and 2003 by providing respectively for public access to all documents submitted to Chapter 11 (dispute settlement) tribunals with the exception of confidential business information, and accepting submissions from third non-disputing parties, subject to certain guidelines.[44] Such an approach has been followed in subsequent IIAs negotiated by both the US and Canada including FTAs between the US and Chile, Singapore, and the Central American countries of Costa Rica, Dominican Republic, El Salvador, Guatemala, Honduras and Nicaragua. Canada has completed BITs with a number of countries that have included these transparency provisions including Peru in 2007 and a number of EU countries in 2009 including Latvia, Slovakia, Czech Republic and Lithuania.[45] Both the US and Canada have entrenched this approach by including a high level of transparency in their model investment agreements.[46]

The implications of such initiatives need to be considered in the context of any comprehensive shift in EU policy. Certainly the trend is towards more transparency and openness with the changes to the ICID Convention in 2006. Countries which make use of ICSID arbitration facilities, or the ICSID additional facilities will come under pressure to comply. Having a clear policy in this respect will be important. In deciding on a way forward it will be important to balance protection of confidential business information against the right of the public to have access to information that impacts important public policy issues. Arguments for the speedy publication of documents are based on the fact that 'there are

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[43] OECD (2005), 'Transparency and Third Party Participation in Investor-State Dispute Settlement Procedures', OECD Working Papers on International Investment, 2005/1,OECD Publishing.
[44] Ibid p.5
[45] See Annex C of the 'Agreement between the Government of Canada and the Government of the Republic of Latvia for the Promotion and Protection of Investment'. 2009 and Annex B of the 'Agreement between the Government of Canada and the Czech Republic for the Promotion and Protection of Investments'. 2009
[46] See the 2004 US Model BIT and the 2004 Canadian Model FIPA.

a growing number of arbitration awards which are likely to influence future cases' and that their publication would facilitate consistency and predictability in the system.[47]

Current concerns with investor-state dispute settlement

The number of investor-state disputes has been growing steadily since 2002 at a rate of between 28 and 48 cases a year reaching the total of 357 known cases by 2009.[48] Along with the increase in the use of international arbitration to resolve investment disputes have come concerns regarding the changing nature of investor-state litigation and its impact on government policy making autonomy. There is also the phenomenon of multiple claims with the increased potential for multiple claims leading to divergent interpretations of treaty provisions and forum shopping by claimants. Last but not least the increased number of cases has led to concerns about the growing financial cost of litigation for governments. These are examined in turn in the next section.

The extent and impact of potential litigation on policy making autonomy

The cases challenging government regulation following the adoption of NAFTA led to a concern in North America that investor-state litigation can serve to 'limit the regulatory flexibility of host countries to pursue not only economic development policies but other public policies as well."[49] Many of these cases have arisen as a result of challenges to government measures in the areas of health, safety and the environment, under the non-discrimination provisions (e.g. national treatment), provisions dealing with the minimum standard of treatment as well as the broad definition of expropriation.[50] The concern was that these challenges could lead to *regulatory chill*[51], as governments curtail or amend their regulatory initiatives in an effort to avoid multi-million dollar lawsuits brought by disgruntled corporate investors. Concerns were heightened by the first few NAFTA Chapter 11 cases which appeared to challenge the government's right to regulate in the areas of health safety and the environment. These cases saw challenges to government measures dealing with for example the banning of a gasoline additive in the cases of *Ethyl Corporation v. Government of Canada* and *Methanex v. Government of the United States of America* or a ban on the export of toxic PCB waste under *S.D. Myers Inc v. Government of Canada*.

However, this concern about regulatory chill does not appear to have been justified. To date the majority of cases related to regulatory policy have either been dismissed or decided in favour of the host Government and where decisions have been in favour of the investor, awards have been relatively small. Exacerbating this problem however is the concern over the 'role of privately contracted adjudicators to determine the legality of sovereign acts and to award public funds to businesses that sustain loss as a result of government regulation.'[52]

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[47] OECD (2005), 'Transparency and Third Party Participation in Investor-State Dispute Settlement Procedures', OECD Working Papers on International Investment, 2005/1,OECD Publishing.

[48]UNCTAD – Recent Developments in International Investment Agreements 2010

[49] Sachs, Lisa and Karl P. Sauvant. 2009. ' BITs, DTTs, and FDI Flows: An Overview' in: Sachs, Lisa and Karl P. Sauvant. 2009. *The Effect of Treaties on Foreign Direct Invesment: Bilateral Investment Treaties, Double Taxation Treaties, and Investment Flows*. Oxford University Press P xxxvii

[50] The provisions on expropriation refer to the compulsory acquisition of property by the state and are grounded in international law as well as in the international regulatory taking doctrine. Some concern has arisen over the broad definition of what constitutes expropriation, prevalent in modern investment protection agreements. Because the definition includes references to 'indirect' expropriation as well as government measures which are 'tantamount' to expropriation, it is conceivable that a government regulatory measure may fall under the definition of expropriation by negatively affecting the value of an investment, but without the actual removal of property rights.

[51] One definition of *regulatory chill* was put forward by Lorenzo Cotula in his article entitled: "Regulatory takings, Stabilization Clauses and Sustainable Development", submitted to the OECD Global Forum on International Investment in March 2008. He argued that regulatory chill could be defined as "the idea that the obligation to pay compensation for regulatory change may make it more difficult for host states to regulate in 'socially' desirable' areas such as human rights or environmental protection.."

[52] Van Harten, Gus. 2007 *Investment Treaty Arbitration and Public Law*. Oxford University Press. p. 5

How should the EU approach the issue of policy autonomy?

Concerns about government policy autonomy can be addressed where both the rules of arbitration are clear and the provisions which give rise to challenges of government measures are specific and well defined. As discussed in the section on standards of investor protection, the importance of clarity on issues such as the scope and desired breadth of *fair and equitable treatment* and the meaning of *indirect expropriation* with respect to what constitutes a non-compensable government regulatory measure will help reduce interpretive uncertainty. As a 2010 UNCTAD report confirms, 'some countries have revised (or are in the process of revising) those treaty provisions in their Model BITs that have been subject to controversial and diverging interpretation (such as the definition of investment, fair and equitable treatment, MFN treatment and indirect expropriation), with a view to clarifying in greater detail the meaning and scope of these provisions and to ensure a more coherent and predictable interpretation.'[53] This would imply longer more well defined - but also more complex - agreements than has been the practice for EU member states to date.

Multiple claims, divergent interpretation of treaties and forum shopping

Given the large number of IIAs currently in place, investors will often have a choice of fora in pursuing an international investment dispute. By claiming breaches of different IIAs and pursuing their claims under different arbitration proceedings the risk exists of conflicting awards. 'The most striking example of multiple proceedings emanating from the same single set of events by one government is the 40 cases launched against Argentina following a 2001 devaluation of the Argentine peso and the accompanying laws and decrees ending the regime of convertibility and parity of the peso with the US dollar, all as part of a stated public economic emergency.[54] The Argentine experience has involved cases initiated on the basis of BITs with G7 countries as well as countries from Latin America, Eastern Europe, Africa and Asia. [55] As UNCTAD spells out in its annual look at the latest developments in investor-state dispute settlement, 'the cases that were concluded in 2009 maintain the trend of diverging – and sometimes conflicting – awards.'[56]

Forum shopping is commonly understood to be the process by which a disputing party can bring a claim to the forum it finds most advantageous. In the case of investment disputes the issue is more complex. While the investor can select from a number of fora including an international arbitration body such as ICSID, domestic courts or an ad-hoc arbitration body such as UNCITRAL, it may also chose the most advantageous IIA under which to raise the claim.[57] The case of CME/Lauder v Czech Republic is illustrative of a number of these problems. In this instance the Czech Republic was subject to two simultaneous cases by the controlling shareholder of a US investor brought under the Czech BIT with the US and of a Dutch company under the Netherlands – Czech BIT. In this case an arbitral tribunal ruled in favour of the investor under the Netherlands-Czech Republic BIT and ordered the Czech government to pay $353m USD ten days after a parallel hearing saw a tribunal dismiss the same claim brought under the US-Czech Republic BIT.[58]

[53] UNCTAD. Latest Developments in Investor State Dispute Settlement. IIA Issues note no. 1 (2010). United Nations
[54] Yannaca-Smnall, K. (2006), "Improving the System of Investor-State Dispute Settlement', OECD Working Papers on International Investment, 2006/1, OECD Publishing. P.17
[55] Ibid. p.18
[56] UNCTAD. Latest Developments in Investor State Dispute Settlement. IIA Issues note no. 1 (2010). United Nations p. 12
[57] Ibid. P 20
[58] Van Harten, Gus. 2007 *Investment Treaty Arbitration and Public Law*. Oxford University Press. p7-8

How can the EU avoid multiple claims and divergent interpretations?

Clear provisions in IIAs on the consolidation of claims can reduce the risk of multiple claims where the challenges and facts of the cases are similar. There can also be rules on the use of the same arbitrators to hear the multiple claims. Current practices based on existing arbitral rules and the provisions in IIAs vary. While the consolidation of claims has been applied in commercial arbitration, currently 'the UNCITRAL Rules, the ICSID Convention, and the Additional Facility Rules, do not have any provision allowing for consolidation of claims.'[59] ICSID has however, in cases where both parties have agreed, consented to the consolidation of claims. Once again NAFTA's Chapter 11 Article 1126 represents the first IIA to make explicit provision for the consolidation of claims and consolidation provisions can now be found in numerous US and Canadian BITs. On the issue of appointing the same arbitrators to hear cases of a similar nature, ICSID has done so in the past with the claims against Argentina among others. 'The ICSID Secretariat recommended such an action in the cases *Salini Construttori S.p.A. and Italstrade S.p.A. v. Kingdom of Morocco* and *Consortium R.F.C.C. v. Kingdom of Morocco,* both based on the same BIT between Italy and Morocco and on similar factual and legal backgrounds. Although the two procedures were conducted separately, the identical tribunal avoided issuing inconsistent decisions.'[60] In the EU the consolidation of member state investment agreements into EU agreements can of course reduce the risk of multiple claims, but there will remain the risk of multiple claims against the EU under different EU agreements.

The financial risk

As eluded to above, the cost of litigation can be quite substantial. In the case of CME/ Lauder v Czech Republic Government the $353mUSD award in this case 'was roughly equal to the country's entire health-care budget.'[61] Argentina has also faced a huge financial burden as a result of the many cases launched in the aftermath of its 2001 emergency measures. In general it appears that not only the number but also the size of awards has been increasing. In 2006 and 2007 a number of awards to investors exceeded US$10 million.[62] The legal costs are in part a factor of legal capacity, which is unlikely to be an issue for the EU.

Should the EU approach provide for appeals/review of arbitral decisions?

International arbitration awards do not rely on domestic courts and are not subject to appeal on their merits. This arguably saves cost and time. But concern over inconsistency or flaws in awards has led to a continuing discussion about the benefits of an appeals process in international investment arbitration, and while the issue has been under consideration within ICSID for many years, no steps have been taken to make this a reality.

In the absence of a formal appeals process within international arbitration fora, countries have sought to establish mechanisms for appeal within the treaties themselves. The US has been at the forefront of this movement and has established provisions within most of its recent IIAs to address this issue. Its FTAs with Chile, Singapore and Morocco and more recently with the Dominican Republic and five Central American countries, along with its 2004 Model BIT have language allowing or in some cases mandating the parties to establish a bilateral appellate body.

