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**INVESTOR-STATE ADJUDICATION IN THE
EUROPEAN UNION CONTEXT**

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INTRODUCTION

Investor-state arbitration is a mechanism usually provided in international agreements on investments, signed by countries in order to establish rules when foreign companies invest on their territory. Investment arbitration allows an investor from one country to bring a suit directly against the state where the investment is set before an arbitration tribunal. In order to bring the case, the investor must claim that the State has breached rules contained in the agreement.¹

After the the Lisbon Treaty, the article 207 TFEU includes “foreign direct investment” in the scope of the Common Commercial Policy.² By virtue of the Article 3 (1)(e) TFEU, foreign direct investments are now considered part of the “exclusive competence” of the Union.³ However, there are still many doubts concerning the extent of the amendment. Firstly, it is still unclear whether or not portfolio investments are included in the new competences of the EU, and secondly, the EU Court of Justice has been asked to clarify the limits of the new competence, and the Opinion has still to be issued.

After the EU acquired a new power in investments, the Commission started to negotiate and conclude new mega-regional free trade agreements (FTAs).⁴

¹ EUROPEAN COMMISSION, *Factsheet on Investor-State Dispute Settlement*, 2013, available at http://trade.ec.europa.eu/doclib/docs/2013/october/tradoc_151791.pdf.

² TFEU, art. 207: “*The common commercial policy shall be based on uniform principles, particularly with regard to changes in tariff rates, the conclusion of tariff and trade agreements relating to trade in goods and services, and the commercial aspects of intellectual property, foreign direct investment, the achievement of uniformity in measures of liberalisation, export policy and measures to protect trade such as those to be taken in the event of dumping or subsidies. The common commercial policy shall be conducted in the context of the principles and objectives of the Union’s external action.*” (introducing the amendment to article 207 TFEU).

³ TFEU, art. 3.

⁴ See BILATERAL INVESTMENT TREATIES 1959-1999, available at <http://unctad.org/en/pages/PublicationArchive.aspx?publicationid=195>.

Most of these FTAs contain an investment chapter and an investor-state adjudication mechanism, such as the Transatlantic Trade and Investment Partnership (TTIP), the EU-Vietnam bilateral trade agreements and the newly released Comprehensive Economic and Trade Agreement with Canada (CETA 2016).⁵

Investor-state arbitration and the competence of European Union in foreign investments is one of most discussed topics in recent years. It is dubious whether or not all these EU Agreements will come to fruition, but in the event that they do, they hold the potential to revolutionize the global economy.⁶

The first chapter of this work will generally discuss investor-state arbitration. First, it will explain how investment treaties are structured and then it will discuss the main provisions. It will then describe the most important multilateral investment agreements in force: NAFTA, ASEAN Investment Treaty, EUROPEAN ENERGY CHARTER and ICSID.

The second chapter will give a background of EU competence in investments before the Lisbon Treaty, then it will analyze the current, actual situation, and some future possible developments. Finally, it will describe the method of negotiations of the aforementioned agreements.

The third and last chapter will discuss three treaties that are being negotiated, or already negotiated by the EU: the TTIP with the United States, the CETA with Canada, and the Agreement with Vietnam. Moreover, the third chapter will discuss the new approach of the EU Commission to the investor-state arbitration: The Investment System Court.

⁵ D. GALLO, F. G. NICOLA, *The External Dimension of EU Investment Law: Jurisdictional Clashes and Transformative Adjudication*, forthcoming in *Fordham Int'l J*, forthcoming 2016 (the The EU-South Korea Free Trade Agreement and the Trade Agreement between the European Union and Colombia and Peru do not contain an investment chapter).

⁶ See generally Paragraph 1.1.1 (analyzing the consequences of the TTIP).

CHAPTER 1- GENERAL OVERVIEW OF INVESTOR- STATE ARBITRATION

ABSTRACT: 1.1. BILATERAL INVESTMENT TREATIES AND THE MAIN PROVISIONS OF INTERNATIONAL INVESTMENT AGREEMENTS – 1.1.1. PROVISIONS REGARDING THE JURISDICTION OF THE TRIBUNAL – 1.1.2. PROVISIONS REGARDING SUBSTANTIVE RIGHTS OF THE INVESTOR – 1.1.3. DEFENSES – 1.1.4. PARALLEL PROCEEDINGS – 1.2. MULTILATERAL INVESTMENT TREATIES IN FORCE – 1.2.1. NAFTA – 1.2.2. ASEAN INVESTMENT AGREEMENT – 1.2.3. ENERGY CHARTER TREATY – 1.2.4. ICSID CONVENTION

Investments play a central role in any modern economy and, today, investments are commonly made across borders.⁷ When companies invest they create new trade values, jobs and income.⁸ Although national frontiers slow down the movements of capital from one country to another, these barriers are usually surmountable.

