The Future of Bilateral Investment Treaties of EU Member States

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Introduction

The era of modern investment treaties began when Germany and Pakistan concluded a bilateral agreement that entered into force in 1962. Germany's interest in investment treaties was grounded in the loss of its earlier foreign investment in negotiated settlements after 1949 owing to the damage it had caused in World War II. In an investment treaty the host state renounces part of its sovereignty to attract foreign investment. In turn, for an investor an investment treaty provides legal protection against state interference, which can come in a range of different forms, including expropriation, conversion and transfer of assets or any forms of unfair, inequitable, discriminatory or arbitrary treatment. Today, these investment guarantees are contained in large part in the approximately 2,000 bilateral investment treaties (BITs) that are currently in force worldwide. Germany has the most comprehensive network, with around 130 BITs in force, whereas other EU Member States also concluded a great number of BITs and continue to conclude such treaties.[1]

Prior to the entry into force of the Treaty of Lisbon, the then European Community had never concluded an investment treaty or an international agreement that predominantly regulated investment with third states. Indeed, from Opinion 1/94 it followed that the Community competence for the common commercial policy (CCP) did not extend to foreign direct investment (FDI) involving

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[1]Other European states with a comprehensive BIT programme are the UK, Italy and France, all of which have around 100 BITs in force. In 2007 the Netherlands (five), Finland, Germany and Spain (three each) together accounted for the majority of the new BITs concluded by EU Member States. See UNCTAD, Recent developments in international investment agreements (2007 to June 2008), available at http://www.unctad.org/en/docs/webdiaeia20081_en.pdf.

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third states.[2] The Community and the Member States together, however, concluded several international agreements with third states that contain provisions in the field of FDI.[3] Regardless of these agreements, the Member States have been the dominant factor in shaping the EU's investment relations with third states. Nevertheless, even prior to the entry into force of the Treaty of Lisbon certain developments casted doubt on Member States' competence to conclude, amend and uphold their BITs.

First, on 3 March 2009, the European Court of Justice (ECJ) rendered its judgments in infringement cases brought by the Commission against Austria and Sweden. The cases concern some BITs entered into by the two Member States, on the one hand, and various third states, on the other hand, under which investors are guaranteed the free transfer of capital connected with their investments. All of the BITs concerned predate the accession of the Member States to the EU and were therefore governed by Article 307 EC (equivalent to Article 351 Treaty on the Functioning of the European Union; TFEU). Under this provision, Member States are obliged to take all appropriate steps to eliminate any incompatibility with the EC Treaty contained in such agreements. The Commission contended that Austria and Sweden infringed that obligation inasmuch as their agreements do not provide for the restrictions on the free movement of capital to and from third states envisaged in Articles 57(2), 59 and 60(1) EC and they had not acted to rectify that situation. In its judgments the ECJ declared that the Member States had failed to fulfil their obligations under Article 307(2) EC.[4] On 19 November 2009, the ECJ confirmed its view in its judgment in parallel infringement proceedings against Finland.[5] With a view to the ECJ's jurisprudence on Article 307 EC, in effect, Austria, Finland and Sweden may have to terminate the BITs in question. In its judgments, the ECJ clarified that the incompatibilities with the EC Treaty to which the BITs with third states give rise are not limited to the defendants in these cases.[6] Therefore, the ECJ's judgments may have consequences for BITs of all EU Member States.

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[2]ECJ, Opinion 1/94, *WTO*, [1994] ECR I, 5267.

[3]The EU-Chile Association Agreement, OJ 2002 L 352/3, is the most advanced bilateral free trade agreement currently in force including investment issues. On the multilateral level, the most important agreement is the Energy Charter Treaty (ECT), a multilateral treaty with 47 contracting parties, including the European Communities and all Member States. Both the European Communities and all Member States are contracting parties to the ECT as it was concluded as a mixed agreement, falling within the scope of both Community and Member State competence. See Council and Commission Decision 98/181/EC, ECSC, EURATOM of 23 September 1997 on the conclusion by the European Communities, of the Energy Charter Treaty and the Energy Charter Protocol on energy efficiency and related environmental aspects, OJ 1998 L 69/1.

[4]ECJ, C-205/06, *Commission v. Austria*, not yet in the official reports; ECJ, C-249/06, *Commission v. Sweden*, not yet in the official reports. The author represented Austria in these proceedings up until but not inclusive of the oral hearing before the ECJ.

[5]ECJ, C-118/07, *Commission v. Finland*, not yet in the official reports.

[6]ECJ, C-205/06, *Commission v. Austria*, not yet in the official reports, para. 43; ECJ, C-249/06, *Commission v. Sweden*, not yet in the official reports, para. 43; ECJ, C-118/07, *Commission v. Finland*, not yet in the official reports, para. 34.

Secondly, on 1 December 2009, the Treaty of Lisbon entered into force.[7] The Treaty of Lisbon shifts the allocation of competences between the EU and its Member States in the field of FDI towards the EU. Article 207(1) TFEU states: "The common commercial policy shall be based on uniform principles, particularly with regard to changes in tariff rates, the conclusion of tariff and trade agreements relating to trade in goods and services, and the commercial aspects of intellectual property, *foreign direct investment*, [. . .]" (emphasis added). The extension of the CCP to FDI under the Treaty of Lisbon means that the EU has exclusive competence to negotiate and conclude investment treaties with respect to FDI.[8] Member States will lose the competence to negotiate and conclude treaties covered by the EU competence. But although the extent of the EU's competence is not yet clear, it would seem that the continued applicability of BITs of Member States in force with third states is not endangered,[9] subject to possible infringement proceedings commenced by the Commission against Member States.

Predominantly as a result of the EU's more recent enlargement process, there are currently around 190 BITs in force between Member States.[10] Prior to the entry into force of the Treaty of Lisbon, it was assumed that these so-called intra-EU BITs would continue to be applicable.[11] But the Treaty of Lisbon does not only extend the CCP to FDI, it also amends Article 60(1) EC insofar as it deletes the reference to third states. Article 75(1) TFEU states: "Where necessary to achieve the objectives set out in Article 67 [. . .] the European Parliament and the Council [. . .] shall define a framework for administrative measures with regard to capital movements and payments, such as the freezing of funds, financial assets or economic gains belonging to, or owned or held by, natural or legal persons, groups or non-State entities." It may be that, as a result, intra-EU BITs come under increased scrutiny of the Commission following the ECJ's judgments.

This article will analyse the future of BITs of EU Member States. First, it will deal with the external dimension, i.e. with the future of BITs of Member States as a result of the ECJ's judgments in the infringement proceedings against Member States and as result of the entry into force of the Treaty of Lisbon. Second, it will look at the internal dimension, i.e. at the future of intra-EU BITs, not least in the

[7] Treaty of Lisbon amending the Treaty on European Union (TEU) and the Treaty Establishing the European Community, signed in Lisbon on 13 December 2007, entered into force on 1 December 2009.

[8] Article 2(1) TFEU states: "When the Treaties confer on the Union exclusive competence in a specific area, 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 or for the implementation of Union acts." The TFEU put an end to the three-pillar-structure of the EU. Reference in the context of the TFEU is therefore made to "Union," "EU" and "EU law" rather than "Community" and "EC law".

[9] BVerfG, 2 BvE 2/08, *Organstreit*, NJW (2009), pp. 2267 et seq., para. 380.

[10] Wehland, Intra-EU Investment Agreements and Arbitration: Is European Community Law an Obstacle? ICLQ 58 (2009) 2, pp. 297–320.

[11] *Eastern Sugar B.V. (Netherlands) v. The Czech Republic,* Partial Award of 27 March 2007, available at http://ita.law.uvic.ca/documents/EasternSugar.pdf.

light of the Treaty of Lisbon. It will argue that for the time being in both dimensions BITs of Member States will continue to play a role.