[59] Yannaca-Smnall, K. (2006), "Improving the System of Investor-State Dispute Settlement', OECD Working Papers on International Investment, 2006/1, OECD Publishing. P 22
[60] Ibid. p.23
[61] Van Harten, Gus. 2007 *Investment Treaty Arbitration and Public Law*. Oxford University Press. p. 7
[62]Sachs, Lisa and Karl P. Sauvant. 2009. ' BITs, DTTs, and FDI Flows: An Overview' in: Sachs, Lisa and Karl P. Sauvant. 2009. *The Effect of Treaties on Foreign Direct Invesment: Bilateral Investment Treaties, Double Taxation Treaties, and Investment Flows*. Oxford University Press

There are a number of advantages and disadvantages to the establishment of an appeal mechanism in international investment disputes. It would promote consistency and coherence in jurisprudence, but can result in delays and costs, increases in caseload, a politicisation of the system as well as the erosion of the principle of finality, which has been the primary benefit of the arbitration system vis-à-vis domestic courts.[63]

Key questions for the EU on dispute settlement are therefore:

– Should investor-state dispute settlement form part of future EU IIAs?
  As mentioned previously, most IIAs include provisions for investor-state dispute settlement. It is clearly questionable how effective a treaty can be without effective investor-state provisions. These provisions are important to investors who have come to expect them and arguably rights without remedies are not rights. At the same time governments have legitimate concerns about the financial and administrative burdens of managing such disputes, as well as the potential impact on policy autonomy.

– Where they are included, how prescriptive should the provisions be?
  Should provisions be made to deal with appeals, consolidation of claims, the selection of arbitrators, key procedural issues and transparency, or should these be left to the discretion of the arbitral body? Clearly there will be differences in the rules of each arbitral body which may go against the wishes of the EU and the other disputing parties to the agreement. Where governments can be explicit about their interest and intentions they are more likely to benefit from the process. Additionally, specificity and clarity of the provisions themselves will reduce interpretive uncertainty.

Finally it will be important in getting the balance between the benefits of greater specificity and detailed investor-state dispute provisions.

8 HOW TO ENSURE FUTURE EU INVESTMENT AGREEMENTS ARE CONSISTENT OTHER POLICY AIMS AND THE COHERENCE REQUIREMENTS DERIVING FROM THE TFEU? WHAT ARE THE INTERNATIONAL TRENDS IN THIS REGARD?

It is important that future EU investment agreements are consistent with other EU principles, such as those concerning sustainable development, human rights and labour standards. The EU will need to balance the interests and rights of investors and the interests and rights of other stakeholders affected by the agreements. Hence it is crucial that the exercise of defining the scope and the content of investment agreements should follow a transparent, accountable and participatory process involving all relevant stakeholders. In this context, this study offers a balanced assessment of major policy areas where issues of coherence could arise and policy options as to how future EU investment agreements could be designed to ensure coherence.

Should EU investment policy include provisions on sustainable development?

As discussed above there has been an emerging consensus in some regions that multilateral and bilateral investment agreements should promote sustainable development in the host and investing

[63] Yannaca-Smnall, K. (2006), "Improving the System of Investor-State Dispute Settlement', OECD Working Papers on International Investment, 2006/1, OECD Publishing. p. 9-14.

countries, but there is no single definition of 'sustainable development' and there is no consensus on how that might be achieved. EU investment agreements may therefore need to be clear on what 'sustainable development' means. It could adopt a 'narrow' definition focusing on specific priority areas, such as labour standards and environmental protection that have already been included in some EU preferential trade agreements. This would ensure regulatory clarity and predictability in relation to the potential impact of agreements on the identified/defined dimensions of sustainable development. Alternatively, the EU could make an explicit commitment to sustainable development (potentially in the Preamble of the Agreement), but leave the definition broader such as in the European Commission's Sustainability Impact Assessment Framework.

Flexibility to accommodate partner country needs?

Given the diversity of the EU's potential partners in terms of their level of development a rigid 'one size fits all' or a 'template agreement' approach would have a number of disadvantages. In the case of agreements with developing countries in particular there is a balance to be found between allowing partner countries 'policy space' or the 'right to regulate' in order to pursue their own development agendas and the objective of promoting (EU) competitiveness through market access and investment protection. 'Policy space' intended to promote public goods can nevertheless lead to inefficient policies or be abused. The Commission has already made clear that it does not wish to establish an EU model BIT or investment agreement. On the other hand, the European Parliament, member states and stake holders wish to know what an EU approach to international investment agreements will look like.

What should EU investment agreements do about performance requirements?

As noted above some IIAs go beyond the TRIMs agreement in the WTO in disciplining 'performance requirements.' There is no clear evidence on the impact of performance requirements on development. They may help create certain public goods, for instance through the spill-over of knowledge and technology transfer, infrastructure improvements, and training of labour force. It has also been argued that they can be used to correct market imperfections, for instance those in labour markets and in sectors in which there is not adequate competition due to monopolistic or oligopolistic structures among investors. Certainly many developed and developing countries have used similar requirements as part of their industrial policies and they still persist in either formal or informal practices. On the other hand, performance requirements can be counterproductive - if they constitute a form of market intervention creating welfare losses by restricting competition and by creating disincentives to invest.

The EU's position on the scope of the 'policy space' in this field should be informed by objective assessment of whether a given set of performance requirements would be effective in achieving their stated objectives, deal with market failures and create public goods, or whether they likely to create welfare losses and form a disguised restriction on investment. Such an assessment could also consider whether there are alternative, more effective or less restrictive means of addressing market failures that are less damaging to welfare. The above discussion suggests that if performance requirements are to be allowed, the EU should be selective and should examine them on a case by case basis according to the circumstances, policy intentions and the needs of the host country.

How to address environment issues?

In the face of major environmental challenges, such as climate change, environmental degradation and loss of biodiversity, it is apposite that the EU investment agreements should deal with the impact of both inward and outward investment flows on the environment. Article 11 TFEU explicitly requires that 'environmental protection requirements must be integrated into the definition and implementation of the Union policies and activities, in particular with a view to promoting sustainable development.' EU investment policy should therefore consider how it might promote the transfer of green technologies, infrastructure improvements and capacity building in the field of environment and consider ways of reducing the adverse impact of inward and outward flows, such as resource degradation, deforestation, water, air and land pollution.

As noted above an important legal question is whether the EU agreements will have explicit provisions dealing with environmental concerns, or whether these are included in the preamble to an agreement, leaving ample discretion for contracting parties to regulate. There is a risk that the latter could lead to a serious asymmetry in relation to the environmental impacts of the EU's inward and outward investment flows. If the parties wish to maintain extensive policy discretion this may result in environmental concerns being properly addressed by the partners with strong and coherent environmental regulation, but ignored by the partners with weak regulation. Carbon leakage is a case in point where increasingly stringent climate mitigation regulations could push carbon-intensive production from industrialised countries to developing countries with less stringent environmental regulation.

In this context, the EU's interests in this field are both defensive (in dealing with environmental impacts of inward investment) and offensive (in preventing environmental damage, carbon leakage and outsourcing enticed by low environmental measures in partner countries). As such the conventional approach to environmental concerns through the Preamble, non-discriminatory and 'not lowering measures', or WTO-GATT Article XX type environmental exceptions may not provide the right legal framework to capture the EU's all defensive and offensive interests. The U.S. Model BIT was one of the first examples of investment agreements specifically addressing environmental concerns. Under it's Article 12, it adopted the 'no lowering measures' approach. It also strongly reinforced the contracting party's right to regulate investments in their territory to address environmental concerns. With a condition that such measures are not applied in an arbitrary, discriminatory or constitute a disguised restriction on international investment, contracting parties could adopt various environmental measures (necessary to protect human, animal, or plant life or health; or the conservation of living or non-living exhaustible natural resources).

Labour rights and standards?

As noted above a recent study on the impact of EU outward investments suggested that low-skilled labour in the EU could lose jobs even if the aggregate impact of outward investment on EU employment is neutral (Copenhagen Economics, 2010).[64] In this context, one needs to distinguish between outward investment (in the form of outsourcing) due differences in wages and due to weak labour laws of the host country. The EU approach to investment agreements should address the latter rather than the former.

One option would be to follow the US model and adopt the 'no lowering measures' principle that prohibits parties to encourage inward investment flows by weakening or reducing the existing levels of labour protection provided by domestic laws. Another option would be to include specific standards for labour rights, such as the 1998 International Labour Organisation's (ILO) Declaration on the Fundamental Principles and Rights at Work or other core ILO labour standards as included in the US BITs and some but very few EU member state BITs. It is worth recalling however, that the US labour provisions are not subject to dispute settlement nor for example are the EU provisions on sustainable development in the Economic Partnership Agreement (EPA) between the EU and Cariforum of 2007.

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[64] Copenhagen Economics (2010). *Impacts of EU Outward FDI*, Final Report, published 20 May 2010, available at < http://trade.ec.europa.eu/doclib/docs/2010/june/tradoc_146270.pdf>.

Again the issue of flexibility in the EU approach to investment agreements crops up. If the EU wishes to conclude an investment agreement with China, as is the stated aim in the Commission's Communication, on the grounds that it is an important emerging market with relatively poor investment protection, it is unlikely that the Chinese government will accept any agreement with binding obligations on core labour standards.

Corporate Social Responsibility and human rights?

There have been a number of multilateral initiatives creating codes of conduct for multinational enterprises. Most notably, the OECD Guidelines for Multinational Enterprises and the United Nations Global Compact. These are voluntary instruments that seek to encourage investors to comply with certain principles in the areas of human rights, environmental protection, anti-corruption and labour standards. Some 42 - mostly developed -countries have endorsed the OECD Guidelines for Multinational Enterprises. Only a small proportion of multinational enterprises (mainly of developed country origin) have shown serious commitment to the Global Compact by complying with regular notification and reporting requirements. Broadening the coverage of these initiatives to non-adhering countries and to non-committed companies (especially those located in developing countries) is a major challenge. Nevertheless these guidelines could be integrated into an EU approach to investment agreements. If this were the objective, a recent revision of the OECD guidelines highlighting the importance of good practices in three policy areas, namely human rights, supply chains, and environment and climate change, could be informative.

Part II – The draft Regulation on transitional arrangements

9 ASSESSMENT OF PRESENT LEGAL UNCERTAINTY

9.1 Legal uncertainty arising from the attribution of exclusive competence

With the coming into force of the Lisbon Treaty, the Union's competence for the area of the CCP has been enlarged to also comprise "foreign direct investment". By defining this competence as an exclusive competence, the member states have accepted that "only the Union may legislate and adopt legally binding acts, the member states being able to do so themselves only if so empowered by the Union".[65] There is a significant degree of uncertainty regarding the exact scope of the Union's competence for investment, which depends on the interpretation to be given to the term "foreign direct investment" used in the Treaty. See discussion in the first study. For the purpose of the present analysis it will be presumed that the EU's new exclusive competence may well cover a number of issues that are presently governed by provisions of the roughly 1200 bilateral investment treaties (BITs) concluded by Member States and third countries.

The change in the allocation of the competences between the Union and the member states does not affect the continuing validity of the member states' obligations under the existing agreements. Under international law, no state can invoke violations of its internal law on competence to conclude treaties to renounce its obligations under a validly concluded treaty.[66] It is, however, not clear to what degree the existing member state obligations can continue to be valid under European law, i.e. from an "internal" (EU) perspective. The Treaty's definition of the Union's exclusive competence suggests that the provisions in these BITs should no longer constitute "legally binding acts" under European law. In principle, this means that such provisions should not be given any legal effect within the European Union, i.e. by its institutions or by the Member States and their organs, on the ground of their incompatibility with the fundamental allocation of competences within the Union. The ECJ has condemned member states for giving effect of international treaty provisions that are found incompatible with the Treaties' competence rules.[67] Furthermore, it is very much disputed and quite doubtful that the Treaty provides for a general exemption for pre-existing international obligations of member states that become incompatible with new rules created in the Treaty itself.[68]

It follows that there is a degree of legal uncertainty regarding the continuing effectiveness of at least some of the existing standards of investment protection under the member state BITs, which translates into the following scenarios:

(1) The member states' obligation of cooperation in principle requires them, as of the entry into force of the Lisbon Treaty, to re-negotiate or where necessary terminate their BITs so as to bring their

[65] Article 2(1) TFEU.

[66] Article 46(1) Vienna Convention on the Law of Treaties (1969).

[67] See ECJ C-459/03, *Commission v. Ireland (Mox Plant)*, [2006] ECR I-4635, condemning Ireland for violating its duty of loyal co-operation and the Treaty's allocation of jurisdiction for certain disputes to the ECJ by having initiated proceedings under arbitration provision in the UN Convention for the Protection of the Marine Environment of the North-East Atlantic (1992) against the UK over their dispute on the MOX plant in Sellafield.