With the increasing importance of international investment, a new sector of international law has been born. This field focuses on the obligation of the host state of the investment towards the foreign investors and the mechanisms to solve disputes between the host State and the foreign investor.

Investors need provisions that ensure certain protections for foreign investors, such as assurances that they will be treated in the same manner as

⁷ EUROPEAN COMMISSION, *Investment Protection and Investor-to-State Dispute Settlement (ISDS) in European Union agreements*, 2014 available at http://trade.ec.europa.eu/doclib/docs/2014/march/tradoc_152273.pdf; M. WEAVER, *The Proposed Transatlantic Trade and Investment Partnership (TTIP): ISDS Provisions, Reconciliation, and Future Trade Implications*, in *Int'l Emory L. Rev.*, 2014, p. 235 (articulating the relevance of foreign investments).

⁸ See *supra* note 7 (disclosing the advantages of investments).

domestic investors.⁹ Sometimes, domestic courts are not appropriate to resolve such disputes, especially when the investor is victim to expropriation without proper compensation, is the subject of discrimination, or is deprived of due process.¹⁰ In this case, Investor-State Dispute Settlements (ISDS) is important because it provides for a neutral forum.¹¹ This means that the parties agree: to give governments the right to regulate in the public interest, to define terms like “indirect expropriation”, “fair and equitable treatment”, and to prevent abuse of the system and conflicts of interest in arbitrators by establishing a code of conduct.¹²

Investment arbitration can be formulated by bilateral treaties, international agreements between two parties, or multilateral treaties, i.e. international agreement between several parties, and foreign investment law enacted by states.¹³

Part 1.1 explains how bilateral investment treaties are structured, discusses the main provisions and compares them to the typical standards of investor-state arbitration. Part 1.2 outlines the most important multilateral investment agreements in force: NAFTA, ASEAN Investment Treaty, EUROPEAN ENERGY CHARTER and ICSID.

⁹ *See supra* note 7 (revealing what investors need).

¹⁰ *See supra* note 7 (explaining why domestic courts are not apt for cross border investment dispute).

¹¹ *See supra* note 7 (stating one characteristic of the ISDS).

¹² *See supra* note 7 (clarifying what an ISDS clause usually provides for).

¹³ C. MCLACHLAN, L. SHORE, M. WEINIGER, *International Investment Arbitration*, Oxford, 2008, p. 52; UNCTAD, *International Investment Agreements Navigator*, available at <http://investmentpolicyhub.unctad.org/IIA/IiasByCountryGrouping#iiaInnerMenu> (laying out where investment arbitration can usually be found).

1.1. BILATERAL INVESTMENT TREATIES AND THE MAIN PROVISIONS OF INTERNATIONAL INVESTMENT AGREEMENTS

Investor-state arbitration represents an instrument given to a national that invests in a foreign country to seek protection from the host state actions. Before investor-state arbitration developed, a foreign national that invested in a country had only two courses of action in asserting their rights against the host state of the investment: diplomatic protection and host state courts' intervention.

Concerning diplomatic protection, this means that the State of the nationality of the investor can intervene in order to protect his own national against another state. Under the traditional view of international law, a state represents the only subject of international law and the only one that can challenge the sovereignty of another state. However, most of the time a state does not have an economic interest in protecting an individual, even if that individual is its own national. Consequently, diplomatic protection does not represent a valid instrument to the investor because it does not give him the certainty that his own State will secure him from the host state actions.¹⁴

Regarding the host state court, this means that the investor can bring suit in the domestic court of the host State. However, this second alternative relies on the trust that an investor has on the legal system of the third country, without guarantee that the latter will assure a level of protection not inferior to the investor's one. In particular, in the past or in the developing countries, a domestic court could not offer to investors an international minimum standard of treatment. For instance, the