The External Dimension: The Future of BITs with Third States

The Infringement Proceedings against Certain Member States

Prior to the entry into force of the Treaty of Lisbon, the scope of the CCP did not *explicitly* extend to FDI. Both the Treaty of Amsterdam and the Treaty of Nice extended the scope of the CCP. These two extensions, however, only had limited relevance for foreign investment policy.[12] To the contrary, the Commission's proposals regarding the expansion of the CCP to FDI at the intergovernmental conferences in Amsterdam and Nice were rejected.[13] In Opinion 1/94 the ECJ ended the expansion of Community competence under the CCP.[14] The ECJ thereafter indicated that trade measures would not necessarily be perceived as trade or commercial policy measures if they pursue other objectives. According to the ECJ's jurisprudence, a Community measure fell within the competence in the field of the CCP provided for in Article 133 EC "only if it relates specifically to international trade in that it is essentially intended to promote, facilitate or govern trade and has direct and immediate effects on trade in the products concerned."[15]

Besides explicit external competence, the Community also could have *implied* external competence. Implied *exclusive* competence arose either as a result of internal legal acts of the Community[16] or because external action was deemed necessary for achieving Community objectives.[17] Several competences of the Community provided for the adoption of measures that affected inward investment

[12]Ceyssens, Towards a Common Foreign Investment Policy? – Foreign Investment in the European Constitution, Legal Issues of Economic Integration 32 (2005) 3, p. 259 (261).

[13]Cremona, EC External Commercial Policy after Amsterdam: Authority and Interpretation within Interconnected Legal Orders, in: Weiler (ed.), *The EU, the WTO, and the NAFTA: Towards a Common Law of International Trade*, 2000, p. 5 (15); Herrmann, Common Commercial Policy after Nice: Sisyphus Would have Done a Better Job, CMLR 39 (2002) 1, p. 7 (14).

[14]In the early cases concerned with the interpretation of the scope of the CCP, the ECJ took a rather liberal stance when it held that the CCP had the same content as the commercial policy of a state. ECJ, Opinion 1/75, *Local Costs*, [1975] ECR, 1355; ECJ, Opinion 1/78, *International Agreement on Natural Rubber*, [1979] ECR, 2871.

[15]ECJ, Opinion 1/94, *WTO*, [1994] ECR I, 5267, para. 57; ECJ, Opinion 2/00, *Cartagena Protocol*, [2001] ECR I, 9713, para. 40; ECJ, C-281/01, *Commission v Council,* [2002] ECR I, 12049, paras. 40 and 41; ECJ, C-347/03, *Regione autonoma Friuli-Venezia Giulia and ERSA*, [2005] ECR I, 3785, para. 75; ECJ, Joined Cases C-402/05 P and C-415/05 P, *Kadi and Al Barakaat*, not yet in the official reports, para. 301.

[16]ECJ, 22/70, *AETR*, [1971] ECR 263.

[17]ECJ, Opinion 1/76, *Laying-up Fund*, [1977] ECR, 741.

to the EU.[18] These competences conferred certain external competences to the Community, but were far from covering all fields that are typically covered by a BIT.[19] However, the consequences of the implied exclusive competence of the Community were illustrated in the BIT infringement proceedings.

The Commission had originally commenced infringement proceedings not only against Austria, Finland and Sweden, but also against Denmark. The reasons why the cases against Austria and Sweden were combined whereas the case against Finland proceeded on a separate, somewhat delayed track remain unclear. Unlike Austria, Finland and Sweden, Denmark appears to have taken a more conciliatory approach. The Commission had argued that the 1968 Denmark–Indonesia BIT violated Denmark's obligation under Article 307 EC. In response, Denmark terminated the BIT and negotiated a new BIT with Indonesia, which was signed on 22 January 2007.[20]

In the cases against Austria and Sweden the BITs at issue contain provisions that guarantee the free transfer, without undue delay and in freely convertible currency, of payments connected with an investment. In its judgments the ECJ noted that the BITs were consistent with the wording of Articles 56(1) and 56(2) EC. Under these provisions all restrictions on the movement of capital and payments between Member States and between Member States and third states were prohibited.[21] Articles 57(2), 59 and 60(1) EC, however, conferred on the Council the power to restrict, in certain circumstances, movements of capital and payments between Member States and third states. As the BITs at issue do not contain any provision reserving such possibilities to restrict such movements, the ECJ found that it was necessary to examine whether Austria and Sweden were under an obligation to take the appropriate steps in accordance with Article 307(2) EC.

The ECJ observed that to ensure the effectiveness of Articles 57(2), 59 and 60(1) EC measures restricting the free movement of capital, where adopted by the Council, had to be capable of being applied immediately with regard to the state to which they relate.[22] The ECJ found that there was an incompatibility in a situation in which the BIT did not contain a provision allowing the Member State to exercise its rights and to fulfil its obligations and in which there was no international law mechanism which made that possible.[23] The ECJ noted that the Member States' measures did not fulfil their Community obligations. First, the time involved in any

[18]See, for example, Articles 47(2), 48 and 56–60 EC.

[19]See ECJ, Opinion 2/92, *OECD*, [1995] ECR I, 521.

[20]To the author's knowledge, the new Denmark–Indonesia BIT has not yet entered into force. Whereas the BIT does not require ratification by the Danish Parliament, it still appears to be awaiting ratification by Indonesia.

[21]ECJ, C-205/06, *Commission v. Austria*, not yet in the official reports, para. 26; ECJ, C-249/06, *Commission v. Sweden*, not yet in the official reports, para. 27.

[22]ECJ, C-205/06, *Commission v. Austria*, not yet in the official reports, para. 36; ECJ, C-249/06, *Commission v. Sweden*, not yet in the official reports, para. 37.

[23]ECJ, C-205/06, *Commission v. Austria*, not yet in the official reports, para. 37; ECJ, C-249/06, *Commission v. Sweden*, not yet in the official reports, para. 38.

international negotiations which would be required to reopen discussion of the BITs was incompatible with the practical effectiveness of measures to restrict the free movement of capital.[24] Second, international law mechanisms such as suspension or termination of the BITs or of some of their provisions were “too uncertain [. . .] to guarantee that the measures adopted by the Council could be applied effectively”.[25]

The ECJ concluded that Austria and Sweden by not having taken appropriate steps to eliminate incompatibilities concerning the provisions on transfer of capital contained in the BITs at issue failed to fulfil their obligations under Article 307(2) EC. The ECJ did not indicate what consequences such failure would have. According to the ECJ’s jurisprudence, once there is an incompatibility, there is an obligation under Article 307 EC to terminate incompatible prior international agreements. This obligation was reinforced by the ECJ in *Kadi and Al Barakaat*. In these joined cases, the court acknowledged that it had previously recognised that Article 307 EC “could, if the conditions for application have been satisfied, allow derogations from even primary law, for example from [Article 133 of the EC Treaty] on the common commercial policy.”[26] It then, however, went on to observe that “Article 307 EC may in no circumstances permit any challenge to the principles that form part of the very foundations of the Community legal order [. . .].”[27]

Importantly, in the BIT infringement cases the court noted that the incompatibilities with the EC Treaty to which the BITs with third states give rise are not limited to the Member States which were defendants in these cases. Put differently, although the ECJ explicitly stated that the BITs violate Article 307 EC, all BITs of Member States with third states that contain similar free movement of capital clauses violate EU law. In the case against Finland the ECJ clarified the required scope of such a provision. Finland had argued that a clause with the following wording would ensure compliance with Community law: “Every contracting party guarantees under all circumstances, within the limits authorised by its own laws and decrees and in conformity with international law, a reasonable and appropriate treatment of investments made by citizens or companies of the other Contracting Party.”[28] The ECJ acknowledged Finland’s argument that restrictive measures adopted on the basis of Articles 57(2), 59 and 60 EC form part of the Finnish legal order.[29] However, the court ultimately found that since the interpretation of

[24]ECJ, C-205/06, *Commission v. Austria*, not yet in the official reports, para. 39; ECJ, C-249/06, *Commission v. Sweden*, not yet in the official reports, para. 40.

[25]ECJ, C-205/06, *Commission v. Austria*, not yet in the official reports, para. 40; ECJ, C-249/06, *Commission v. Sweden*, not yet in the official reports, para. 41.