[68] Article 351(1) TFEU only refers to "agreements concluded before 1 January 1958"; numerous legal scholars argue for an analogous interpretation of the provision to fundamental changes in the Treaty, while others reject this as contrary to the clear wording, which could have been changed in the various modifications of the Treaty introducing new competences of the Union.

international obligations in line with European law and the transfer of powers to the Union that they accepted in the Treaty.[69]

(2) In the meanwhile – or rather during the continuing validity of the BITs under international law,[70] there remains some uncertainty about the enforceability of an award of damages to an investor against a member state on basis of the problematic BIT. This is because, in an extreme case, a member state paying an award could risk infringement procedures brought by the Commission. Moreover, courts in members states would be facing the dilemma of whether to breach the (external) obligation of the country under international law or accept the (internal) primacy of European law.[71] This could arise when a non-EU investor tries to enforce an arbitral award made against the member state in which the court is located (or another) EU member state.[72]

(3) Third countries, for the sake of gaining leverage in negotiations or escaping enforcement, could start questioning the continuing validity of their own obligations under the BITs vis-à-vis European investors. This is the 'very negative result' the Commission refers to in its Explanatory Memorandum to the proposed Regulation.

9.2 Legal uncertainty arising out of conflict with EU law unrelated to competence

Irrespective of the new allocation of exclusive competence to the Union, the BITs of the member states may contain provisions that are incompatible with EU Law. This has been highlighted by three recent judgments by the ECJ against Austria, Sweden and Finland.[73] These member states were found to be in breach of their obligations to re-negotiate certain BITs in order to bring them in line with the requirements of the Treaty. The Court found that the member states' BIT provision of an unconditional guarantee of the free transfer of capital was incompatible with the Treaty provisions authorising the Council to restrict the movement of capital to and from third countries in exceptional circumstances.[74] The three member states had to comply with the Commission's 2004 request to (re)negotiate additional

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[69] cf Article 4(3) TEU and *a fortiori* Article 351(2) TFEU; see ECJ, Case C-205/06, *Commission v Austria*, and Case 249/06, *Commission v Sweden*, [2009] ECR I-1301 and I-1335; also AG Poiares Maduro in these cases [2009] ECR I-1301, ¶ 33.

[70] Virtually all BITs contain final clauses providing for their continuing protection of past investments for periods between 10 and 20 years after their termination.

[71] The relation of primacy between EU law and international law is not clear in this respect. Clear is only that international law trumps secondary EU, cf. ECJ Case C-61/94, *Commission v. Germany (Milk Products)*, [1996] ECR I-3989 ¶ 52. The situation of the BITs could, however, be understood as a problem of primary EU law, as Article 2(1) TFEU on the effects of the EU's exclusive competence is concerned.

[72] cf. Article 54(1) ICSID Convention (1965), which establishes an unconditional obligation to enforce ICSID awards. For non-ICSID awards, Member State courts could – and might have to – refuse enforcement on the basis of Article V(2)(b) of the UN Convention on Recognition and Enforcement of Foreign Arbitral Awards of 1958 ("New York Convention"), which allows refusal in case of violation of public policy. If enforcement is sought in the country condemned to pay in arbitration, however, such a refusal nevertheless constitutes a violation of the country's international treaty obligation to pay the award. Enforcement against assets of the condemned Member State in third countries would remain possible as their courts have no obligation to uphold European state aid law.

[73] ECJ Cases C-205/06 and 269/06, see above n. 69, and ECJ Case C-118/07, *Commission v. Finland*, [2009] ECR I-0000.

[74] Now Articles 64(2) [primarily as a measure to ensure reciprocity of treatment of financial operators in third countries as defined in a number of directives]; Article 66 [in case of serious difficulties for the operation of the economic and monetary union]; and Article 75 TFEU [to allow the freezing of funds, financial assets or economic gains relating to terrorist or similar activities].

clauses clarifying that their implementation of restrictions imposed by the Council would not constitute a breach of their international obligations to foreign investors.[75]

The worries about the incompatibility of BIT provisions and the Council's power to impose restrictions on the free movement of capital had already led the Commission to negotiate, in 2003, a Memorandum of Understanding (MoU) with the United States regarding eight of the accession states,[76] whose BITs with the U.S. also contained unqualified capital transfer clauses.[77] The same MoU also included an invitation to the parties to take note of the circumstance that companies established in the EU but owned or controlled by third country nationals (typical investment vehicles) could, like any other EU company, be subject to different treatment regarding the freedom of establishment and the freedom to provide services for reasons of public policy, public security or public health.[78] This clarification was aimed at preventing investors from obtaining awards for damages against member states. The concern was that investors could argue that by applying EU directives co-coordinating the legal framework for special treatment of foreign nationals, the accession states would violate BIT provisions guaranteeing national or most-favoured-nation (MFN) treatment.[79] This suggests that *all* European acts implementing or allowing restrictions on *any* economic freedoms (goods, workers, services, establishment, and capital) of the common market could potentially be attacked by foreign investors in investment tribunals.

The MoU with the U.S. also addressed the prohibition of performance requirements in some member state BITs that could conflict with EU quotas for certain agricultural products or the "European content" in television broadcasting.[80] These EU provisions could also possibly have allowed investors from third countries to seek damages against a member states in investment arbitration. The same problem applies to EU procurement rules that require supplies and materials purchased with EU special funds to originate the supplies from the EU,[81] as well as for EU rules requiring a carrier seeking permission for

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[75] For such a re-negotiated clause see the Protocol of 26 August 2009 to the French-Turkish BIT of 15 June 2006: "The provisions of [Article 5 on the free transfer of capital] do not hinder the exercise in good faith by one Contracting Party of its international obligations as well as its right and obligations resulting from its participation or association in a free trade zone, a customs union, a common market, an economic and monetary union or any other form of regional co-operation or integration."

[76] Press release by the Delegation of the European Union to the USA, EU/NR 59/03 of 23 September 2003.

[77] It is worth noting that the Commission reached an agreement with the U.S. regarding the two Treaty provisions allowing restrictions relating to the safeguard of reciprocal treatment of European financial operators abroad as well as to take action against terrorist or related activity, but not regarding the provision allowing restrictions relating serious difficulties for the operation of the European economic and monetary union (see above n. 77), presumably because of the losses suffered by U.S. investors resulting from the economic and monetary turbulences in Argentina leading to its default in early 2002 (and triggering the biggest wave of BIT claims against a one country in the history).

[78] Now Article 52(2) TFEU. For the MoU on this point see Anca Radu, "Foreign Investors in the EU – Which 'Best Treatment'? Interactions between Bilateral Investment Treaties and EU Law", (2008) 14 European Law Journal 237, 245.

[79] A typical clause reads: "Each Contracting Party shall accord investments of investors from the other Contracting Party, including their operation, management, maintenance, use, enjoyment or disposal by such investors, treatment which shall be no less favourable than that accorded to its [own] investors, or the most favourable treatment accorded to investments of investors of any third countries, whichever is most favourable." (Article 5(1) of the Agreement between India and France on the Reciprocal Promotion and Protection of Investments of 2 September 1997).

[80] cf. Article 4 of Council Directive 89/552/EEC of 3 October 1989, [1989] OJ L298/23.

[81] Article 5 of Regulation (EC) 2110/2005 of the European Parliament and the Council of 14 December 2005, [2005] OJ L433/1.

inland waterway transport to use only vessels owned and controlled by member state nationals.[82] The MOU therefore excluded sensitive sectors from the obligation to grant foreign investors the same rights as national investors. The sectors concerned included areas of agriculture, audio-visual, securities, investment and other financial services, fisheries, hydrocarbons, subsidies and transport (air carriers, inland waterways and maritime). These exceptions are understood to reflect the parties' agreement on the need for "policy space in strategic issues."[83]

A series of ongoing or very recently concluded investment cases provides yet another example of potential conflict between BITs and EU law. These cases relate to financial privileges (subsidies) granted by Hungary and Romania to foreign investors prior to their accession and terminated so as to conform to EU State Aid rules.[84] The foreign investors initiated arbitration procedures to claim damages (totaling more than € 800 million) for the termination of the benefits with the argument that this revocation violated their rights under the respective BITs ratified by Hungary and Romania.[85] An arbitral tribunal finding that one of the member states had to pay damages irrespective of its obligations under Article 108 TFEU on state aid, would mean maintaining a subsidy that distorted competition within the single market and was illegal under European law. Payment of an award of damages by the member state for breach of the BIT would thus in itself constitute a breach of the Treaty and the Commission would be obliged to initiate proceedings before the ECJ to order the member state not to pay out. If the member state refused to pay such an award, any court within the European Community would face the dilemma, as discussed above, of having to breach international law or uphold the supremacy of Union law.[86]

Another argument pointing a possible incompatibility of existing BITs and EU law has been repeatedly voiced by some smaller member states, who feel they do not have sufficient negotiating clout to get protection for their investors abroad equivalent to that of the bigger member states. The argument is that this distorts competition among European investors within the EU, since as discussed in part I FDI can enhance the competitiveness of companies. This argument is more telling when the small member state has no BIT at all with a given third country, because if such a small member state has a BIT, however weak, MFN may provide a level playing field with other EU outward investors. If investors in the smaller state have no recourse to MFN treatment the BIT of the larger member state could then be seen as a kind of "state aid"[87] distorting competition on the European market.[88]

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[82] Article 2(1) Council Regulation (EEC) 3921/91 of 16 December 1991, [1991] OJ L373/91.

[83] Radu (above n. 78) at 252.

[84] *Micula v Romania*, ICSID Case No. ARB/05/20 (claimant requests reinstatement of the legal framework prior to the revocation of certain financial incentives to invest in disfavoured regions or alternative € 450 million in damages); *Electrabel S.A. v Hungary*, ICSID Case No. ARB/07/19; *AES Sumnit Generation Ltd and AES-Tisza Erőmű Kft v Hungary*, ICSID Case No. ARB/07/22; *EDF International S.A. v Hungary* (ad hoc arbitration under UNCITRAL Rules) (all three relating to the termination of long-term power purchase agreements providing for benefits which were probably incompatible with EU state aid rules; the Claimants see the revocations as violations of the prohibition to impair investments by unreasonable or discriminatory measures under the Energy Charter Treaty).

[85] The BITs in question are with other European countries, thus aggravating the problem, but the fundamental question of collision with EU law would be no different the BITs were concluded with third countries.

[86] See above n. 72.

[87] It should be noted that BITs, although conferring a benefit by securing property rights abroad, technically cannot qualify as state aid prohibited by Article 107(1) TFEU since the benefit does not favour "certain undertakings or the production of certain goods" but is granted generally to all investors irrespective of the sector they operate in.

[88] From a practical point of view, however, investors whose home country has no BIT with the targeted host state can frequently circumvent this problem by setting up an intermediate company in a country that does

Finally, a potential for conflict arises when investors have recourse to an international arbitral tribunal and are not limited to litigation before the courts of the host state. Member state BITs have to contain special clauses exempting third country investors from benefits and privileges (such as national treatment or MFN) conferred under EU law[89] or exempting restrictions to capital movements under EU law from the BIT provisions guaranteeing free transfer.[90] These specific exemptions, however, usually do not cover other standards such as fair and equitable treatment, full protection and security or full compensation for expropriation. This means that investors can, in principle, use BIT arbitral proceedings to challenge any change in European legislation or regulatory action that affects their investment. In principle and if construed properly, BIT standards should not afford any more protection than the European standards as elaborated by the ECJ and now enshrined in the Charter of Fundamental Rights, which are certainly among the most protective standards against state interference in economic activities. A problem arises, however, from the extreme vagueness of the BIT provisions, the absence of any binding and consistent case law as well the lack of any central instance that could guarantee the uniform interpretation and application of the law. This means that member states may have to pay large damages awarded by arbitrators who owe no allegiance to any constitution or constitutional treaty other than the BIT itself.[91] As shown by the numerous cases brought against Argentina discussed in part I, arbitral tribunals can disagree with the host government's assessment of necessity and fairness in an economic emergency. This could lead to damages being awarded that would not have been awarded even by the investor's home courts in similar circumstances.