¹⁴ E. SCISO, *Appunti di Diritto Internazionale Dell'Economia*, Torino, 2012, p. 181 ff.

investor could be deprived of any right to challenge the state decisions or he could lose substantial and procedural rights.¹⁵

The investor-state arbitration represents a mechanism where the investor can challenge the host state action before a neutral forum where international law will be applied. The basis of investor-state arbitration is usually, but not only, found in a bilateral investment treaty (BIT) between two countries that bind themselves in the respect of certain rights in the area of the investment, most of them already recognized as part of international customary law.¹⁶

The first BIT was signed in 1959 between Germany and Pakistan.¹⁷ Many followed suit and have exponentially increased to reach a global total of 2,928 BITs in 2015.¹⁸ A BIT is typically structured to include the following sections: preamble, definitions, admission, substantive rights (fair and equitable treatment, most favored nation, national treatment, umbrella clause and full protection and security, protection from expropriation), compensation for losses, free transfer of payments, and settlement of dispute, subrogation, state to state dispute and duration.¹⁹

This Part will explore investor-state arbitration in general and in particular, looking at the BIT provisions, which are the requirements that a tribunal has to fulfil in order to have jurisdiction over a BIT violation and which are the main substantive rights of an investor. Then, it will focus on the defenses available to the

¹⁵ *Id.*

¹⁶ *Id.*

¹⁷ See Treaty between the Federal Republic of Germany and Pakistan the Promotion and Protection of Investments, 1961 available at http://www.iisd.org/pdf/2006/investment_pakistan_germany.pdf.

¹⁸ UNCTAD, *International Investment Agreements Navigator*, available at <http://investmentpolicyhub.unctad.org/IIA/IiasByCountryGrouping#iiaInnerMenu>.

¹⁹C. MCLACHLAN, L. SHORE, M. WEINIGER, *op.cit.*, 52.; J. WONG, *Umbrella Clauses in Bilateral Investment Treaties: Of Breaches of Contract, Treaty Violations, And The Divide Between Developing And Developed Countries In Foreign Investment Disputes*, in *Mason l. Rev.* 2006, p. 141 (explaining how a BIT is constructed).

State in order to preclude wrongfulness. Finally, it will analyze some procedural aspects of investor-state arbitration.

1.1.1. PROVISIONS REGARDING THE JURISDICTION OF THE TRIBUNAL

A tribunal has jurisdiction under a BIT only if three elements are met: the notion of investor, investment and the duration of the treaty.²⁰ This paragraph will discuss first the notion of nationality and when an investor, person or corporation can be defined a national of a foreign state. Following this, the focus will turn to the concept of investment, what the typical definition is, how broad the definition is, the issue of the duration of a BIT and what happens when it expires. Finally, it will discuss the concept of the consent to arbitration and how it can be given by the parties to the tribunal.

Nationality identifies the *ratione personae* of the tribunal and it consequently establishes the personal jurisdiction. In the past, before the development of international investment treaties, nationality was relevant to determine which state could bring a claim of an injured alien under diplomatic protection.²¹ In particular, customary international law allowed a state to confer nationality upon a person only if there was a “genuine link” between that person and the state of nationality.²² The relevance of nationality has been pointed out in a very famous case, *Belgium v. Spain*, where Belgium claimed Spain should be held accountable for the injury to

²⁰ C. MCLACHLAN, L. SHORE, M. WEINIGER, *op.cit.*, 29; A. D. GRAMONT & M. GRITSENKO, *Key Issues and Recent Developments in International Investment Treaty Arbitration*, Washington, 2007, p.6.

²¹ C. MCLACHLAN, L. SHORE, M. WEINIGER, *op.cit.*, 29; A. D. GRAMONT & M. GRITSENKO, *op.cit.*, 6 (stating which was the function of the nationality definition when there were no international investment agreements).

²² *Nottebohm Case (Liech. v. Guat.)*, Judgement, 1955, I.C.J (Second Phase) Rep. 4 ¶ 23.

a Canadian corporation operating in Spain.²³ However, it was held that only the State from where the company originated could exercise this right to seek payment, thus only Canada, a non-EU Member State, had such a right.²⁴ No such law has been established for shareholders.²⁵ If a wrong was done to a company that resulted in harm to its shareholders, then only the company has the authority to seek compensation.²⁶ The court found that Belgium did not have the right to bring Spain to court since the company was located in Canada.²⁷ In conclusion, this hallmark and old case established that only the state of the company, and not the state of the shareholders could bring suit against the host of the investment. Since *Belgium v. Spain* a lot has changed.