[26]ECJ, Joined Cases C-402/05 P and C-415/05 P, *Kadi and Al Barakaat*, not yet in the official reports, para. 301.

[27]ECJ, Joined Cases C-402/05 P and C-415/05 P, *Kadi and Al Barakaat*, not yet in the official reports, para. 304.

[28]ECJ, C-118/07, *Commission v. Finland*, not yet in the official reports, para. 5.

[29]ECJ, C-118/07, *Commission v. Finland*, not yet in the official reports, para. 38.

those provisions was too uncertain, they are not sufficient to ensure compatibility of the BITs with Community law.[30]

Austria, Finland and Sweden ultimately may have to terminate the challenged BITs, even if termination should be considered an *ultima ratio*. Therefore, the immediate consequence will be felt by these Member States.[31] Because their efforts to amend these BITs had not been successful up until the commencement of the infringement proceedings, it seems unlikely that they will be able to do so in the foreseeable future. Thus, they may be forced to terminate these BITs.[32] In the light of the ECJ's reasoning, however, the intermediate-term consequences may well be felt not only by some, but by all Member States. BITs of Member States that do not contain a provision allowing them to exercise their rights and to fulfil their obligations under EU law (a so-called REIO clause) violate EU law. Although more recent BITs tend to contain such a clause, there are numerous BITs of Member States with third states in force that do not contain such a clause or a clause that does not adequately take into account Member States' obligations under EU law.[33] Potentially, therefore, numerous BITs of all Member States may be challenged by the Commission in infringement proceedings before the ECJ.

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[30]ECJ, C-118/07, *Commission v. Finland*, not yet in the official reports, paras. 42 and 43.

[31]Typically, the BITs at issue remain in force for a further period of 10 years (see, for example, Article 12(3) of the Austria-Turkey BIT, signed on 16 September 1988, entered into force on 1 January 1992, available at http://www.unctad.org/sections/dite/iia/docs/bits/austria_turkey_ger.pdf) to 20 years (see, for example, Article 11(3) of the Sweden-Vietnam BIT, signed on 8 September 1993, entered into force on 2 August 1994, available at http://www.unctad.org/sections/dite/iia/docs/bits/sweden_vietnam.pdf) from the date when the termination of the BIT becomes effective in respect of investments made prior to the effective termination date. However, investments of, say, Austrian investors in Turkey after the termination of the Austria–Turkey BIT would not be protected under the BIT until the entry into force of a new BIT.

[32]There is no exact timeframe until when such termination has to take place. However, if Member States do not comply with ECJ judgments, the Commission may institute proceedings under Article 260 TFEU (equivalent to Article 228 EC) for non-compliance. According to the ECJ's jurisprudence, it has no jurisdiction under this article to require Member States to comply with its judgment within a specified period of time. ECJ, C-473/93, *Commission v. Luxembourg*, [1996] ECR I, 3207, paras. 46 and 47. However, although Article 260 TFEU does not specify the period within which a judgment must be complied with, the ECJ ruled that the interest in the immediate and uniform application of Community law required compliance as soon as possible. ECJ, C-291/93, *Commission v. Italy,* [1996] ECR I, 859, para. 6. Judgments in proceedings pursuant to the said article may well result in hefty fines for Member States; see ECJ, C-304/02, *Commission v. France,* [2005] ECR I, 6263. However, under Article 260 TFEU the court does not have the power either to seek an injunction or to order a Member State to take specific action. ECJ, C-105/02, *Commission v. Germany,* [1996] ECR I, 9659, paras. 44 and 45.

[33]It would seem that a clause such as the one contained in Article 7(c) of the most recent UK Model BIT of 2005 ("The provisions of this Agreement relative to the grant of treatment not less favourable than that accorded to the nationals or companies of either Contracting Party or of any third State shall not be construed so as to oblige one Contracting Party to extend to the nationals or companies of the other the benefit of any treatment, preference or privilege from any requirements of European Community law resulting from the United Kingdom's membership of the European Union prohibiting, restricting or limiting the movement of capital to or from any third country.") might be interpreted so as to comply with the UK's obligations under EU law even

The EU's FDI Competence under the Treaty of Lisbon

Limitation to FDI

The extension of the CCP under the Treaty of Lisbon has one significant limitation: the EU competence is limited to foreign *direct* investment (FDI).[34] Thus, agreements which cover forms of investment other than FDI are not covered by the exclusive EU competence. The TFEU, however, does not define the term "direct investment." Neither was the term defined in the EC Treaty. The term is referred to in Article 64 TFEU (equivalent to Article 57 EC). The explanatory notes of Council Directive 88/361/EEC, the secondary legislation passed with respect to Article 57 EC, define the term in the following way: "Investments of all kinds by natural persons or commercial, industrial or financial undertakings, and which serve to establish or to maintain lasting and direct links between the person providing the capital and the entrepreneur to whom or the undertaking to which the capital is made available in order to carry on an economic activity. This concept must therefore be understood in its widest sense."[35] Annex I to Directive 88/361/EEC gives some examples for direct investments such as "[e]stablishment and extension of branches or new undertakings belonging solely to the person providing the capital, and the acquisition in full of existing undertakings," "[p]articipation in new or existing undertakings with a view to establishing or maintaining lasting economic links,"[36] "[l]ong-term loans with a view to establishing or maintaining

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though it remains unclear why this provision limits its scope of application to treatment not less favourable.

[34] In the draft articles of the Convention's Praesidium it was explained that FDI was included in the scope of the CCP "in recognition of the fact that financial flows supplement trade in goods and today represent a significant share of commercial exchanges." European Convention, draft articles on external action in the Constitutional Treaty, CONV 685/03. The Treaty of Lisbon did not change the Constitutional Treaty's provisions in respect of the EU's competence for FDI, which is why the Convention's deliberations are a useful point of reference for the interpretation of the EU's competence for FDI.

[35] Council Directive 88/361/EEC of 24 June 1988 for the implementation of Article 67 of the Treaty, OJ 1988 L 178/5. The ECJ has endorsed this definition of direct investment. See ECJ, C-446/04, *Test Claimants in the FII Group Litigation,* [2006] ECR I, 11753, paras. 179–182; ECJ, C-157/05, *Holböck*, [2007] ECR I, 4051, paras. 33 and 34; ECJ, C-112/05, *Commission v. Germany*, [2007] ECR I, 8995, para. 18; ECJ, C-101/05, *Skatteverket v. A,* [2007] ECR I, 11531, para. 46.

[36] According to the explanatory notes "there is participation in the nature of direct investment where the block of shares held by a natural person of another undertaking or any other holder enables the shareholder, either pursuant to the provisions of national laws relating to companies limited by shares or otherwise, to participate effectively in the management of the company or in its control." Council Directive 88/361/EEC of 24 June 1988 for the implementation of Article 67 of the Treaty, OJ 1988 L 178/5.

lasting economic links"[37] and "[r]einvestment of profits with a view to maintaining lasting economic links."[38]

The ECJ summarised the scope of direct investment in the following terms: "[T]he concept of direct investments concerns investments of any kind undertaken by natural or legal persons and which serve to establish or maintain lasting and direct links between the persons providing the capital and the undertakings to which that capital is made available in order to carry out an economic activity. As regards shareholdings in new or existing undertakings [. . .] the objective of establishing or maintaining lasting economic links presupposes that the shares held by the shareholder enable him, either pursuant to the provisions of the national laws relating to companies limited by shares or otherwise, to participate effectively in the management of that company or in its control."[39] The ECJ also ruled that a participation of 25% constitutes direct investment. At the same time, the ECJ was willing to adopt a flexible approach.[40] Overall, however, it is not entirely clear what "effective management" or "control" of a company means under EU law.