Could fear of violating BIT standards result in regulatory chill in the EU? Part I suggests that such fears in other countries have, to date, not been well founded. Nevertheless there may remain scope for international arbitrators to interpret and apply European law. But such arbitrators are not entitled[92] to request a preliminary ruling from the ECJ and their awards cannot be reviewed be the ECJ to ensure the necessary uniformity and the rule of law as required by the Treaty.[93]

The ECJ cases cited above show that legal uncertainty existed regardless of the entry into force of the Lisbon Treaty. The cases also show that some conflicts are more direct than others. Compare for example, the Council's powers to restrict transfers (a conflict arising *specifically* from the different content of EU law and the BIT provisions) with the potential incompatibility resulting from the interpretation of general "fair and equitable treatment" (a problem arising *generally* from the lack of

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and whose BIT merely uses the place of incorporation (rather than nationality of the owner) as the criterion (such as especially the Netherlands and the UK) for the sake of "shopping" the BIT protection.

[89] See, e.g. Article 7(a) of the UK-Argentina BIT of 11 December 1990; Article 4(2) of the Germany-India BIT of 10 July 1995; Article 3(4) France-Turkey BIT of 26 August 2009. These clauses are often referred to as Regional Economic Integration Organisation (REIO) clauses.

[90] See above n. 75.

[91] See, e.g. CME *Czech Republic BV v Czech Republic* (Damages) (14 March 2003) 15(4) World Trade and Arbitration Material 83, where the Czech Republic was condemned US$ 353 million for issuing regulatory advice (not involving EU law) that lead CME, a Dutch investment vehicle of Ralf Lauder, a U.S. cosmetics billionaire, to divest itself of a popular TV station, despite the fact that another tribunal under the Czech-U.S. BIT had six months earlier found that the conduct of the Czech broadcast authority constituted no violation of any investment protection standards. The amount awarded corresponded roughly to the Czech Republic's annual health care budget and, adjusted for population size and gross national income, was equivalent to an award of US$ 26 billion against Germany; see separate opinion by Ian Brownlie, *ibid*. at 245 ¶ 80.

[92] ECJ Case 102/81, *Nordsee Deutsche Hochseefischerei* [1982] ECR 1095 ¶¶ 10 to 12, and Case C-126/97 *Eco Swiss* [1999] ECR I-3055 ¶ 34: an arbitral tribunal is not a "court or tribunal of a Member State" in the sense of Article 267 TFEU.

[93] Article 19 TEU.

review of arbitral awards under BITs and the exclusion of the ECJ's jurisdiction). It is still unclear to what degree the Commission will feel obliged to request amendments of BITs. Given the number of BITs it will clearly only be able to do so when it is really necessary, but the fact that the Commission is increasingly seeking to appear as an *amicus curiae* in arbitration to defend EU interests shows concern about potential incompatibilities.

9.3 The overlap between member state BITs with third countries and the emergence of a new EU common investment policy

Even prior to the entry into force of the Lisbon Treaty, the EU had already negotiated so called mixed agreements with third countries that covered elements of foreign investment, such as the Free Trade Agreements (FTA) with Chile (2002),[94] the EPA with Cariforum (2008),[95] and South Korea. There are also presently plans for further FTAs. To date EU FTAs have primarily concerned liberalization/pre-establishment, but the introduction of comprehensive agreements covering pre and post establishment could create legal uncertainty if it is not clear whether these EU agreements take precedence over the member state BITs where their provisions overlap.[96]

One specific example of overlap and incompatibility is the provision in the EU-Chile FTA. This allows the contracting parties in case of "serious balance of payments and external financial difficulties" to adopt "restrictive measures with regard to trade in goods and in services and with regard to payment and capital movement, including those related to direct investments."[97] BITs concluded by member states with Chile, however, contain unqualified guarantees of free transfer of capital. If investors could challenge restrictions allowed by the FTA by invoking the BIT provision, this would undermine the overall balance of the FTA and could also raise questions of equal treatment for investors in Chile from Ireland or Slovakia, whose home countries have no BIT with Chile.

It has been suggested that there is also some potential overlap between member state BITs and the WTO Agreements to which the EU is a party, such as especially the General Agreement on Trade in Services (GATS) and the Agreement on Trade-Related Investment Measures (TRIMS). It is, however, widely recognized that BITs are, in general, compatible with these agreements.

The problem of potential overlap and incompatibility between existing BITs and EU agreements will be aggravated to the degree that the EU uses its powers to negotiate its own investment treaties or agreements containing investment protection chapters or provisions. If – which should be the rule – these agreements are negotiated and concluded as mixed agreements, most problems can be avoided by including explicit provision on the precedence of the EU agreement in the event of any incompatibility. If exclusive EU competence for FDI were to be interpreted such as to allow the Union to negotiate, on the basis of a qualified majority decision in the Council, a "pure" EU agreement without the Member States, the member states that opposed such negotiations because of the consequences for their respective BIT would be obliged to co-operate (duty of loyal cooperation) and thus to re-negotiate or terminate their BIT.[98] Such 'pure' EU agreements are however, unlikely to be the norm.

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[94] [2002] OJ L 352/3.
[95] [2008] OJ L 289/1/3.
[96] As a matter of international law (the Vienna Convention on the Law of Treaties (1969), the Member State BITs remain in force since they do not cover exactly the same subject matter as the EU agreements (cf. Article 59), but their provision are not be applicable anymore to the degree that they are incompatible with the later EU agreement with the same third country, to which all Member States are also a party (cf. Article 30(3)).
[97] Article 195 EU-Chile FTA.
[98] Article 4(3) TEU and Article 351(2) TFEU.

Finally, existing BITs could constitute "an obstacle to the development and implementation of the Union's policies relating to investment", as noted in the Commission's Explanatory Memorandum to the proposed Regulation. This is where the existence of agreement(s) undermines the willingness of a third country to negotiate with the Union.[99] Indeed, third countries (or member states) that have BITs might find it advantageous keep the existing BITs. To take one example, the existing BIT might be preferred to an EU investment agreement that included provisions on labour or environmental policy. In view of the EU's exclusive competence, it would then seem necessary to allow the EU to eliminate such obstacles to its negotiations. But renegotiation has a major potential of creating legal uncertainty.

10 ANALYSIS OF THE PROPOSED SOLUTIONS

There are thus two challenges facing the EU during the transition from member state BITs to EU (mixed) agreements with third countries: to ensure the continued effectiveness of the existing protection for investors (both inward and outward); and to ensure the conformity of the existing BITs with EU law, other EU international agreements and EU policies relating to foreign investments.

10.1 Ensuring the continuing effectiveness of Member State BITs

10.1.1 The necessity to empower the member states to maintain their BITs

The Treaty of Lisbon is silent on the transition from national BITs to the full implementation of EU investment agreements. It does not address the issue of the continued validity of member state BITs or specify deadlines for their replacement. As discussed above, it is far from clear that the general provision in the TFEU ensuring the continuing validity of agreements concluded by member states with third countries before 1958 can be applied in an analogous way to fundamental modifications of the allocation of competences in the updated Treaty.[100] The solution is provided in the general provision of the Treaty defining the consequences of an exclusive competence of the Union according to which member states can be empowered by the Union to adopt – and thus also to keep – legally binding acts in an area of exclusive competence.[101] This solution has been used by the Commission in its draft Regulation in Article 3:

> "Notwithstanding the Union's competence relating to investment and without prejudice to other obligations of member states under the law of the Union, member states are authorised in accordance with Article 2(1) of the Treaty to maintain in force bilateral agreements relating to investment that have been notified in accordance with Article 2 of this Regulation."

By adopting the draft Regulation in the ordinary legislative procedure,[102] the European Parliament and the Council would, for the Union, empower the member states retain their BITs and thus eliminate any incompatibility resulting from the transfer of exclusive powers to the Union. There would appear to be no real alternative to this procedure, given the far reaching legal uncertainty resulting from the present situation.

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[99] Explanatory Memorandum, p. 5.

[100] For Article 351(1) TFEU see above n. 68.

[101] Article 2(1) TFEU; see above n. 65.

[102] Articles 207(2), 289, 294 TFEU.

10.1.2 Is a Regulation the right instrument to authorise existing BITs?

It is questionable that a *regulation* is needed for the authorization of existing BITs. The Treaty defines the different legal acts the European institutions may adopt when exercising the Union's competences and specifies that a regulation "shall have general application". Despite its broader "general" consequences for the stakeholders, the authorisation of member state BITs is focused on fixing specific legal consequences for a defined group of addressees regarding a definite number of national instruments.[103] This suggests that the authorisation is, *a priori*, a form of *decision*, for which the Treaty merely provides that it "is binding in its entirety" and that, if it specifies the addressees, it shall be binding on only on them.[104] However, it has to be taken into consideration that the Union's act of empowering members states to adopt – and keep – legally binding acts is the equivalent to the exercise of the power by the Union itself. By empowering the member states to set rules in an area of exclusive competence, the Union's authorisation ultimately provides legal force for national acts and therefore could be seen as legisaltion. This suggests that the procedures for the adoption of the authorisation should follow the legislative procedure specified for the CCP in the treaty. This is the "European Parliament and the Council, acting by means of regulations in accordance with the ordinary legislative procedure, … adopt(ing) the measures defining the framework for implementing the common commercial policy".[105] But it is doubtful that authorisation of a BIT would qualify as a "measure defining the framework for implementing that he common commercial policy". Authorisation of a BIT implements one aspect of the CCP, so it would be more suitable to use a decision adopted jointly by the European Parliament and the Council in the ordinary legislative procedure to authorize member state BITs.[106] It would, however, still be possible to include the (decision-like and specifically addressed) authorisation as a part of a regulation that has "general application" and that more broadly and genuinely "defines the framework for implementing the common commercial policy" – which is what the Commission proposal purports to do.

10.2 Ensuring the general conformity of Member State BITs with EU laws and policies

The Commission proposes that it should monitor the member state BITs and remedy any incompatibilities with EU law or policy. According to the Commission's Explanatory Memorandum to the draft Regulation, failure to authorise all member state BITs would result in a lack of legal certainty. "The extent to which investment agreements of member states are incompatible with EU law can be subject to discussion. The Commission is of the view that *any* legal uncertainty on the status and validity of these agreements ... is to be avoided [by the adoption of the Regulation] ... [T]he impact of inaction is considered to be much higher than the impact of this action, which is neutral given that it preserves the status quo."[107] As the analysis above showed the status quo is far from satisfactory. But is it not clear that the proposed Regulation would greatly improve the lack of legal certainly over the status quo. Legal certainty for the estimated 1200 BITs' compatibility with EU laws and policies cannot be brought about instantly or even reasonably quickly. Even if member states were to terminate all their BITs in the near future virtually all BITs contain clauses that provide for their continuation in force for 10-20 years after their termination.

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[103] cf ECJ Case C-3/00
[104] Article 288(4) TFEU.
[105] Article 207(2) TFEU.
[106] cf. Article 289(1) TFEU, which specifies that also decisions can be jointly adopted.
[107] Explanatory Memorandum, p. 3; emphasis in original.