Nowadays, under investor-state arbitration, in nearly every case, only nationals of a contracting State other than the host state in which the investment is made can be protected by the treaty provisions.²⁸ As a result, a foreign investor receives more protection than a national investor of a State.

In order to define the nationality of the investor it is important to distinguish between natural persons and corporations. Usually, natural persons are considered nationals of a state when they are citizens.²⁹ Obviously, whether or not a person holds citizenship of any given country is established by the domestic law of that

²³ Case Concerning the *Barcelona Traction Light and Power Co, Limited* (Belg. v. Spain), Judgment, 1970 I.C.J. Rep.1970 ¶ 53 (Feb.5) (specifying how diplomatic protection worked).

²⁴ *Id.*

²⁵ *Id.* (noting that shareholders do not have the right to bring a claim).

²⁶ *Id.* (explaining that the state entitled to bring a claim was the state in which the company has nationality).

²⁷ *Id.* (determining which country bring the claim).

²⁸ C. MCLACHLAN, L. SHORE, M. WEINIGER, *op.cit.*, 29; A. D. GRAMONT & M. GRITSENKO, *op.cit.*, 6 (clarifying that the investment agreement protects foreign nationals and the nationality represents the subject matter jurisdiction).

²⁹ *Nottebohm Case*, *supra* note 59 ¶ 23.

country. For instance, sometimes citizenship is acquired by birth, sometimes it is passed by parents.

However, it is more complex to identify the nationality of a corporation.³⁰ Usually BITs use one, or a combination of these three tests: incorporation, which refers to the nationality of the company to the state under the laws of which it is organized; control, i.e., an investor that has the nationality of one BIT party is entitled to protection only of investment in the territory of the other BIT party that it owns or controls; or management of the company, which ascribes nationality to the state where the company investor has its place of business.³¹

One of the main cases concerning the nationality tests for a corporation is *Tokios Tokelés v. Ukraine*, where the International Centre for Settlement of Investment Disputes (“ICSID”) tribunal discussed whether jurisdiction existed to hear claims brought by Tokios Tokelès.³² The Tribunal, interpreting Article 25 of the ICSID Convention, established that the nationality of a corporation must be decided in accordance with the place of incorporation in the absence of an express “control provision”.³³ Consequently, although 99 percent of Tokios was owned by a Ukrainian national, the Tribunal determined that it was a Lithuanian

³⁰C. MCLACHLAN, L. SHORE, M. WEINIGER, *op.cit.*, 52; A. RIGO SUREDA, *Investment Treaty Arbitration: Judging Under Uncertainty*, Cambridge, 2012, p.43 (affirming that it is easier to identify the nationality of a natural person than the nationality of a corporation).

³¹C. MCLACHLAN, L. SHORE, M. WEINIGER, *op.cit.*, 52; A. RIGO SUREDA, *Investment Treaty Arbitration: Judging Under Uncertainty*, Cambridge, 2012, p.43 (listing the different tests which can be used to identify the nationality of a corporation).

³² *Tokios Tokelés v. Ukraine*, (ICSID case No. ARB/02/18) Decision on Jurisdiction ¶ 23, (Apr. 29 2004); M.R. MAURO, *New International Tribunals and New International Proceedings*, in Del Vecchio, Milano, 2006 p. 281 (introducing the case regarding Tokios Tokelés, a Lithuanian corporation, with no substantial business activities in Lithuania, with 99 percent of the shares in the corporate entity owned by nationals of Ukraine, with a managerial control of the company vested in nationals of Ukraine, and the capital also originated in Ukraine).

³³ *Id.* (discussing the application of the incorporation test).

corporation.³⁴ In his dissenting opinion, Professor Weil proposed a more flexible approach.³⁵ He suggested that it was necessary to look at the origin of capital, not the formal incorporation, to avoid that, in contrast with the purpose of the ICSID system, the ICSID mechanism will be applied to national investments (“veil piercing doctrine”).³⁶

The case is relevant because the tribunal established that the doctrine of the “veil piercing” should not override the terms of the BIT, causing the declining of jurisdiction.³⁷

However, modern BITs are quite specific and they clarify which of the three criteria must be used to identify the nationality of a corporation.