It seems therefore sensible to look at other definitions of the term "direct investment" in international legal instruments. Notably, the IMF defines FDI as "an incorporated or unincorporated enterprise in which a direct investor, who is resident in another economy, owns 10 percent or more of the ordinary shares or voting power (for an incorporated enterprise) or the equivalent (for an unincorporated enterprise)."[41] Similarly, pursuant to the OECD's definition, FDI is characterised by a long-term participation of at least 10% in a foreign enterprise.[42] Consequently, there appear to be good reasons why FDI means participation in a company through an investment of at least 10% in that company.[43]

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[37]The explanatory notes explain that the term "long-term loans" means "loans for a period of more than 5 years which are made for the purpose of establishing or maintaining lasting economic links. The main examples which may be cited are loans granted by a company to its subsidiaries or to companies in which it has a share and loans linked with a profit-sharing arrangement. Loans granted by financial institutions with a view to establishing or maintaining lasting economic links are also included under this heading." Council Directive 88/361/EEC of 24 June 1988 for the implementation of Article 67 of the Treaty, OJ 1988 L 178/5.

[38]See also ECJ, C-463/00, *Commission v. Kingdom of Spain*, [2003] ECR I, 4581.

[39]ECJ, C-446/04, *Test Claimants in the FII Group Litigation,* [2006] ECR I, 11753, paras. 181 and 182.

[40]ECJ, C-492/04, *Lasertec,* [2007] ECR I, 3775, paras. 22–24.

[41]IMF, *Balance of Payments Manual*, (5th ed.) 1993, p. 86.

[42]OECD, *Benchmark Definition of Foreign Direct Investment*, 1999 (3rd edition), p. 7.

[43]Tietje, Die Außenwirtschaftsverfassung der EU nach dem Vertrag von Lissabon, in: Tietje/Kraft (eds); *Beiträge zum Transnationalen Wirtschaftsrecht, Heft 83*, 2009, p. 16 (discussing systematic problems with this interpretation).

Further Limitations to the EU's FDI Competence?

The wording of Article 207 TFEU does not contain any further limitation to the EU competence. Some commentators, however, argue that further restrictions to the EU's competence would apply. For example, it has been argued that the EU's competence would be limited in a sense that FDI has to be connected to international trade law. This limitation would be justified because the CCP traditionally concerned trade agreements and because the Convention deliberations would support such a reading.[44] But it is unclear why the traditional scope of the CCP should limit the EU competence for FDI. Rather, it would seem that precisely because the drafters intended to broaden the EU competence, such a limitation can hardly be justified.[45] Indeed, the Convention deliberations show that several representatives proposed the exclusion of FDI from the draft chapter on the CCP.[46] One representative emphasised the need for a clarification in the treaty to the extent it was not the intention to remove the competence of Member States to conduct bilateral investment activity.[47] No clarification, however, was made. Neither was any limitation included. This reinforces the view that the EU's competence is not limited to the extent that FDI has to be connected to international trade law.

Another possible limitation may flow from the parallelism clause contained in Article 207(6) TFEU which reads as follows: "The exercise of the competences conferred by this Article in the field of the common commercial policy shall not affect the delimitation of internal competences between the Union and the Member States, and shall not lead to harmonisation of legislative or regulatory provisions of Member States insofar as the Treaties exclude such harmonisation." The most important question with regard to international investment law is to what extent this clause may limit the scope of investment treaties which the EU is competent to conclude. It has been argued that by virtue of Article 207(6) TFEU substantive treatment standard provisions against expropriation would be excluded from the

[44] Krajewski, External Trade Law and the Constitution Treaty: Towards a Federal and more Democratic Common Commercial Policy? CMLR 42 (2005) 1, p. 91 (113–114).

[45] The fact that Article 207 TFEU, unlike Article 133 EC, does not distinguish between trade in goods and other areas of the CCP supports the view that the Treaty of Lisbon put an end to the traditional approach of the CCP which henceforth expands towards other areas of economic activity.

[46] Fischer, Amendment Form: Suggestion for amendment of Article: 24, available at http://european-convention.eu.int/Docs/Treaty/pdf/866/Art24Fischer.pdf; De Villepin, Fiche Amendement: Proposition d'amendement à l'article III-211, available at http://european-convention.eu.int/Docs/Treaty/pdf/866/Art%20III%20211%20de%20Villepin%20FR.pdf; Palacio, Fiche Amendement: Proposition d'amendement à l'Article: 23: Chapitre 2, Titre B, Partie, available at http://european-convention.eu.int/Docs/Treaty/pdf/866/Art23Palacio%20FR.pdf.

[47] Hain, Amendment Form: Suggestion for amendment of Article: Part II, Title B, Article 23, available at http://european-convention.eu.int/Docs/Treaty/pdf/866/Art23Hain.pdf.

EU's competence.[48] Indeed, Article 345 TFEU (equivalent to Article 295 EC) states that "[t]he Treaties shall in no way prejudice the rules in Member States governing the system of property ownership." But the better interpretation of this article is that it does not preserve exclusive powers for Member States to determine expropriation. According to the ECJ's settled case law, the right to property is one of the general principles of Community law. However, it is not absolute, but must be viewed in relation to its social function. The exercise of the right to property may be restricted, provided that those restrictions in fact correspond to objectives of general interest pursued by the Community and do not constitute in relation to the aim pursued a disproportionate and intolerable interference, impairing the very substance of the rights guaranteed.[49] More specifically, the ECJ has interpreted Article 295 EC narrowly so that its scope does not reserve for Member States the power to decide the conditions under which an expropriation takes place.[50] In *Kadi and Al Barakaat*, the court emphasised that even temporary measures which entail a restriction of the exercise of the right to property need to be justified under Community law. There must exist a reasonable relationship of proportionality between the means employed and the aim sought to be realised.[51] There is one more reason why expropriation is covered by the EU's competence for FDI. Before the Treaty of Lisbon was opened for signature, a footnote to Article 207 TFEU excluded expropriation from the scope of the reference to FDI.[52] The footnote, however, does not appear in the final text of the Treaty of Lisbon. For these reasons, the better view is that the EU competence extends to expropriation.

Neither does the parallelism clause in Article 207(6) TFEU mean that the lack of exercise of EU internal competence limits the existence or the exercise of EU external competence. As said, the drafters of the treaty deliberately extended the scope of the CCP to all sectors of the service economy. To interpret the clause as a limitation to the external and internal competences of the EU would limit the EU's external competences. Such an interpretation would contradict the express intention of the drafters of the treaty. Therefore, the better interpretation is that Article 207(6) TFEU may limit the internal, but not the external competence of the EU. As a consequence, the EU's external competence extends beyond the scope of the

[48]Ceyssens, Towards a Common Foreign Investment Policy? – Foreign Investment in the European Constitution, Legal Issues of Economic Integration 32 (2005) 3, p. 259 (279–281); Tietje, Die Außenwirtschaftsverfassung der EU nach dem Vertrag von Lissabon, in: Tietje/Kraft (eds.), *Beiträge zum Transnationalen Wirtschaftsrecht, Heft 83*, 2009, p. 14–15.

[49]ECJ, C-306/93, *SMW Winzersekt,* [1994] ECR I, 5555, para. 22; ECJ, Joined Cases C-37/02 and C-38/02, *Di Lenardo and Dilexport*, [2004] ECR I, 6911, para. 82; ECJ, C-347/03, *Regione autonoma Friuli-Venezia Giulia and ERSA*, [2005] ECR I, 3785, para. 119; ECJ, Joined Cases C-402/05 P and C-415/05 P, *Kadi and Al Barakaat*, not yet in the official reports, para. 355.

[50]See ECJ, 4/73, *Nold,* [1974] ECR 491; ECJ, C-84/95, *Bosphorus*, [1996] ECR I, 3953.

[51]ECJ, Joined Cases C-402/05 P and C-415/05 P, *Kadi and Al Barakaat*, not yet in the official reports, paras. 358 and 360.

[52]In addition, this footnote also excluded investor–state arbitration from the EU's FDI competence.

internal competence.[53] This interpretation is in line with the jurisprudence of the ECJ[54] and Article 3(2) TFEU.[55] An external competence may exist without a parallel internal competence.