10.2.1 Summary of the compliance procedure proposed by the Commission

The draft Regulation would require all ember states to notify their existing BITs so as to allow the Commission to review them, "including by assessing, in particular, whether the agreements: (a) conflict with the law of the Union other than the incompatibilities arising from the allocation of competences between the Union and its Member States, or (b) overlap, in part or in full, with an agreement of the Union in force with that third country..., or (c) constitute an obstacle to the development and the implementation of the Union's policies relating to investments..."[108]

Only BITs notified by the member states would be covered by the global authorisation of member states' BITs. Notified and thus authorised BITs are to be put on a list to be published by the Commission on a regular basis. If the Commission finds that a member state BIT conflicts with EU law, it shall deliver a reasoned opinion on the necessary steps to be taken by the member state. If consultations between the Commission and the member state concerned fail to resolve the matter, the Commission shall withdraw the authorisation of the agreement concerned after having taken "utmost account" of the opinion of an advisory committee composed of representatives of the member states and having informed the European Parliament.[109] A Commission's decision to withdraw authorisation would result in the BIT being removed for the list published by the Commission. [110] With no empowerment by the Union, the BIT would no longer constitute a "legally binding act" under EU law, despite its continuing validity under international law.[111]

In order to allow the member states to get their BITs back into line with the Commission's position[112] other than by terminating them, the Regulation would provide for a mechanism by which the member states would have to notify their intention and seek authorisation from the Commission to negotiate amendments.[113] This mechanism of authorisation would also be available to member states who want to negotiate new BITs with third countries during the transitional period, i.e. until the EU has taken up its own negotiations with those third countries.[114] In either scenario, the Commission would have to refuse authorisation if it concluded that the negotiations planned for a member state BIT conflict with EU law or with ongoing EU negotiations. Alternatively the Commission could require the member state to neutralise any potential conflict.[115] If the Commission authorises the negotiations, it must be kept

[108] Articles 3 and 5(1) draft Regulation.

[109] Articles 6(3) and 15 draft Regulation, read in conjunction with Articles 3 and 7(2) of Council Decision 1999/468/EC of 28 June 1999, [1999] OJ L 184/23.

[110] Two accessory consequences would be that the Commission could immediately initiate infringement proceedings against the Member State before the ECJ since the required procedural step of requesting the Member State to comply with Commission's reasoned opinion would already have been taken (see Article 6(2) draft Regulation) and that the Member State would have the possibility to challenge the Commission's decision before the ECJ, especially if it considers that the Commission erred in its assessment of the incompatibility of the BIT provisions (Article 263 TFEU) and request the ECJ to order the Commission to abstain from striking the BIT from the list until the ECJ has decided on the matter (Article 279 TFEU).

[111] Article 6(4) draft Regulation.

[112] Which might have to be confirmed by the ECJ if challenged.

[113] Articles 7 and 8 draft Regulation.

[114] This mechanism has largely been copied from Council Regulations No. 662/2009 and 664/2009 of 13 July, [2009] OJ L 200/25 and 46 on the procedure for Member States to negotiate agreements with third countries concerning certain conflict of laws and conflict of jurisdiction matters, which had become a (non-exclusive) EC competence with the entry into force of the Treaty of Amsterdam in 1999.

[115] Article 9(1) and (2) draft Regulation.

informed of the progress and results and may ask to participate in the negotiations.[116] Before signing and concluding the amendment or the new BIT, the member state must again obtain authorisation from the Commission. In taking any decisions the Commission must take into account the opinion of the advisory committee.[117] The member state finally has to notify the conclusion and the entry into force of the amended or the new agreement.[118] This final notification would be equivalent to the notification of an existing BIT and should thus lead to the automatic authorization. [119] But the BIT would still be scrutinized by the Commission to ensure it does not impede the evolution of EU policy, such as in negotiating an EU agreement with the third country concerned.

The proposed Regulation would secure for the Commission an important role in any dispute settlement proceedings activated under any BIT "falling within the scope of this Regulation",[120] i.e. including un-notified or de-authorised BITs. If a dispute procedure is initiated against a Member State it would have to inform the Commission immediately. In either case, the Member State would have to take all necessary steps to ensure that the Commission can participate in the procedure.

10.2.2 Evaluation of the proposed procedure

The publication of the list of notified BITs is the main means of ensuring legal certainty. Notified BITs are automatically authorised and remain in force under EU law. There are however some ambiguities resulting from this approach. For example, if the Commission finds that a BIT "constitute[s] an obstacle to development and the implementation of the Union's policies relating to investment" the BIT will be taken off the list. Investor rights will, however, not be affected because as noted above the protection afforded by a BIT will continue in force for typically 15-20 years. If the member state does not terminate the BIT, but authorisation is revoked because the BIT is an obstacle to EU investment policies, the result would not be much different. Under international law the BIT obligations would continue to be valid and, absent any direct conflict with EU law, member states or their courts would be obliged to uphold the obligations. Put another way, the BIT would most probably continue to provide effective protection; legal uncertainty is suggested whether there should be none.

Insofar as the Commission finds a BIT to conflict with the law of the Union, this incompatibility can be expected to be only limited to individual - or a select few - provisions.[121] Because of the principle of proportionality,[122] the Commission could, in such a case, just request the member state to negotiate a specific amendment to remedy the position. In such a case, the general authorisation of the BIT remains valid so long as the member state acts on the Commission's report and starts negotiating an amendment. The BIT remains on the list; the incompatibility with EU law, however, remains, together with potential doubts as to the full and effective protection afforded under the BIT. Legal certainty is suggested where it is actually doubtful. On the other hand, if the member state does not act to negotiate a remedy the incompatibility, the authorisation is withdrawn, the BIT is taken off the Commission's list. The problem with the BIT is not only highlighted, but accentuated. With the withdrawal of the authorisation, the problem is no longer limited to the original specific incompatibility of specific provisions. The loss of authorisation would suggest that *all* provisions of the BIT falling within

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[116] Article 10 draft Regulation.
[117] Articles 9(3), 11(6) and 15 draft Regulation.
[118] Article 11(7) draft Regulation.
[119] Articles 3 and 4 draft Regulation.
[120] Article 13 draft Regulation.
[121] Most BITs of Member States follows their own models, which are themselves rather similar due to the standard practice co-ordinated in the OECD.
[122] Article 5(4) TEU.

the EU's exclusive competence are deprived of their quality of "legally binding acts" within the EU. Significant legal uncertainty is suggested and actually created where the uncertainty was originally rather limited in scope.

It could therefore be argued that the list mechanism primarily uses the element of legal uncertainty to put pressure on the member states to comply with the Commission's requests for modification or termination rather than hedging against the effects of existing legal uncertainty.

10.2.3 Evaluation of proposed criteria for review and withdrawal of authorisation and the role of the Commission

The criteria for reviewing notified BITs are essentially: (i) conflict with the law of the Union; (ii) overlap with Union agreements with third countries; and (iii) obstruction of the development and implementation of the Union's policies relating to investment.

(i) Conflict with EU law

As shown by the recent ECJ cases, conflict with the law of the Union is a source of legal uncertainty. Given the breadth and the varying degrees and intensities of the different potential incompatibilities, one question arising from the proposal is just where the Commission – always controlled by the ECJ – will set the threshold for intervention. The wording suggests that every actual conflict between a BIT and EU law will allow the withdrawal of authorisation.[123] The ECJ has accepted that Member State guarantees of unconditional free transfer is, itself, sufficient to imperil the Council's right (and also obligation) to restrict transfers in future exceptional circumstance, even if such circumstances may never actually arise.[124] This suggests a rather broad understanding of what constitutes an actual conflict with EU law. On the other hand, it seems quite clear that the potential (and for a member state very damaging) conflict resulting from an investor-friendly interpretation of vague BIT standards of protection will not suffice. Such a conflict may result from international tribunals' manifest disregard of EU law designed to govern the situation (such as the EU state aid regime), coupled with the exclusion of the jurisdiction of member state courts and European courts through the arbitration mechanism. This type of conflict, however, does not derive from the specific content of individual BIT provisions. Rather, it derives from the general weakness of the investment treaty and arbitration system. The vagueness of substantive BIT provisions coupled with the peculiarities and risks of the dispute settlement process would not, in itself, be sufficient to withdraw the authorisation – let alone because it would probably concern all +1200 Member State BITs. The same issue could be relevant for future EU policy on foreign investment and come into play if the EU attempts – as hinted in the Commission's Communication – to negotiate BITs that might have more detailed and restrictive provisions (e.g. on the definition of fair and equitable treatment),[125] as well as more sophisticated procedural mechanisms for dispute settlement (such as appellate bodies, maybe with the possibility of preliminary rulings).[126] See discussion in part I of the study above. According to the proposed Regulation the Commission must give a reasoned opinion on whether a BIT provision conflicts with EU law thus justifying the withdrawal of authorisation. The latter is an act that can be challenged by the member state concerned so that the ECJ would have the final say in this matter.[127]

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[123] Article 6 (1)(a): "... where an agreement conflicts...".
[124] See the cases discussed above at n. 73.
[125] Cf. Commission Communication, p. 8-9.
[126] Cf. Commission Communication, p. 10.
[127] Article 263 TFEU.

(ii) Overlap with the EU's international agreements with third countries

More or less the same holds for the criterion of overlap with EU agreements with third countries. There is an obvious need for the primacy of comprehensive EU agreements, especially where negotiated and concluded together with the member states. If a member state challenges a decision to withdraw authorisation any dispute over whether there is overlap would eventually have to be settled by the ECJ following legal analysis of the scope of the respective provisions. So again the ECJ would eventually have the final say.

(iii) Obstacles to the development and implementation of EU policies

The question is far more complicated when it comes to the evaluation whether a BIT constitutes an obstacle to EU policies on investment. The primary problem is to define what should constitute the benchmark for determining what these policies actually are at any given time – bearing in mind that the definition of these policies is, under the proposal, necessary to assess whether the authorisation of a BIT can be withdrawn or not.

It is doubtful that the Communication of the Commission "Towards a comprehensive European international investment policy"[128] accompanying the draft Regulation, or any future Commission white paper could, in itself, be taken as the benchmark for defining the Union's policies in this field. This would mean granting the Commission itself the possibility of defining in a simple soft law instrument when it could withdraw authorisation. Put another way, the Commission would have unfettered discretion as to when it finds it expedient to withdraw an authorisation, and ultimately to force member states to terminate their BITs. member states' possibilities of challenging such a decision would be extremely limited as the ECJ could only review whether the Commission properly exercised its very broad discretion.

On the other hand, one could say there is a clear Union policy when the Council formally adopts a mandate for the EU to negotiate and authorises the opening of negotiations with a third country covering international investment.[129] The Commission has right of initiative but all such mandates are agreed by the Council, which can also address negotiation directives to the Commission.[130] Such a formal mandate could then constitute a clear source of EU policy against which the ECJ could review the Commission's assessment that a BIT constitutes an obstacle. Limiting the definition of EU policy to specific negotiation mandates, however, would also be problematic. Individual negotiations may not always reflect a model EU BIT and the EU has in the past been flexible and accommodated its negotiating partner's interests when negotiating FTAs. Moreover, there is an institutional problem with limiting the definition of the Union's power to the Council.[131] The member states, united in the Council, might be wary of abandoning their existing BITs. Hindered politically from rejecting the Commission's recommendations to open negotiations outright, the Council could simply block the development of the policies recommended by the Commission by not taking any decision. This inactivity would mean

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[128] COM(2010) 343 final.

[129] ECJ Case C-266, Commission v. Luxemburg, [2005] ECR I-4805 ¶ 60; C-246/07, Commission v Sweden (PFOS), [2010] ECR I-0000 ¶ 74: "adoption of a decision authorising the Commission to negotiate a multilateral agreement on behalf of the Community marks the start of a concerted Community action at international level."

[130] Article 218(2)-(4) TFEU. The Parliament's formal powers are limited to granting consent to the final agreement, rather than the mandate for negotiations.

[131] This problem also applies to the scenario of the ECJ Case C-266 (above n. 129), where the Court at ¶¶ 76-91 found a "concerted strategy" of the Commission and the Council, where the latter did not propose in its recommendation, and the latter hence did not include in its decision, the inclusion of a chemical substance in an exemptions list under the Stockholm Convention on Persistent Organic Pollutants.

that the global authorisation of existing BITs would allow the erosion the Union's exclusive competence for foreign direct investment – if it is ultimately to be interpreted as covering also the protection of investment[132] – and, de facto, reduce it to a merely concurrent competence. This would contradict the Treaty.