Finally, it is important to point out that the ICSID tribunals established the corporation must possess home-state nationality continuously from the date of injury to the date of official commencement of the arbitration request.³⁸ As such, if a corporation loses the nationality, under which it starts a procedure, before the judgment, the tribunal will not have jurisdiction over the case.

Considering the concept of investment, it is relevant in order to identify the subject matter jurisdiction, the *ratione materiae* of the tribunal. Almost all BITs adopt a similar formula for investment, which usually includes a wide inclusive phrase as well as a list of specific categories such as property, shares contracts, and

³⁴ *Id.* (explaining the finding of the Tribunal).

³⁵ *Id.* (introducing the dissenting opinion).

³⁶ *Id.* (explaining the control test).

³⁷ *Id.* (explaining the relevance of the case).

³⁸ *The Loewen Group Inc and Raymond Loewen v. United States of America*, ICSID, Case No. ARB(AF)/98/3, Award, ¶225 (June 26, 2003) (Discussing a case where the chairman of a Canadian corporation involved in the death-care industry filed claims seeking damages for alleged injuries arising out of litigation in which the company was involved in Mississippi state courts).

intellectual property rights.³⁹ One of the most well known definitions of “investment” is provided by the ICSID tribunal in *Salini Costruttori SpA and Italstrade SpA v. Kingdom of Morocco*, where two Italian companies claimed damages against Morocco.⁴⁰ The definition is comprised of four cumulative elements: contributions to the economic development of the host state, monetary contribution, certain duration of performance for a contract, and a participation in the risks of the transaction.⁴¹ If not all these elements are present the tribunal cannot hear the case, since the matter is considered outside its jurisdiction.

This typical notion of investment is broad, but not enough as tribunals usually consider pre-contract costs as separate to the investment unless there is the consent of the State.⁴²

Tribunals usually accept, not only direct investment, but also indirect investment and, as such, they generally consider the claims brought by shareholders, whether they are controlling shareholders or not, as valid ultimate beneficiaries.⁴³

³⁹ See NAFTA, ASEAN agreement, Energy Charter Treaty, art. 1(6) 2080 UNTS 95; 34 ILM 360 (1995) (addressing the notion of investment).

⁴⁰ *Salini Costruttori SpA and Italstrade SpA v. Kingdom of Morocco*, ICSID Case No. ARB/00/4, Decision on Jurisdiction, (July 23 2001); M.R. MAURO, *op. cit.*, 281 (describing the foremost definition of investment).

⁴¹ *Id.*

⁴² *Milhaly International Corporation v. Republic of Sri Lanka*, ICSID Case No. ARB/00/2, Award, ¶ 61 (Mar. 15 2002) (explaining that generally pre-investment is not considered part of the investment).

⁴³ C. MCLACHLAN, L. SHORE, M. WEINIGER, *op.cit.*, 184 ff.; INNA UCHKUNOVA, *Indirect Investments Through Chain Of Intermediary Companies: A Philosopher's Stone Or Not Any More?*, 2013, available at <http://kluwerarbitrationblog.com/blog/2013/07/03/indirect-investments-through-chain-of-intermediary-companies-a-philosophers-stone-or-not-any-more/> (stating that the notion of investment regularly includes indirect investments).

Finally, the tribunal can have jurisdiction only if the *ratione temporis* requirement is fulfilled. This means that the BIT between the two Contracting Parties temporally covers the investment.⁴⁴

BITs generally provide for a fixed duration of at least ten years. However, the treaties usually continue in force until specific notice.⁴⁵ An investment can be protected even if the BIT came into force after the investment was made as many treaties include a retroactive provision that expressly establishes this.⁴⁶ In addition, after termination, there is usually a period during which investment originally covered by the BIT continues to retain protection provided in the BIT.⁴⁷

Obviously, in order to initiate a suit before an arbitral tribunal both parties must give consent. The State usually gives a general consent in the BIT while the investor expresses his consent filing the suit. The concept of consent is inherently linked to the *ratione temporis* and it is debated whether or not the expiration of the BIT covers or not the investment made prior to that moment.