In conclusion, under the Treaty of Lisbon the EU is competent to conclude comprehensive investment treaties. The competence covers market access, pre- and postestablishment standards of treatment, performance requirements, investor–state dispute settlement provisions and the terms of the conditions under which expropriation may take place.[56] The major apparent limitation of the EU's competence results from the term "foreign direct investment" (FDI). Because of this limitation, the EU's competence does not cover portfolio investments. The limitation is mitigated owing to the broad interpretation which should be given to this term. Nevertheless, owing to this limitation, investment treaties that cover all forms of investments will have to be concluded as mixed agreements. Mixed agreements have to be ratified by the EU and all 27 Member States. Therefore, the EU and its Member States will have to sign and ratify agreements with coverage beyond the exclusive EU competence for FDI.[57] In the process of negotiation, conclusion and application of mixed agreements, Member States are bound by the duty of cooperation. They are under a duty, if not to abstain from action, at the very least to

[53] Krajewski, External Trade Law and the Constitution Treaty: Towards a Federal and more Democratic Common Commercial Policy? CMLR 42 (2005) 1, p. 91 (116–117).

[54] ECJ, Case 22/70, *AETR*, [1971] ECR 263; ECJ, Opinion 1/75, *Local Costs*, [1975] ECR 1355.

[55] Article 3(2) TFEU states: "The Union shall also have exclusive competence for the conclusion of an international agreement when its conclusion is provided for in a legislative act of the Union or is necessary to enable the Union to exercise its internal competence, or in so far as its conclusion may affect common rules or alter their scope".

[56] It should not be overlooked that the EU's action on the international scene has to respect some non-economic principles enshrined in Article 21 TEU. Article 21(1) TEU states: "The Union's action on the international scene shall be guided by the principles which have inspired its own creation, development and enlargement, and which it seeks to advance in the wider world: democracy, the rule of law, the universality and indivisibility of human rights and fundamental freedoms, respect for human dignity, the principles of equality and solidarity, and respect for the principles of the United Nations Charter and international law." Further, Article 21(2) TEU states: "The Union shall define and pursue common policies and actions, and shall work for a high degree of cooperation in all fields of international relations, in order to [inter alia] foster the sustainable economic, social and environmental development of developing countries, with the primary aim of eradicating poverty; [. . .] help develop international measures to preserve and improve the quality of the environment and the sustainable management of global natural resources, in order to ensure sustainable development; [. . .]." It is unclear, however, to what extent these principles may in effect limit the EU's competence to conclude investment treaties with third states.

[57] As far as negotiation is concerned, the division of competence under a mixed agreement does not, generally, influence participation in negotiations. Although the practice is decided on a case-by-case-basis, it is accepted that the Commission may act as a sole negotiator for the whole agreement according to the mandate given to it by the Council. See Craig/de Burca, *EU Law*, 2008, pp. 198–199. See also Article 218 TFEU. On the problems with regard to mixed agreements generally see, for example, Weiler, The External Legal Relations of Non-Unitary Actors: Mixity and the Federal Principle, in: Weiler (ed.), *The Constitution of Europe: Do the New Clothes Have an Emperor?*, 1999, pp. 168–183.

cooperate closely with the EU's institutions to "facilitate the achievement of the [Union] tasks and to ensure the coherence and consistency of the action and its international representation."[58] Consequently, the result of the vertical allocation of competences under the Treaty of Lisbon may be an increased cooperation on foreign investment policy between the EU and the Member States.

Consequences of the EU's FDI Competence for the BITs of Member States and European Foreign Investment Policy

Upon the entry into force of the Treaty of Lisbon, existing BITs of Member States with third states remain valid under international law.[59] Further, without further qualification, these BITs are compatible with EU law since they were concluded before the new EU competence for FDI entered into force and thus do not violate the vertical allocation of competences between the EU and its Member States. The issue of compatibility with EU law cannot arise because the supervening external EU competence in matters previously regulated by BITs of Member States does not suffice in itself to render those agreements incompatible with the rules and principles governing the division of powers.[60] However, under Article 351(2) TFEU (equivalent to Article 307(2) EC) Member States will be under an obligation to terminate these BITs. Following the ECJ's judgments in the infringement cases and the entry into force of the Treaty of Lisbon, it remains to be seen whether the Commission will move on to challenge comprehensively the compatibility of BITs between Member States and third states with EU law. Until the Commission does, from its point of view, successfully challenge these BITs, they will remain in force, at least until the EU exercises its new competence in this field under the Treaty of Lisbon. Thus, investors may rely upon and commence arbitration under such BITs.

It is important to note that the Treaty of Lisbon does not contain a provision that would recognise the right of Member States to keep in place their existing agreements.[61] Neither does the Treaty of Lisbon contain a transition period. To that extent, the situation is different from the situation upon the full entry into force of the CCP. Then, two Council decisions were issued. The Council Decision of

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[58]ECJ, C-266/03, *Commission v. Luxembourg,* [2005] ECR I, 4805, para. 60; ECJ, C-433/03, *Commission v. Germany,* [2005] ECR I, 6985, para. 66; ECJ, C-459/03, *Commission v. Ireland,* [2006] ECR I, 4635, para. 174. The principle of cooperation can be seen as a constitutional principle within EU external relations law. See Koutrakos, The Elusive Quest for Uniformity in EC External Relations, Yearbook of European Law 4 (2001), p. 243 (258).

[59]Compare Eeckhout, *External Relations of the European Union*, 2004, p. 335; but see Manzini, The priority of pre-existing treaties of EC Member States within the framework of international law, EJIL 12 (2001) 4, p. 781 (785).

[60]ECJ, C-466/08, *Commission v. United Kingdom,* Opinion of AG Tizzano [2002], ECR I, 9427, para. 113.

[61]Again, it should be emphasised that most BITs contain post-termination protection clauses.

9 October 1961 set out the guidelines on the duration of trade agreements with third states in light of the transitional period of 12 years under Article 111 EEC combined with Article 8 Treaty EEC. Article 1 of the Council Decision prohibited Member States from concluding trade agreements with third states beyond the transitional period. Article 2 provided for a default rule of a 1-year termination period for agreements which neither foresaw the entry into force of the CCP nor allowed for an "annual notice of termination." Article 3 determined the joint examination by Member States and the Commission of the Member States' international agreements to ensure "that they [did] not constitute an obstacle to introduction of the common commercial policy provided for in the Treaty." Finally, Article 4 stated that the Member States, in consultation with the Commission, shall arrange that the terminal dates of their agreements with third states coincide.[62] A second decision, the Council Decision of 29 December 1969, shows that some flexibility in the regime set out in the previous Council Decision was adopted. In particular, Article 3 of this Council Decision stated that if the Member State instrument did not constitute an obstacle to the implementation of the CCP, the Commission may propose to the Council that the Member State concerned be authorised, by way of derogation from Article 1 of the Council Decision of 9 October 1961, to extend, expressly or tacitly, for a period to be specified, the provisions in question of agreements of Member States.[63]

It may well be that these Council decisions of 1961 and 1969 will be used as a template to set time limits and guidelines for the termination and/or renegotiation of BITs of Member States with third states, even if the Treaty of Lisbon does not contain a transition period to that effect. Another possibility in the transitory stage of transfer of competence would be to conclude an EU investment framework agreement with third states while leaving details to the individual Member States. Such a framework agreement would lay down the basic conditions of investment protection with a third state, whereas the necessary details concerning the actual investment guarantees may be better agreed by the Member State and the third state in question. There are also precedents for the application of this latter model, which has sometimes been called the Community's multilevel governance reflected in a multilevel conclusion of international agreements.[64]

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[62]Council Decision of 9 October 1961 on standardisation of the duration of trade agreements with third countries, OJ 1961 71/1274.

[63]Council Decision of 16 December 1969 on the progressive standardisation of agreements concerning commercial relations between Member States and third countries and on the negotiation of Community agreements (69/494/EEC), OJ 1969 L 326/42.