This problem is addressed in the Commission proposal that it has the power to withdraw the authorisation.[133] The draft Regulation provides that the Commission can withdraw authorisation where "the Council has not taken a decision on the authorisation to open negotiations on an agreement which overlaps, in part or in full, with an agreement notified [by a member state], within one year of the submission of a recommendation by the Commission pursuant to Article 218(3) of the Treaty."[134] This makes clear that the Commission wants to have the ability to oblige member states to authorise EU negotiations by retaining the power to deprive them of their own BITs. This may be considered an attempt to arrogate additional powers to the detriment of the member states. It is, however, consistent with the EU Treaty's definition of the obligations of the Commission, which are to "promote the general interest of the Union" and to "ensure the application of the Treaties",[135] and thus arguably a necessary institutional safeguard to ensure the transfer of the competence for investment from the member states to the Union.[136]

10.2.4 Evaluation of the EU's role in dispute settlement proceedings

All member state BIT dispute settlement procedures are designed to provide effectiveness in determining the rights and obligations arising under the BIT. The generalized arbitration procedure provided for in virtually all BITs de facto excludes the jurisdiction of the Member State courts and the European courts. Disputes involving matters in which Union laws and policies may have a keen interest are thus in the hands of arbitrators, who are not necessarily under an obligation to give due consideration to those Union interests. It is therefore understandable that the Commission has in the past requested to be heard as an *amicus curiae*, i.e. as a non-party in investment disputes touching upon Union interests. In the proposed Regulation the Commission stresses the need for it participate in BIT dispute procedures and seeks a commitment from Member States to take all necessary measures to ensure, where appropriate, "that the Commission participates in the procedure." It is, however, unclear how such an obligation to co-operation would be different from the current situation.

First, as discussed in part I, most member state BITs provisions on dispute settlement refer to the arbitration procedure of the International Centre for the Settlement of Investment Disputes (ICSID). ICSID rules are contained in the World Bank's ICSID Convention (1965), to which the European Union, as a supranational organisation, cannot be a party since its signature is only open to "states".[137] Second, because of the privacy of arbitral proceedings, member states could do little more than to seek the investor's agreement or, where the rules so provide, to support the Commission's petition to be granted

[132] Otherwise, the whole point of defining a Union policy on this point would be moot for lack of competence.
[133] Article 6(3) draft Regulation.
[134] Article 6(1)(d) draft Regulation.
[135] Article 17(1) TEU.
[136] In the context of the Commission's powers it is worth mentioning that Article 6(3) draft Regulation, in its third sentence seems to suggest that the Commission (or its decision) shall not only include a requirement that the Member State takes appropriate action, but also "it" (the Commission or its decision) shall, where necessary, "terminate the relevant agreement." This would, of course, be impossible under international law, which suggests that there is a "s" missing after the word "terminate<u>s</u>" so as to mean that the Member State shall, where necessary, terminate the agreement.
[137] Article 67 ICSID Convention.

the status of *amicus curiae* in order to allow the Commission to submit observations in writing and to attend hearings. An investor can simply refuse such a petition leaving the tribunal unable to admit the Commission under the ICSID Rules.[138] The right to submit written observations can be granted by the tribunal on a discretionary basis.[139] As one tribunal observed: "What is not expected, however, is that the Petitioners will not (a) simply consider themselves as in the same position as either party's lawyers, or (b) will see their role as suggesting to the Arbitral Tribunal how issues of fact or law as presented by the parties ought to be determined (which is the sole mandate of the Arbitral Tribunal itself)."[140] Furthermore, the tribunal also has the discretion to order the confidentiality of arbitral proceedings as well as of the documents produced therein.[141] Contrary to what the draft Regulation suggests,[142] such an order of confidentiality would bar a member states from informing the Commission of the content of the proceedings or providing documents.[143] A breach of the obligation of confidentiality could have serious repercussions for the procedural position of the member state concerned. Again, the member state could do little more than support the Commission's petition for an exemption from such an order of confidentiality, which could again simply be denied by the tribunal on a discretionary basis.[144]

To address these procedural obstacles Commission could request member states to negotiate amendments of their BITs so as to allow the Commissions participation in proceedings. The adoption of the draft Regulation would strengthen the Commission's claim to represent the Union interests in this way.

10.2.5 Evaluation of the participation of other institutions in the decision making

The draft Regulation provides for the creation of an "Advisory Committee for the Management of Transitional Arrangements on International Investment Agreement" composed of representatives of the member states and chaired by a representative of the Commission.[145] According to its draft, the Commission would have to "take the utmost account of the opinion delivered by the committee" for any decision implementing the transitional measures. [146] It is worth noting that the Commission is proposing the establishment of an advisory rather than a management or regulatory committee.[147] Either of the latter two would give the Council more power.[148] Again the Commission's intention here seems to be to avoid giving a member state (or member states) the ability to frustrate the development of EU policy in investment.

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[138] Rule 32(2) ICSID Arbitration Rules (effective from 2006).
[139] Rule 37(2) ICSID Arbitration Rules (effective from 2006).
[140] Procedural Order No. 5 of 2 February 2007 in ICSID Case No. ARB/05/22, p. 19-20,
[141] Cf. Rule 39(1) ICSID Arbitration Rules allowing the Tribunal to "recommend" provisional measures for the preservation of the rights of the requesting party.
[142] Article 14 draft Regulation.
[143] This problem was also at the origin of the Commission initiating proceedings against Ireland in the MOX plant case (see above n. 67) at ¶ 54: Ireland refused the Commission's request for information on the arbitration proceedings that Ireland had brought against the UK because of its obligation of confidentiality, which the Commission qualified as a breach of Ireland's obligation to co-operate.
[144] Cf. Procedural Order No. 5 of 2 February 2007 in ICSID Case No. ARB/05/22, p. 20.
[145] Article 15(1) draft Regulation, read together with Article 4(1) of Council Decision 1999/468/EC of 28 June 1999, [1999] OJ L 184/23.
[146] Articles 9(3) and 11(6) draft Regulation.
[147] These would become an "examination committee" if the proposal COM(2010) 83 final for a new comitology regulation were adopted by the Parliament and the Council.
[148] Articles 4 and 5 of Council Decision 1999/468/EC.

10.3 Evaluation of the need for a Regulation

As discussed above, it could well be argued that the form of a regulation is – as regards the global authorisation of existing BITs – only adequate as long as the other provisions on monitoring, withdrawal and authorisation of new negotiations actually constitute "measures defining the framework for implementing the common commercial policy".[149] A legitimate follow-up question is whether the form of a regulation is actually necessary for these other provisions. The Commission's Explanatory Memorandum states that "[s]oft law instruments, such as a declaration or statement by the Commission services or by the College on the status and validity of bilateral investment agreements, would not establish the legal certainty that is required to guarantee the agreements concerned. This is why a legal instrument is the preferred option." The evaluation of the proposed "framework", however, raises some doubts as to its added value.

As shown above, the list mechanism does not really contribute to enhancing legal certainty but could be seen as an instrument to give the Commission more leverage in its relation with Member States that are reluctant to change or give up their BITs. There are also doubts about the advantage of the proposed framework when it comes to monitoring and remedying conflicts with EU law and dealing with the obstruction of EU negotiations with third countries. These problems could be tackled by recourse to the ordinary infringement procedure as was the case in the cases against Austria, Sweden and Finland. If the Commission finds BITs to conflict or overlap with EU laws or investment policy vis à vis third countries, it could issue a reasoned opinion addressed to the Member State with the request to remedy the problem. In such instances the Member State would be obliged to remedy the situation as a consequence of it duty of loyal co-operation. Failure to do so allows the Commission to initiate proceedings before the ECJ. The only difference to the procedure proposed in the draft Regulation is that the latter would provide for the intermediate step of revoking the authorisation for the BITs and taking it off the list. As shown above, this intermediate step adds another layer of legal uncertainty rather than tackling the actual problem. Direct infringement proceedings would equally have the effect of flagging up problematic BIT provisions to investors, without adding the extra layer.

What remains is the Commission's lack of leverage to force an inactive Council to adopt the necessary negotiation mandates to develop and implement the Union's policies in the exercise of its exclusive competence. The situation is somewhat comparable to that in 2002, when the Commission recommended the Council to adopt decisions finding that Germany and France were in breach of the stability pact due to their budget deficits. The Commission's attempt to force the Council to adopt the decision in the court was ultimately frustrated by the ECJ's formalism. The action for a declaration of failure to act[150] was unavailable to the Commission because the Council was not legally required to adopt the decisions in question. The Commission's action for annulment of the Council's failure to adopt the decisions eventually failed because the ECJ found that the failure to take a decision did not constitute itself an implied negative decision which could be attacked by the annulment action.[151] This illustrates the lack of remedies for the Commission when confronting a Council that is inactive because of the Member States' common interest in holding off Union actions, despite the existence of a clear and exclusive Union competence to develop and to implement the Union's policies in a given area. It is therefore understandable and justifiable that the Commission seeks the adoption of a mechanism that will provide it with the necessary leverage to overcome inactivity in the Council.

[149] Cf. Article 207(2) TFEU.

[150] Now Article 265 TFEU.

[151] ECJ Case C-27/04, *Commission v. Council*, [2004] ECR I-6649 ¶¶ 31, 34.

The same logic applies to the draft Regulation's provisions giving the Commission the power to authorise Member States to negotiate new BITs or amendments to existing BITs during the transitional period. Renegotiation would clearly be an alternative to simple termination of BITs. Renegotiation would allow incompatibilities to be eliminated while maintaining the legal protection and the legal certainty afforded by the existing treaties. Member States can only open negotiations in the field of exclusive competences when empowered by the Union. And it is the Commission that must ensure that the Union's interests are respected, especially regarding the development and implementation of the new competence for investments. Insofar, the proposed procedure is probably the most efficient solution for tackling the problem. However, it is questionable whether the Council will accept delegating the central power for authorising negotiations to the Commission. Technically, there is no absolute need for such delegation, as in absence of a special transitional regime, Member States should be able to request the Commission to recommend the adoption of a Council decision to authorise their negotiations.[152] This might be less efficient, but it would still allow the Commission some influence on the shaping of the Union's policies in this respect.

11 DISCUSSION OF POLICY OPTIONS

Facing the present draft Regulation, the Parliament has essential three options: (1) to reject the project as granting the Commission too much unchecked power to shape the future investment policy of the Union; (2) to support the Commission's project to ensure that the Union's exclusive competence is effectively developed and implemented despite potential – and expected – resistance by numerous member states; or (3) to work towards and intermediate solution that would favour the development of the Union's policy on foreign investment by accepting the principle of a procedural framework as proposed by the Commission to ensure progress towards a common EU policy is mantained but with a modification that would allow the Council to retain a say over critical issues while, at the same time, ensuring a transparent public debate on the development in the Parliament.

(1) Option 1: Rejection of the Commission's proposal

As shown above, there are ultimately legitimate reasons for framework proposed by the Commission. The solutions of the proposed draft Regulation would clearly strengthen the Union's exclusive competence for international investment. But there is doubt that the proposed Regulation would provide more legal certainty than the present situation. The absence of any framework for managing the transition, however, could potentially also lead to a significant loss of the legal certainty. Given the ECJ's favourable position in the cases against Austria, Sweden and Finland, the Commission may feel obliged to initiate a wave of infringement procedures against Member States over their duty to loyal co-operation. Simply blocking the Commission's proposal is therefore unlikely to be in the interests of either the Council or the Parliament. This laborious and potentially damaging route of litigation would *de facto* leave the ultimate definition of the future shape of the Union's approach to investment to the ECJ.

[152] Given that such a decision would not constitute a "measure defining the framework for implementing the common commercial policy" but an implementation measure, it can be doubted whether the ordinary legislative procedure applies under Articles 2(1), 207(2), 288(4) TFEU. Instead, the analogous application of Article 218(2) TFEU would seem more fitting.