One of the most discussed issues deals with the relationship between the withdrawal from the ICSID Convention and the consent. ICSID Convention established an investor-state mechanism. Under ICSID a tribunal has jurisdiction only if the tribunal has jurisdiction not only under a BIT but also under the ICSID

⁴⁴ C. MCLACHLAN, L. SHORE, M. WEINIGER, *op.cit.*, 29; A. D. GRAMONT, M. GRITSENKO, *op.cit.*

⁴⁵ C. MCLACHLAN, L. SHORE, M. WEINIGER, *op.cit.*, 128; UNCTAD, *Bilateral Investment Treaties 1995–2006: Trends In Investment Rulemaking* available at unctad.org/en/docs/iteiia20065_en.pdf (clarifying the duration of a BIT).

⁴⁶ *Tradex Hellas Sa v. Republic of Albania*, ICSID Case No. ARB/94/2, Jurisdiction, ¶ 192 (Dec. 24 1996) (noting that investments may be protected retrospectively).

⁴⁷ C. MCLACHLAN, L. SHORE, M. WEINIGER, *op.cit.*, 92.; P. GRANÉ, *Umbrella Clause Decisions: The Class of 2012 and a Remapping of the Jurisprudence*, in *Kluwer Arbitration Blog*, 2013, available at <http://kluwerarbitrationblog.com/2013/01/17/umbrella-clause-decisions-the-class-of-2012-and-a-remapping-of-the-jurisprudence/> <http://kluwerarbitrationblog.com/2013/01/17/umbrella-clause-decisions-the-class-of-2012-and-a-remapping-of-the-jurisprudence/> (discussing the protection after the termination of the BIT).

convention. Recently, Argentina, Bolivia and Venezuela denounced the ICSID Convention, which gave rise to the issue whether or not prior foreign investments are also recognized before this tribunal. Part of the doctrine believes that once the State withdraws its consent, denouncing the Convention, the ICSID tribunal does not have jurisdiction, since it is a compulsory requirement. On the other hand, article 72 of the ICSID Convention must be interpreted in a way to protect the prior investment that are, in any case, still protected by the BIT providing that it has not been terminated.

In conclusion, an arbitral tribunal or even a domestic court, in the case in which the parties refer to it, can have jurisdiction under a BIT only if the investor is a national of a Contracting party, the investment is covered by the definition given to the BIT, the BIT is still in force at the time of the claim or still covers the the investment and the parties gave prior consent to the tribunal.⁴⁸

1.1.2. PROVISIONS REGARDING SUBSTANTIVE RIGHTS OF THE INVESTOR

BITs always provide foreign investors with standard benefits, that despite some variations are considered common features of all the investment treaties.⁴⁹ This paragraph will discuss the main standard protections of the investor. In particular, it will analyze: the fair and equitable standard, the protection in case of expropriation, the full protection and security, the national treatment and the most favored nation. All these standards are considered part of an international minimum

⁴⁸ ICSID Convention.

⁴⁹ SIDLEY AUSTIN LLP, *The Basics Of Bilateral Investment Treaties*, 2016, available at <http://www.sidley.com/experience/the-basics-of-bilateral-investment-treaties>; M. L. MOSES, *The Principles And Practice Of International Commercial Arbitration*, Cambridge, 2012 p. 240 (introducing the standard rights of BITs).

standard of treatment that the host state must make available to the foreign investor and a violation of them gives rise to a claim before a competent tribunal.

The fair and equitable treatment is recognized as part of customary international law.⁵⁰ The fair and equitable standard is a non-contingent right, usually formulated with vague and imprecise language.⁵¹ This contributes in large part to the controversy surrounding this standard, mainly because many of its imprecise formulations provide space for different interpretations of its content.⁵² In order to define this standard it is appropriate to refer to the ICSID tribunal jurisprudence. However, it is important to specify that investor-state arbitration is neither civil law nor common law. There is no binding precedent but the awards have a persuasive value. The fair and equitable standard relates to the treatment of investors by the host State's courts and to the administrative decision making of the host state.⁵³

Considering the role of the host state's courts, the ICSID tribunal in *Azinian v. Mexico* opined that a failure to entertain a suit, undue delay, inadequate administration of justice, or a clear and malicious misapplication of the law can cause a breach of that standard and, in particular, a denial of justice.⁵⁴ An example

⁵⁰ *CMS Gas Transmission Company v. Argentina*, ICSID Case No ARB/01/8, Award ¶ 284 (May 12, 2005). According to the tribunal: "treaty standard of fair and equitable treatment and its connection with the required stability and predictability of the business environment founded on solemn legal and contractual commitments, is not different from the international law minimum standard and its evolution under customary law." (affirming that the fair and equitable standard under domestic law is not different from the one under international law).