[64]See, for example, the example of readmission agreements described by Kuijper, Fifty Years of EC/EU External Relations: Continuity and the Dialogue Between Judges and Member States as Constitutional Legislators, Fordham International Law Journal 31 (2008) 6, p. 1571 (1597). In the context of international trade see, for example, Petersmann, Multilevel Judicial Governance of International Trade Requires a Common Conception of Rule of Law and Justice, Journal of International Economic Law 10 (2007) 3, p. 529 (551).

Yet another possibility would be to look at treaty partners individually and conclude an EU investment treaty only in selected cases. For example, in the case of aviation policy, one outcome of the ECJ's AETR jurisprudence was that the new "Open Skies" agreement with the USA was concluded as a mixed agreement.[65] Contrarily, aviation agreements with smaller treaty partners, in which only a few Member State carriers would be interested, could be left to these Member States, constrained by some principle rules of Community law laid down in a regulation.[66] To be sure, an approach used in one policy area may not be equally suitable for another policy area because the economics, the history and any other factors are different. But such an approach may nevertheless be useful and be it for the consistency and coherence of the EU's external relations policy alone. Further, it may well be that the EU will face severe practical constraints in the exercise of its new competence for FDI under the Treaty of Lisbon. In this context, it would seem unlikely that the EU has the resources to enter into BIT negotiations with third states on a broad scale. Rather, it would seem more likely that the EU focuses on selected third states, thereby adopting a piecemeal approach.

In the end, from an EU policy perspective, an enhanced EU competence is to be welcomed because the negotiating power of the Commission is likely to be stronger than that of individual Member States, in particular smaller ones. A strengthened EU competence will also contribute to the development of an integrated policy approach concerning trade and investment. As was recognised by the drafters of the Constitutional Treaty (and thus, by implication the drafters of the Treaty of Lisbon), there are strong linkages between these two areas and an increased EU competence for investment might make it easier for the EU to conclude combined international agreements on trade and investment. Indeed, the main rationale for including investment into the CCP was to strengthen the EU as an actor in multilateral negotiations on foreign investment.[67] Thereby, the drafters followed a proposal which the Commission has made for many years.[68]

An extension of the CCP to investment will also lead to efficiency gains, since an investment treaty between the EU and a third state will cover 27 Member States at once. The multiplying effect will be particularly beneficial for those Member States with few BITs.[69] An EU competence for investment will also reduce distortions

[65]See Council Decision No. 2007/339/EC, OJ 2007 L 134/1.

[66]See Council Regulation No. 847/2004, OJ 2004 L 157/7.

[67]European Convention, Draft Articles on external action in the Constitutional Treaty, CONV 685/03.

[68]The Commission made proposals to that effect for example during the intergovernmental conferences leading to the Treaty of Amsterdam and the Treaty of Nice. See European Commission, Report on the operation of the Treaty on European Union, SEC (95) 731, 57–60 and European Commission, Commission Opinion in accordance with Article 48 EU, COM (2000) 34, 27.

[69]On the other hand, Member States might have different priorities in the respective third state, depending how extensively their investors are engaged in that state and how strongly they are

between EU investors in third states through replacing the existing BITs of Member States with EU BITs. This will remedy a comparative advantage which a few Member States enjoy compared with other Member States. Such competence will also improve the transparency at the global level, as the total number of BITs will be reduced significantly. A common EU investment policy will further increase the attractiveness of the EU as a location for FDI from third states because a harmonised investment scheme on an EU level will create an equal level playing field for foreign investors in the EU. Economies with more transparent trade and FDI regimes attract more FDI compared with those economies with less transparent trade and FDI regimes.[70]

But even upon the entry into force of the Treaty of Lisbon, the continued fragmentation of competences between the EU and its Member States, in particular due to the limitation of the EU competence to FDI under the Treaty of Lisbon, is likely to cause confusion both within the EU and with the EU's treaty partners. Because the EU's exclusive competence to conclude investment treaties with third states only covers FDI, and does not cover portfolio investments, BITs comparable to the US Model BIT covering all kinds of investments will have to be concluded as mixed agreements. On the other hand, if the EU were to conclude BITs with third states alone, without the involvement of Member States, the most significant problem would be Article 67 of the International Centre for Settlement of Investment Disputes (ICSID) Convention. The ICSID is the most important arbitral institution in the field of investment disputes. The availability of the ICSID presents numerous advantages for the settlement of investment disputes.[71] According to its Article 67, the ICSID Convention is open "for signature on behalf of States members of the Bank." Notably, the ICSID Convention is not open for signature for a supranational organisation such as the EU. It is doubtful, at least, whether Article 67 of the ICSID Convention would allow for the EU to sign "on behalf of States." Rather, it would seem that the EU cannot become a member of the ICSID Convention. Until and unless it may do so, however, the EU may not offer its treaty

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interested in attracting investors from there. Individual Member States may also have different preferences for political and historical reasons. See the discussion by Karl, The Competence for Foreign Direct Investment – New Powers for the European Union, JWIT 5 (2004) 3, p. 413 (425–426).

[70]Drabek/Payne, The Impact of Transparency on Foreign Direct Investment, World Trade Organization Economic Research and Analysis Division Staff Working Paper ERAD-99-02, available at http://www.wto.org/english/res_e/reser_e/erad-99-02.doc.

[71]For example, the rules of procedure for arbitral proceedings are specifically tailored for arbitration with the participation of a government party; oversight by the ICSID Secretariat and the availability of the institution's resources and experienced personnel represent a major asset in investment arbitration; and the self-contained enforcement regime of the ICSID Convention means that enforcement of ICSID awards will generally be smoother than enforcement of non-ICSID awards. See McLachlan/Shore/Weiniger, *International Investment Arbitration*, 2007, pp. 4–5; Muchlinski, Policy Issues in: Muchlinski/Ortino/Schreuer (eds.), *The Oxford Handbook of International Investment Law*, 2008, pp. 4–48; Dolzer/Schreuer, *Principles of International Investment Law*, 2008, pp. 20–21; Schreuer/Malintoppi/Reinisch/Sinclair, *The ICSID Convention – A Commentary*, (2nd ed.) 2009, pp. 1117–1150.

partners to arbitrate under the ICSID arbitration rules. Moreover, according to Article 66(1) ICSID Convention, each amendment to the ICSID Convention requires that all Contracting States have ratified, accepted or approved the amendment. Therefore, in practice such an amendment is unlikely. Potentially, the non-availability of the ICSID dispute settlement mechanism may be a drawback for investors protected only under an EU investment treaty.

The Internal Dimension: The Future of Intra-EU BITs

On 27 March 2007, an arbitral tribunal constituted under the authority of the Arbitration Institute of the Stockholm Chamber of Commerce issued a partial award in the matter of an ad hoc arbitration in the case *Eastern Sugar B.V. (Netherlands) v. The Czech Republic*.[72] The tribunal quoted extensively from a letter by the Commission Directorate-General Internal Market and Services of 13 January 2006 (2006 Letter) and a note by Commission Directorate-General Internal Market and Services of November 2006 (2006 Note). In the end, the tribunal rejected the Czech Republic's objections to the tribunal's jurisdiction. At heart, the tribunal rejected the Czech Republic's argument that the applicable BIT in force between the Netherlands and the Czech Republic ("Netherlands–Czech Republic BIT")[73] would not be applicable after the accession of the Czech Republic to the EU. The tribunal held that therefore, "the BIT, including its arbitration clause, is still in force".[74]

In *Eastern Sugar* the Czech Republic did not argue that the Netherlands–Czech Republic BIT had been expressly terminated. Rather, it invoked Article 59(1) of the Vienna Convention on the Law of Treaties (VCLT)[75] and argued that the BIT was

[72] *Eastern Sugar B.V. (Netherlands) v. The Czech Republic,* Partial Award of 27 March 2007, available at http://ita.law.uvic.ca/documents/EasternSugar.pdf. The Final Award dated 12 April 2007 dealt merely with the arbitration costs, available at http://ita.law.uvic.ca/documents/FinalAward_EasternSugar.pdf.

[73] Agreement on encouragement and reciprocal protection of investments between the Kingdom of the Netherlands and the Czech and Slovak Federal Republic, signed on 29 April 1991, entered into force on 1 October 1992. As of 1 January 1993 the Czech Republic succeeded into the Czech and Slovak Federal Republic's international obligations, including those arising from the BIT.