(2) Option 2: Support of the Commission's proposal

As also shown above, the current proposal would give the Commission very broad discretion to manage the transitional period and shape the Union's future investment policy. This stems from the proposed powers to force member states to revoke their BITs on the basis of them constituting "an obstacle to the development and implementation of the Union's policy". The lack of definition of this ground, and the resulting difficulty of judicial review of the Commission's decisions by the ECJ, raise questions about the institutional balance and accountability in an area of the common commercial policy that is highly controversial and of potentially far reaching consequences. Furthermore, de-authorisation would seem to be detrimental to the EU's negotiating aims. The aim of EU negotiations should be to at least match the standards of existing member state BITs, de-authorising a high standard member state BIT opens up the possibility of the EU's negotiating partner pressing for something weaker rules. If there are MS BITs of a high standard in place the EU can clearly argue that it cannot accept less than what the third country has negotiated with one member state.

(3) Option 3: Working towards an institutionally balanced compromise

Based on the above, it seems desirable to dispose of a clear procedural framework for managing the transition from the patchwork of existing member state BITs to a CCP for the Union that covers international investment. A framework along the basic lines of the Commission proposal would, despite all criticism, offer a fairly stable solution. The legal uncertainty resulting from BITs potentially being incompatible with EU law and policies cannot be eliminated by a general measure, but can only be resolved on a case by case basis. At least, a framework as proposed by the Commission has the merit of providing a slightly more foreseeable procedure than litigation on an ad hoc basis. Moreover, it would ensure that the Union can effectively take up its new exclusive competence and consistently develop its future policy on international investments.

The key issue however, is how to ensure trust and cooperation between the EU institutions in the process of decision making. On one hand, the member states have a legitimate interest in ensuring a smooth transition from member state to EU investment agreements. On the other hand, the European public has a legitimate interest ensuring the transparent and democratic basis for decision making on EU investment policy. These interests could be reconcilled by providing for adequate representation of the Council and the Parliament in the decision making process. The means of achieving such an institutional balance would be to provide a greater role for the committee envisaged in the Commission's draft Regulation. Given the ongoing discussions about the future of the comitology system, it may be sufficient to point out that the present proposal of creating a simple advisory committee does not provide for significant checks and balances of the Commission's powers. The need for balance might be better addressed by what is currently provided by the "regulatory procedure".[153] If,

[153] Article 5 of Council Decision 1999/468/EC of 28 June 1999 ("Comitology Decision"), [1999] OJ L 184/23. The only recent regulation in the area of the common commercial policy creating a committee also provides for regulatory procedure: see Article 27 of Council Regulation (EC) No 732/2008 of 22 July 2008 applying a scheme of generalised tariff preferences for the period from 1 January 2009 to 31 December 2011 and amending Regulations (EC) No 552/97, (EC) No 1933/2006 and Commission Regulations (EC) No 1100/2006 and (EC) No 964/2007, [2008] OJ L 211/1. It is also worth noting that some earlier instruments in the context of the common commercial policy – but prior to the introduction of the co-decision procedure – provide for equivalents to the "management procedure", such as in Council Regulation (EEC) No 3030/93 of 12 October 1993 on common rules for imports of certain textile products from third countries, [1993] OJ L 275/62; Council Regulation (EC) No 520/94 of 7 March 1994 establishing a Community procedure for administering quantitative quotas, [1994] OJ L

for example, the committee of national experts disagrees with a Commission's assessment, the Parliament would get to state its position and the Council, "where appropriate in view of any such position", could block the adoption of the decision within three months. Failing a Council decision within that time limit, the Commission can adopt the decision.

This mechanism would be of particular interest in cases involving an assessment of "the development and implementation of the Union's policies", since any decision to withdraw the authorisation of a BIT on this ground can be considered a further step in the determination of the contours of that policy.[154] Council and Parliament would thus have the opportunity to influence the Commission's decisions and ensure a more concerted and gradual development and implementation of the Union's policies on international investment.[155]

66/1; Council Directive 98/29/EC of 7 May 1998 on harmonisation of the main provisions concerning export credit insurance, [1998] OJ L 148/22.

[154] And hence make the decision an equivalent to a "measure of general scope" in the sense of Article 3(b) of the Comitology Decision.

[155] An even stronger degree of involvement of the Council and especially of the Parliament would result from the adoption of the "regulatory procedure with scrutiny" as introduced by Council Decision 2006/512/EC of 17 June 2006, [2006] OJ L 200/11, which would allow both institutions to scrutinize and to veto a planned decision by the Commission.

Table 9 The structure EU member state BIT provisions on investor protection

EU BITs - Investor-to-state dispute settlement - Indirect Expropriation - Fair and Equitable Treatment Legend: Y = Yes; N = No								
EU member state signatory	**EU member state partner**	**Date of signature**	**In Force?**	**Does the BIT provide for investor-to-state dispute settlement?**	**Does the BIT cover 'indirect expropriation'?**	**Does the BIT cover 'Fair and Equitable Treatment'?**	**Is Fair and Equitable Treatment linked to 'minimum standard of treatment'?**	**Is Fair and Equitable Treatment linked to 'international law' (or 'customary', or 'principles of')?**
Germany	China	01-Dec-03	11-Nov-05	Y	Y	Y	N	N
Germany	India	10-Jul-95	13-Jul-98	Y	N	Y	N	N
Germany	Russia	13-Jun-89	13-Jun-89	Y	N	N*	N	N
Germany	Pakistan	01-Dec-09	No	Y	N	Y	N	N
Germany	Oman	30-May-07	No	Y	Y	Y	N	N
Germany	Jordan	13-Nov-07	No	Y	Y	Y	N	N
Germany	Yemen	02-Feb-05	Mar-08	N	N	Y	N	N
Germany	Nigeria	28-Mar-00	Sep-07	Y	Y	N	N	N
United Kingdom	China	15-May-86	May-86	Y	N	Y	N	N
United Kingdom	India	14-Mar-94	Jan-95	Y	N	Y	N	N
United Kingdom	Russia	06-Apr-89	Jul-91	Y	N	Y	N	N
United Kingdom	Ethiopia	19-Nov-09	No	Y	N	Y	N	N
United Kingdom	Mexico	12-May-06	Jul-07	Y	Y	Y	Y	Y
United Kingdom	Vanuatu	22-Dec-03	No	Y	N	Y	N	N
United Kingdom	VietNam	01-Aug-02	No	Y	N	Y	N	N
France	India	02-Sep-97	17-May-00	Y	Y	Y		N
France	China (1985 agreement)	26-Nov-07 ----	No	N	N	Y	N	N
France	Russia	04-Jul-89	18-Jul-91	Y	N	N	N	N
France	Tajikistan	01-Jan-02	24-Aug-04	Y	Y	Y	N	Y
France	Venezuela	02-Jul-01	30-Apr-04	Y	Y	Y	N	Y

Italy	China	28-Jan-85	28-Aug-87	N	N	N	N	N
Italy	India	23-Nov-95	26-Mar-98	Y	N	Y	N	N
Italy	Russia	17/12/2002 ???	17-Dec-02	Y	N	Y	N	N
Netherlands	Brazil	25-Nov-98	No	Y	Y	Y	N	N
Netherlands	China	26-Nov-01	1-Aug-04	Y	N	Y	N	N
Netherlands	India	06-Nov-95	01-Dec-96	Y	N	Y	N	N
Netherlands	Russia	05-Oct-89	20-Jul-91	Y	N	Y	N	N
Netherlands	Serbia	16-Apr-07	No	Y	N	Y	N	N
Netherlands	Oman	17-Jan-09	No	N	Y	Y	N	N
Netherlands	Benin	13-Dec-01	15-Dec-07	N	Y	Y	N	N
Netherlands	Kazakhstan	27-Nov-02	1-Aug-07	Y	Y	Y	N	N
Belgium & Luxembourg	China	06-Jun-05	No	Y	N	N	N	N
Belgium & Luxembourg	India	31-Oct-97	08-Jan-01	Y	N	Y	N	N
Belgium & Luxembourg	Colombia	4-Feb-09	No	Y	Y	Y	Y	Y
Belgium & Luxembourg	Benin	18-May-01	30-Aug-07	Y	Y	Y	N	N
Belgium & Luxembourg	Gabon	27-May-98	28-May-05	Y	N	Y	N	Y
Belgium & Luxembourg	Peru	12-Oct-05	12-Sep-08	Y	Y	Y	N	Y
Spain	Colombia	31-Mar-05	22-Sep-07	Y	N	Y	N	N
Spain	Mexico	10-Oct-06	04-Apr-08	Y	Y	Y	Y	Y
Czech Republic	United States	22-Oct-91	19-Dec-92	Y	Y	Y	N	N
Czech Republic	China	8-Dec-05	9-Jan-06	Y	N	Y	N	N
Czech Republic	India	11-Oct-96	06-Feb-98	Y	N	N	N	N
Czech Republic	Mexico	04-Apr-02	13-Mar-04	Y	Y	Y	Y	Y
Romania	China	16-Apr-07	01-Sep-09	Y	N	Y	N	N
Romania	Lebanon	15-Apr-09	No	Y	Y	Y	N	N

Romania	Canada	08-May-09	No	Y	N	Y	Y	Y
Finland	Brazil	28-Mar-95	No	Y	N	Y	N	N
Finland	China	15-Nov-04	15-Nov-06	Y	N	Y	N	N
Finland	VietNam	21-Feb-08	No	Y	Y	Y	N	N
Finland	Indonesia	12-Sep-06	02-Aug-08	Y	N	Y	N	N
Finland	Nigeria	22-Jun-05	20-Mar-07	Y	Y	Y	N	N

Source; UNCTAD BIT Database: http://www.unctadxi.org/templates/DocSearch____779.aspx - last viewed on October 3, 2010

Table 13 Known Investor to State Dispute Settlement Cases where EU Member States Are Respondents

Year of case initiation	Respondent country	Investor Home	Parties to the Dispute	Topic	Venue of DS Proceedings	Award	Decions	Who Wins Case
1994	Poland	Germany	Saar Papier v. Poland I	claim arising out of enforcement of environmental regulations	UNCITRAL	DM 2.3 million awarded (equivalent in US$ unknown)	awarded in favor of the investor	awarded in favor of the investor
1996	Poland	Germany	Saar Papier v. Poland II	claim arising out of the enforcement of environmental regulation	UNCITRAL	unknown	unknown	unknown
1996	Poland	United States	Ameritech v. Poland	not available	UNCITRAL	case was settled in 1996-97, but terms were never made public	settled	settled
1996	Poland	France	France Telecom v. Poland	not available	UNCITRAL	case was settled in 1996-97, but terms were never made public	settled	settled
1997	Slovak Republic	Czech Republic	Ceskoslovenska Obchodni Banka, a.s. v. The Slovak Republic (ICSID Case No. ARB/97/4)	not available	ICSID	Slovak Crowns 24,8 billion (approx US$ 800 million) plus interest	Decision on Jurisdiction issued on 24 May 1999;Second Decision on Jurisdiction issued on 1 December 2000; Award issued on 29 December 2004	awarded in favor of the investor
1997	Spain	Argentina	Emilio Agustin Maffezini v. The Kingdom of Spain (ICSID Case No. ARB/97/7)	claims arising from treatment allegedly received by the investor from Spanish entities, in connection with his investment in an enterprise for the production and distribution of chemical products in	ICSID	Spanish Pesetas 30 million awarded plus interest - for a total of 57,641,265.28 Spanish Pesetas (equivalent to US$ 296,597 at time of award in 2000)	Procedural Order on Provisional Measures issued on 28 October 1999;Decision on Jurisdiction issued on 25 January ; Rectification of the Award issued on 31 January 2001Award issued on 13 November 2000;2000;	awarded in favor of the investor

				the Spanish region of Galicia				
1998	Poland	Germany	Lutz Ingo Schaper v. Poland	claims arising out of the enforcement of environmental regulation	UNCITRAL	pending		pending
1999	Czech Republic	United States	Ronald Lauder v. Czech Republic	claims arising out of the conduct of the Czech Media Council towards the broadcasting enterprise partly owned by the foreign investor	UNCITRAL	no damages awarded	Award issued on 3 September 2001	awarded in favor of the state
1999	Estonia	United States	Alex Genin, Eastern Credit Limited, Inc v. Republic of Estonia (ICSID Case No. Arb/99/2)	not available	ICSID	all claims were rejected on the merits	Award issued on 25 June 2001	awarded in favor of the state
1999	Latvia	Sweden	Swembalt AB v. Latvia	not available	UNCITRAL	US$ 2,506,235 awarded, with interest of 10 % per year starting 9 April 1999; Award unsuccessfully challenged in Swedish courts	Award issued on 23 October 2000	awarded in favor of the investor
2000	Czech Republic	Netherlands	CME v. Czech Republic	claims arising from the actions and omissions attributed to the Media Council, an organ of the Czech	UNCITRAL	US$ 269,814,000 awarded plus interest (at 10% from 23 February 2003 until	Partial Award issued on 13 September 2001;Final Award issued on 14 March 2003	awarded in favor of the investor