⁵¹ M. MALIK, *Bulletin #3: Fair and Equitable Treatment, IISD Best Practices Series*, Winnipeg, 2009 available at http://www.iisd.org/pdf/2009/best_practices_bulletin_3.pdf; I. TUDOR, *The Fair and Equitable Treatment Standard in the International Law of Foreign Investment*, Oxford, 2008, p. 236 (introducing the fair and equitable treatment standard).

⁵² M. MALIK, *op.cit.*, 9; I. TUDOR, *op.cit.* 236 (addressing a problem regarding the fair and equitable treatment standard).

⁵³ M. MALIK, *op.cit.*, 9; C. MCLACHLAN, L. SHORE, M. WEINIGER, *op.cit.*, 226 (introducing the context in which a fair and equitable treatment issue can arise).

⁵⁴ *Robert Azinian, Kenneth Davitian, & Ellen Baca v. Mex.*, ICSID Case No ARB (AF) /97/2, Award, ¶ 102-103 (Nov. 1999).

of how a national court may be sanctioned for breach of fair and equitable treatment is represented by *Loewen*, a famous case, pertaining to the American legal system.⁵⁵ In *Loewen*, the Canadian claimant alleged that the jury ruling, that awarded its American competitor US\$500 million in damages, was unfair and discriminatory.⁵⁶ The tribunal found that the judicial process “amounted to an international wrong” because local procedural rules required *Loewen* to post a bond of 125 percent of the amount of the judgment in order to secure a stay of execution pending appeal.⁵⁷

The second category of cases involving the standard of fair and equitable treatment deals with the review of administrative conduct.⁵⁸ Tribunals usually refer to two types of factors that determine investor treatment: legitimate expectations and due process.⁵⁹ Legitimate expectations concern the treatment afforded to an investor by reference to the law of the host State at the time of the investment.⁶⁰ Meanwhile, due process depends on whether administrative decisions were reached through a fair process, or if the host State acted according to improper purposes within its administrative powers.⁶¹ Concerning legitimate expectations, the ICSID tribunal in *Tecmed v. Mexico* defined the scope of the fair and equitable treatment

⁵⁵ M. MALIK, *op.cit.*, 10; C. MCLACHLAN, L. SHORE, M. WEINIGER, *op.cit.*, 227 (introducing two cases in which domestic courts have been sanctioned for violation of the fair and equitable treatment standard).

⁵⁶ *The Loewen Group Inc and Raymond Loewen v. United States of America*, ICSID, Case No. ARB(AF)/98/3, Award, (June 26, 2003).

⁵⁷ *Id.*

⁵⁸ M. MALIK, *op.cit.*, 41; TUDOR, *op.cit.*, 41.

⁵⁹ M. MALIK, *op.cit.*, 11; C. MCLACHLAN, L. SHORE, M. WEINIGER, *op.cit.*, 233 ff. (clarifying the two ways in which the administrative conduct can violate the fair and equitable treatment).

⁶⁰ *Id.* (explaining what the legitimate expectation is).

⁶¹ *Id.* (identifying the concept of due process).

standard based on an autonomous interpretation under the Spain-Mexico BIT.⁶² It stated that the fair and equitable treatment provision requires the Contracting Parties to provide international investments treatment that does not affect the basic expectations that were taken into account by the foreign investor to make the investment.⁶³ According to the tribunal, the foreign investor expects the host State to act in a consistent manner, free from ambiguity and totally transparent in its relations with the foreign investor.⁶⁴

The second factor that determines the treatment of the investor is due process in administrative decision making.⁶⁵ Proper due process bars arbitrary and discriminatory decisions against non-nationals, requires transparent proceedings, bars use of improper purposes, forbids inconsistency of conduct vis-a-vis the investor, and also forbids coercion or harassment by State authorities and bad faith.⁶⁶

A second standard of protection in favor of the investor is the full protection and security.⁶⁷ This concerns a State's failures to protect an investor's property from actual damage caused by either corrupt State officials or by the actions of others,

⁶² *Tecnicas Medioambientales Tecmed S.A. V. The United Mexican States*, ICSID CASE No. ARB (AF)/00/2, Award (May 29 2003).