[74] *Eastern Sugar B.V. (Netherlands) v. The Czech Republic,* Partial Award of 27 March 2007, para. 172.

[75] Article 59 VCLT ("Termination or suspension of the operation of a treaty implied by conclusion of a later treaty") states: "1. A Treaty shall be considered as terminated if all the parties to it conclude a later treaty relating to the same subject matter and: (a) it appears from the later treaty or is otherwise established that the parties intended that the matter should be governed by that treaty; or (b) the provisions of the later treaty are so far incompatible with those of the earlier one that the two treaties are not capable of being applied at the same time. 2. The earlier treaty shall be considered as only suspended in operation if it appears from the later treaty or is otherwise established that such was the intention of the parties".

not applicable beyond the Czech Republic's accession to the EU, i.e. beyond 1 May 2004. The Czech Republic was of the view that the BIT should be considered as terminated following its accession to the EU and that Dutch investments in the Czech Republic should be governed by Community law. As of the date of its accession to the EU, the intra-EU investment regime would supersede the obligations in the BIT.[76] Moreover, if earlier treaties survived after its accession to the EU, this might distort the principle of equality of treatment.[77] The application of the BIT would also breach the principle of mutual trust. This principle would imply that Eastern Sugar would have to bring its claim before a Czech national court. There would be no room for international arbitration in this area. The Czech Republic concluded that the BIT was not applicable and that the arbitral tribunal did not have jurisdiction.[78]

The tribunal quoted extensively from the 2006 Letter. The 2006 Letter noted that the date of the Czech Republic's accession to the EU was the decisive date. For facts occurring after accession, the BIT was not applicable to matters falling under Community competence. The Commission stated: "Only certain residual matters, such as diplomatic representation, expropriation and eventually investment promotion, would appear to remain in question. Therefore, where the EC Treaty or secondary legislation are in conflict with some of these BITs' provisions - or should the EU adopt such rules in the future - Community law will automatically prevail over the non-conforming BIT provisions. [. . .] intra-EU BITs should be terminated in so far as the matters fall under Community competence. However, the effective prevalence of the EU *acquis* does not entail, at the same time, the automatic termination of the concerned BITs or, necessarily, the non-application of all their provisions. Without prejudice to the primacy of Community law, to terminate these agreements, Member States would have to strictly follow the relevant procedure for this in regard in the agreements themselves."[79]

With regard to dispute settlement procedures between Member States, the 2006 Letter observed that Member States, in the light of Article 292 EC,[80] cannot apply the dispute settlement procedures in the BIT insofar as the dispute concerns a matter falling under Community competence. With regard to investor–state

[76] *Eastern Sugar B.V. (Netherlands) v. The Czech Republic,* Partial Award of 27 March 2007, paras. 101–104.

[77] In *Matteucci v. Belgium* the ECJ concluded that "[a] bilateral agreement which reserves the scholarships in question for nationals of the two Member States which are the parties to the agreement cannot prevent the application of the principle of equality of treatment between national and Community workers established in the territory of one of those two Member States." ECJ, 235/87, *Matteucci v. Begium,* [1988] ECR, 5589, para. 23.

[78] *Eastern Sugar B.V. (Netherlands) v. The Czech Republic,* Partial Award of 27 March 2007, paras. 106–108.

[79] *Eastern Sugar B.V. (Netherlands) v. The Czech Republic,* Partial Award of 27 March 2007, para. 119.

[80] Article 292 EC (= Article 344 TFEU) states: "Member States undertake not to submit a dispute concerning the interpretation or application of this Treaty to any method of settlement other than those provided for therein".

dispute settlement, the Commission stated: "Since Community law prevails from the time of accession, the dispute should be decided on basis of Community law (which indirectly also follows from Article 8(6) first bullet point in the agreement between the Czech Republic and the Netherlands).[81] However, it may be argued that the private investor could continue to rely on the settlement procedures provided for in the agreement until formal termination of the BIT if the dispute concerns facts which occurred before accession."[82]

The *Eastern Sugar* tribunal found the 2006 Letter "for the most part diplomatic and ambiguous."[83] Although the tribunal was right to emphasise that it was not bound by the 2006 Letter, some of its reasoning lacks support. The tribunal's notion that the Commission "did not start infringement proceedings against the Netherlands and the Czech Republic and other Member States for failure to terminate their BITs"[84] does not support its position. It is well established that the Commission has a *right*, but *no obligation* to commence infringement proceedings against Member States. In fact, the Commission has substantial leeway to commence proceedings against Member States and the discretion of the Commission is not even subject to judicial review.[85] Similarly, the tribunal's observation that "neither the Czech Republic nor the Netherlands, nor anybody else, did file a complaint to the European Commission, against the Netherlands and the Czech Republic"[86] does not support its position, as there is no obligation of Member States or "anybody else" to that effect.

In the 2006 Note, the Commission reiterated its view, expressed in the 2006 Letter, that most of the content of intra-EU BITs was superseded by Community law upon accession of the respective Member State and that there "appears to be no need for agreements of this kind in the single market and their legal character after accession is not entirely clear".[87] The Commission feared that investor–state

[81] Article 8(6) of the Netherlands-Czech Republic BIT states: "The arbitral tribunal shall decide on the basis of the law, taking into account in particular though not exclusively:

- the law in force of the Contracting Party concerned;
- the provisions of this Agreement, and other relevant Agreements between the Contracting Parties;
- the provisions of special agreements relating to the investment;
- the general principles of international law."

It bears emphasising that the Commission referred only to the first bullet point of this provision.

[82] *Eastern Sugar B.V. (Netherlands) v. The Czech Republic*, Partial Award of 27 March 2007, para. 119 (footnote added).

[83] *Eastern Sugar B.V. (Netherlands) v. The Czech Republic*, Partial Award of 27 March 2007, para. 120.

[84] *Eastern Sugar B.V. (Netherlands) v. The Czech Republic*, Partial Award of 27 March 2007, para. 121.

[85] See, for example, CFI, T-126/95, *Dumez v. Commission*, [1995] ECR II, 2863.

[86] *Eastern Sugar B.V. (Netherlands) v. The Czech Republic*, Partial Award of 27 March 2007, para. 122.

[87] *Eastern Sugar B.V. (Netherlands) v. The Czech Republic*, Partial Award of 27 March 2007, para. 126.

dispute settlement procedures could lead to arbitration taking place without relevant questions of Community law being submitted to the ECJ, with unequal treatment of investors among Member States as a possible outcome. "In order to avoid such legal uncertainties and unnecessary risks for Member States, it is strongly recommended that Member States exchange notes to the effect that such BITs are no longer applicable, and also formally rescind such agreements. The [Economic and Financial] Committee is invited to endorse this approach and Member States are asked to communicate to the Commission by 30 June 2007 which actions have been taken in that regard and which of their intra-EU investment agreements still remain to be terminated."[88]

The *Eastern Sugar* tribunal, without giving any reasons, rightly concluded that the 2006 Note did not support the view that intra-EU BITs are all automatically superseded.[89] The tribunal went on to reject the Czech Republic's submission to refer the matter to the ECJ.[90] Indeed, under the ECJ's case law, an arbitral tribunal is not a "court or tribunal of a Member State" within the meaning of Article 267 TFEU (equivalent to Article 234 EC). The reason put forward by the ECJ is that the parties are under no obligation, in law or in fact, to refer their dispute to arbitration and the public authorities of the Member States concerned are not involved in the decision to opt for arbitration nor are they required to intervene of their own accord in the proceedings before an arbitral tribunal.[91]

After the tribunal had found that neither the BIT nor the Czech Republic's preaccession agreement with the Commission (the "Europe Agreement") nor the Accession Treaty had dealt expressly with the question of whether the BIT was still valid, it noted that the effect of the Czech Republic's accession to the EU would have to be judged by international law, and in particular Article 59 VCLT.[92] The tribunal rejected the Czech Republic's argument that EU law would relate to the

[88]*Eastern Sugar B.V. (Netherlands) v. The Czech Republic*, Partial Award of 27 March 2007, para. 126. Subsequently, the Czech Ministry of Finance proposed to the Czech Government that it terminate Czech intra-EU BITs. As a consequence, Italy and the Czech Republic terminated their BIT and Denmark is in the process of terminating its BIT with the Czech Republic. Slovenia and Malta announced their agreement with the Czech position, and their intent to unwind their own BITs. Italy also has indicated that it intends to terminate a number of other intra-EU BITs. However, not all EU member states concur with the Czech Republic's approach, including, according to public reports, Belgium, Germany, the Netherlands and the UK.