				Republic, that allegedly commercially destroyed the broadcasting station operator which was partly owned by the investor		payment)		
2001	Czech Republic	Netherlands	Saluka Investments BV (The Netherlands) (Nomura -- Japan) v. Czech Republic	not available	UNCITRAL, PCA is providing secretarial support; seat is geneva, hearings have been in London	pending; Tribunal found a breach of FET; question of the appropriate redress for that breach, including questions of quantum, will be addressed in a second phase of this arbitration	Decision on Jurisdiction over the Czech Republic's Counterclaim issued on 7 May 2004;Partial Award issued on 17 March 2006	awarded in favor of the investor
2001	Latvia	Sweden	Nykomb Synergetics v. Latvia	not available	SCC	Lats 1,600,000 (equivalent to approx US$ 3 million) plus interest	Award issued on 16 December 2003	awarded in favor of the investor
2001	Romania	United States	Noble Ventures v. Romania (ICSID Case No. ARB/01/11)	claims arising out of a privatization agreement concerning the acquisition, management, operation and disposition of a substantial steel mill with associated and other assets	ICSID	claims rejected on the merits	Award issued on 12 October 2005; Decision on the Respondent's Request for Rectification of the Award of October 12, 2005 issued on 19 May 2006	awarded in favor of the state
2002	Czech Republic	United Kingdom	William Nagel v. Czech Republic	not available	SCC	claim was rejected on the merits (award partly public); currently	Award issued in 2003	awarded in favor of the state

						being challenged in Swedish courts		
2002	Portugal	Germany	German investor v. Portugal	not available	UNCITRAL	settled at an early stage		settled
2003	Bulgaria	Cyprus	Plama Consortium Limited v. Republic of Bulgaria (ICSID Case No. ARB/03/24)	not available	ICSID	Tribunal has jurisdiction but claims dismissed on the merits	Decision on Jurisdiction issued on 8 February 2005;Order on provisional measures issued on 6 September 2005;Award issued on 27 August 2008	awarded in favor of the state
2003	France/United Kingdom	France/United Kingdom	Eurotunnel Group v. France and United Kingdom	claims arising out principally of the allegedly inadequacy of protection afforded to the eurotunnel rail services by the respondents from disruptions caused by clandestine migrants	ad-hoc	pending; Tribunal has jurisdiction and finds the respondents in violation of the Concession Agreement; calculation of losses to be determined if necessary in a subsequent phase	Award issued on 30 January 2007	awarded in favor of the investor
2003	Hungary	Cyprus	ADC Affiliate Limited and ADC & ADMC Management Limited v. Republic of Hungary (ICSID Case No. ARB/03/16)	claims arising out of the alleged take-over by the Government of Hungary of all activities of the investor's company in the Budapest airport	ICSID	US$ 75 million awarded plus costs of US$ 7.6 million	Award issued on 2 October 2006	awarded in favor of the investor
2003	Poland	Netherlands	Eureko v. Poland	not available	UNCITRAL	claims was successful; damages not yet quantified	Partial Award on Liability issued on 19 August 2005	awarded in favor of the investor
2003	Romania	Poland	An investor-state dispute between a Polish investor and	not available	UNCITRAL; administered at PCA	case was settled on undisclosed terms on 24 May 2004		settled

			Romania					
2004	Czech Republic	Netherlands	Eastern Sugar v. Czech Republic	not available	UNCITRAL	approx US$ 25,539,995, plus annual interest of 7%;The arbitration cost will be fixed at a later date.	Partial award issued on 27 March 2007	awarded in favor of the investor
2004	Estonia	Finland	OKO Osuuspankkien Keskuspankki Oyj and others v. Republic of Estonia (ICSID Case No. ARB/04/6)	Claim arising out of the alleged non-payment of a loan which had been made to a joint-venture Estonian company	ICSID	Investor prevailed (award not public)	Award issued on 19 November 2007 (not public)	awarded in favor of the investor
2004	Hungary	Norway	Telenor Mobile Communications AS v. Republic of Hungary (ICSID Case No. ARB/04/15)	not available	ICSID	Tribunal lacks jurisdiction	Decision on Jurisdiction issued on 13 September 2006	awarded in favor of the state
2004	Poland	United States	Cargill, Incorporated v. Republic of Poland (ICSID Case No. ARB(AF)/04/2)	not available	UNCITRAL (This case was switched from an ICSID case to an UNCITRAL case at the request of the parties)	unknown	Award issued on 18 September 2009 (not public)	unknown
2004	Slovenia	Netherlands	Interbrew v. Slovenia (ICSID Case No. ARB/04/17)	not available	ICSID	settled by the parties	Order taking note of the discontinuance pursuant to Arbitration Rule 44 issued by the Tribunal on 18 July 2005	settled

2005	Czech Republic	Netherlands	Mittal Steel Company N.V.(Dutch company) v Czech Republic	not available	UNCITRAL	pending	Settlement reached in early 2009	settled
2005	Czech Republic	Luxembourg	European Media Ventures v. Czech Republic	not available	UNCITRAL	unknown	Award on jurisdiction issued in 2007;Award issued on 8 July 2009 (not public)	unknown
2005	Czech Republic	Croatia	Pren Nreka v. Czech Republic	not available	UNCITRAL	pending; Tribunal has jurisdiction (decision is not public);review of decision on jurisdiction rejected by French court	Decision on Jurisdiction issued on 5 February 2007;Final Award issued on 22 July 2008	awarded in favor of the investor
2005	Lithuania	Norway	Parkerings Compagniet AS v. Republic of Lithuania (ICSID Case No. ARB/05/8)	not available	ICSID	Tribunal has jurisdiction; claims dismissed on the merits	Award issued on 11 September 2007	awarded in favor of the state
2005	Romania	United Kingdom	EDF (Services) Limited v. Republic of Romania (ICSID Case No. ARB/05/13)	claims arising out of a concession to provide duty free and other retail services at Romanian airports	ICSID	claims rejected on the merits	Award issued on 8 October 2009	awarded in favor of the state
2005	Romania	Sweden	Ioan Micula, Viorel Micula and others v. Romania (ICSID Case No. ARB/05/20)	not available	ICSID	pending; Tribunal has jurisdiction	Decision on Jurisdiction issued on 24 September 2008	pending
2005	Slovenia	Croatia	Hrvatska Elektropriveda d.d. (HEP) v. Republic of Slovenia (ICSID Case No. ARB/05/24)	not available	ICSID	pending		pending
2005	Romania	United States	EDF (Services) Limited v. Romania (ICSID Case No. ARB/05/13)	not available	ICSID	pending		pending

2005	Czech Republic	Netherlands	K+Venture Partners v. Czech Republic	unknown	UNCITRAL	Settled (details of the settlement agreement are not public)	Settlement reached in late 2006	settled
2006	Czech Republic	Germany	R.J. Binder v Czech Republic	claim arising out of alleged fraud by Czech customs authorities causing bankruptcy of the investment	UNCITRAL	pending; Tribunal has jurisdiction (decision is not public);review of decision on jurisdiction before Czech courts	Decision on Jurisdiction issued in 2006 (not public)	pending
2006	Poland	France	Vivendi v Poland	not available	UNCITRAL	unknown		unknown
2006	United Kingdom	India	Sancheti v United Kingdom	not available	UNCITRAL	unknown		unknown
2006	Romania	Greece	Spyridon Roussalis v. Romania (ICSID Case No. ARB/06/1)	not available	ICSID	pending		pending
2006	Romania	Netherlands	The Rompetrol Group N.V. v. Romania (ICSID Case No. ARB/06/3)	not available	ICSID	pending; Tribunal has jurisdiction	Decision on Jurisdiction issued on 18 April 2008	pending
2006	Czech Republic	Israel	Phoenix Action Ltd v. Czech Republic (ICSID Case No. ARB/06/5)	not available	ICSID	Tribunal lacks jurisdiction	Award issued on 15 April 2009	awarded in favor of the state
2006	Estonia	Netherlands and United States	Rail World LLC and others v. Republic of Estonia (ICSID Case No. ARB/06/6)	not available	ICSID	Case was settled and proceeding discontinued	Order taking note of the discontinuance pursuant to Arbitration Rule 43(1) issued by the Tribunal on 5 February 2007	settled
2006	Czech Republic	Norway	Czechoslonor v. Czech Republic	not available	Unknown	unknown		unknown

2006	Slovak Republic	Switzerland	Branimir Mensik v. Slovak Republic (Case No. ARB/06/9)	not available	ICSID	Tribunal issued an order for the discontinuance of the proceeding on 9 December 2008, for lack of payment of advances, pursuant to Regulation 14(3)(d) of the ICSID Administrative and Financial Regulations		unknown
2007	Slovak Republic	Austria	Austrian Airlines v Slovak Republic	not available	UNCITRAL	Tribunal declines jurisdiction	Award issued on 20 October 2009 (not public)	awarded in favor of the state
2007	Czech Republic	Canada	Frontier Petroleum Services (FPS) v Czech Republic	not available	UNCITRAL	pending		pending
2007	Hungary	United Kingdom	AES Summit Generation Limited and AES-Tisza Eromu Kft. v. Republic of Hungary (ICSID Case No. ARB/07/22)	not available	ICSID	pending		pending
2007	Hungary	Belgium	Electrabel S.A. v. Republic of Hungary (ICSID Case No. ARB/07/19)	not available	ICSID	pending		pending
2007	Romania	United States	S&T Oil Equipment & Machinery Ltd. v. Romania (ICSID Case No. ARB/07/13)	Claim arise out of a cancellation of privatization agreement	ICSID	pending		pending

2007	Czech Republic	Netherlands	Invesmart v. Czech Republic	Claims arising out of the alleged withdrawl by the Czech Republic of previous commitments to provide state support to the foreign-owned bank	UNCITRAL	unknown	Award issued on 3 July 2009 (not public)	pending
2007	Lithuania	Russian Federation	Kalingrad Region v Lithuania	Claims arising out of the seizure of a building allegedly owned by the Kalingrad regional government	ICC	Pending		pending
2007	Poland	Germany	Nordzucker v Poland	claims arising out of the alleged non-privatization of two Polish sugar producers	UNCITRAL	Pending		unknown
2008	Czech Republic	Germany	InterTrade v Czech Republic	not available	Unknown	pending	Decision on Jurisdiction issued in 2009 (not public);Award issued in 2009 (not public)	pending
2008	Poland	Cyprus	Mercuria Energy Group Limited (Mercuria) v Poland	claims arising out of Poland's implementation of European Union directive on mandatory fuel reserves	SCC	pending		pending
2008	Slovak Republic	Netherlands	HICEE v Slovak Republic	claims arising out of the alleged reversal of a series of health care reforms initiated by a previous administration (including the requirement that	UNCITRAL (administered by PCA)	pending		pending

				insurance must be provided on a not-for-profit basis)				
2008	Czech Republic	Germany	Nepolsky v. Czech Republic	not available	UNCITRAL	pending		pending
2009	Slovak Republic	the Netherlands	Eureko v Slovak Republic	not available	Unknown	pending		pending
2009	Germany	Sweden	Vattenfall AB, Vattenfall Europe AG, Vattenfall Europe Generation AG v. Federal Republic of Germany (ICSID Case No. ARB/09/6)	not available	ICSID	pending		pending
2009	Hungary	France	EDF v. Hungary	claims arising out of the termination of the power generation contract	UNCITRAL	pending		pending
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