[89]*Eastern Sugar B.V. (Netherlands) v. The Czech Republic*, Partial Award of 27 March 2007, para. 128.

[90]*Eastern Sugar B.V. (Netherlands) v. The Czech Republic*, Partial Award of 27 March 2007, para. 138.

[91]ECJ, Case 102/81, *Nordsee*, [1982] ECR 1095, paras. 10–12; ECJ, Case C-126/97, *Eco Swiss China Time Ltd v. Benetton International NV*, [1999] ECR I, 3055, para. 34; ECJ, Case C-125/04, *Denuit and Cordenier v. Transorient*, [2005] ECR I, 923, para. 13.

[92]*Eastern Sugar B.V. (Netherlands) v. The Czech Republic*, Partial Award of 27 March 2007, paras. 144–158.

same subject matter as the BIT.[93] It also noted that it was neither the common intention of the Czech Republic and the Netherlands that the EU Treaty should supersede the BIT nor were the BIT and the EU Treaty incompatible.[94] It did not only reject the Czech Republic's argument based on Article 59 VCLT, but it also rejected its argument based on Article 30 VCLT.[95] Indeed, if the restrictive conditions of Article 59 VCLT are not met, Article 30 VCLT governs treaty relationships. The latter article is concerned with the application of successive treaties relating to the same subject matter, and deals only with the priority of inconsistent obligations in treaties when there is no doubt that both are in force. It therefore comes into play once it has been determined by way of application of Article 59 VCLT that the parties did not intend to abrogate or suspend the earlier treaty.[96] The tribunal, however, neither engaged in an analysis of Article 30 VCLT[97] nor did it refer to Article 307 EC.[98]

Eastern Sugar is not the only arbitral award that deals with the validity and applicability of intra-EU BITs. It is highlighted because to date it appears to be the

[93] *Eastern Sugar B.V. (Netherlands) v. The Czech Republic*, Partial Award of 27 March 2007, para. 165.

[94] *Eastern Sugar B.V. (Netherlands) v. The Czech Republic*, Partial Award of 27 March 2007, paras. 167–168.

[95] Article 30 VCLT ("Application of successive treaties relating to the same subject-matter") states in relevant parts: "2. When a treaty specifies that it is subject to, or that it is not to be considered as incompatible with, an earlier or later treaty, the provisions of that other treaty prevail. 3. When all the parties to the earlier treaty are parties also to the later treaty but the earlier treaty is not terminated or suspended in operation under Article 59, the earlier treaty applies only to the extent that its provisions are compatible with those of the later treaty".

[96] Anthony Aust, *Modern Treaty Law and Practice,* 2007, p. 293. On the problems regarding the application of Article 30 VCLT see Vierdag, The time of the "conclusion" of a multilateral treaty: Article 30 of the Vienna Convention on the Law of Treaties and related provisions, BYIL 59 (1988), p. 75 (110–111). It has been suggested that owing to the highly integrated nature of Community secondary law the implications of Member States' duties under Community law should be considered in the light of Article 27 VCLT ("A party may not invoke the provisions of its internal law as justification for its failure to perform a treaty.") rather than Article 30 VCLT. Licková, European Exceptionalism in International Law, EJIL 19 (2008) 3, p. 463 (470). However, the better view seems to be that EU law constitutes a highly developed order of international law.

[97] The tribunal shrugged off Article 30 VCLT and confined itself to stating that: "The Arbitral Tribunal moreover does not believe that it can accept the Czech Republic's argument that the treaty can end partially and remain in force otherwise. This situation would be governed by Article 30 of the Vienna Convention." *Eastern Sugar B.V. (Netherlands) v. The Czech Republic*, Partial Award of 27 March 2007, para. 178.

[98] Although Article 307 EC applies to agreements of Member States with third states only, it is nevertheless remarkable that the tribunal did not refer to it, while at the same time rejecting the Czech Republic's arguments by glancing at Article 13(3) of the Netherlands–Czech Republic BIT. *Eastern Sugar B.V. (Netherlands) v. The Czech Republic,* Partial Award of 27 March 2007, paras. 174–175. Article 13(3) of the Netherlands–Czech Republic BIT states: "In respect of investments made before the date of the termination of the present Agreement the foregoing Articles [regulation entry into force, tacit extension and procedure for termination; MB] thereof shall continue to be effective for a further period of fifteen years from that date".

only publicly available award in this regard. There appears to be at least one more award in which the respondent, again the Czech Republic, raised a jurisdictional challenge against the application of an intra-EU BIT. In a dispute between a German national, Mr Binder, and the Czech Republic under the Germany–Czech Republic BIT, an arbitral tribunal appears to have rejected the Czech Republic's argument that its BITs concluded with other EU Member States are no longer applicable following the Czech Republic's accession to the EU. Apparently, the Czech Republic challenged the tribunal's decision on jurisdiction in the Prague courts with a view that the courts ask the ECJ for a preliminary ruling. There is no public information available with regard to the status of the court proceedings in Prague.[99]

In conclusion, under the EC Treaty, intra-EU BITs remain applicable until they are terminated. From a Community perspective, this was not a welcome conclusion. However, Article 75(1) TFEU is unlikely to change this conclusion. Although it deletes the reference to third states, there is no reason to conclude that as a result intra-EU BITs would not be applicable upon the entry into force of the Treaty of Lisbon. Rather, these BITs continue to remain applicable for the reasons stated. Since arbitral tribunals are called upon to apply EU law in intra-EU BIT disputes, central questions of EU law will continue to be decided by arbitral tribunals rather than the ECJ. This result is facilitated by the ECJ's jurisprudence that arbitral tribunals do not qualify as courts or tribunals in the meaning of Article 267 TFEU. On the other hand, EU law does not provide for investor–state dispute settlement. However, if compared with redress before domestic courts or through a complaint to the Commission, investor–state arbitration is not necessarily the better dispute settlement mechanism for investors. Nevertheless, one reason why EU investors prefer their claims to be solved by international arbitral tribunals rather than in domestic courts of another Member State may be their lack of trust in these courts. This may well reflect the current state of the EU.

Conclusion

In both the internal and the external dimensions, BITs of Member States will continue to play a role. With regard to the external dimension, it remains to be seen whether the Commission comprehensively challenges the BITs of Member States with third states following the ECJ's judgments in the infringement cases and the entry into force of the Treaty of Lisbon. Until the Commission does successfully challenge these BITs, they will continue to be applicable. Further, given the limitation of the EU's exclusive external competence to FDI under the Treaty of Lisbon, Member States will continue to play a role in shaping the EU's external

[99]See IA Reporter 1 (July 1, 2008) 4, available at http://www.iareporter.com. It seems likely that in other cases based on intra-EU BITs the respondent argued along these lines. The most recent award based on an intra-EU BIT, though unpublished, appears to be *Austrian Airlines v. Slovak Republic*, Award of 20 October 2009.

investment policy. Although the extended competence under the Treaty of Lisbon is a step towards a comprehensive EU investment policy, further steps will be needed if the EU endeavours to become an efficient player in international investment law. Unless and until such steps are taken, the continued fragmentation of competences between the EU and its Member States is likely to cause confusion both within the EU and with the EU's treaty partners. With regard to the internal dimension, save for few exceptions, Member States have not yet followed the Commission's suggestion to terminate intra-EU BITs. However, even after the entry into force of the Treaty of Lisbon, these BITs continue to be applicable.