⁶³ *Id.* (defining when the concept of legitimate expectations is violated).

⁶⁴ *Id.* (defining when the concept of legitimate expectations is violated).

⁶⁵ M. MALIK, *op.cit.*; C. MCLACHLAN, L. SHORE, M. WEINIGER, *op.cit.*, 236 ff. (introducing the importance of the due process).

⁶⁶ M. MALIK, *op.cit.*, 14; C. MCLACHLAN, L. SHORE, M. WEINIGER, *op.cit.*, 239 ff. (defining the concept of due process).

⁶⁷ *See* US Model BIT art. 5(2).

where the State has failed to exercise due diligence.⁶⁸ It is thus principally concerned with the exercise of police power.⁶⁹

According to the ICSID tribunal a State has an obligation to take reasonable steps to protect its investors against harassment by third parties and/or State actors.⁷⁰ However, ICSID tribunal rejected the argument that the full protection and security standard creates absolute liability.⁷¹ One of the most contested issues, with respect to the standard of full protection and security, is whether or not it extends beyond situations where the physical security of the investor is compromised, including damages to intangible assets.⁷²

Considering national treatment, an example is considered in North American Free Trade Agreement (“NAFTA”) Article 1102.⁷³ It ensures that each Party shall accord to investments of investors of another Party treatment no less favorable than that it accords to investments of its own investors.⁷⁴ In particular, the ICSID tribunal held that the treatment accorded to a foreign owned investment should be compared with that accorded to domestic investment in the same business or economic sector.⁷⁵

⁶⁸ *See id.* (defining the concept of the full protection and security standard).

⁶⁹ *See id.* (addressing the link between the full protection and security standard and the police power).

⁷⁰ *AES Summit Generation Limited and AES-Tisza Erömi Kft v. Hungary*, ICSID case no. ARB/07/22, IIC 455 (September 17, 2010/dispatched September 24, 2010).

⁷¹ *Asian Agricultural Products Ltd (AAPL) v. Republic of Sri Lanka*, ICSID Case No. ARB/87/3 ¶48 (June 21, 1990).

⁷² JEFFERY COMMISSION, *The Full Protection and Security Standard in Practice*, in *Kluwer Arbitration Blog*, 2009) available at <http://kluwerarbitrationblog.com/2009/04/16/the-full-protection-and-security-standard-in-practice/> (addressing the problem of physical security).

⁷³ North American Free Trade Agreement, U.S.-Can.-Mex., art 1102(2), Dec. 17, 1992, 32 I.L.M. 289 (1993) [hereinafter NAFTA].

⁷⁴ *Id.*

⁷⁵ *Pope & Talbot Inc. v. The Government of Canada*, ICSID, Interim Award ¶ 119-120 (June 26, 2000).

Another important international clause is the most favored nation (MFN).⁷⁶ The International Law Commission (“ILC”) has defined the MFN treatment as treatment accorded by the granting State to the beneficiary State, or to persons or things in a determined relationship with that State.⁷⁷ It must not be less favorable than treatment extended by the granting State either to a third State or to persons or things in the same relationship with that third State.⁷⁸

Nowadays, there is much debate as to whether the MFN provision can be extended or not to the dispute solution clause. This is important because, if the most favored nation provision is extended to the dispute solution clause, a country concluding two BITs with two different countries, cannot provide different dispute mechanisms, since the most favorable mechanism will be extended to the investors of the country with the less favorable clause.⁷⁹ The general tendency of the doctrine is that, unless explicitly excluded, the most favored nation should be applied to any provision of the BIT. However, a minority doctrine considers that this tendency will cause legal uncertainty.⁸⁰

Expropriation probably represents the main reason why the investor-state arbitration is born and the strongest violation of the investor’s rights. In particular, in the past, when a State seized an investor’s assets without compensation as part of a program of economic reform, the classical reaction was that the investor, in

⁷⁶ INTERNATIONAL LAW COMMISSION, Draft articles on most-favored-nation clauses (ILC Draft), art. 5 in Yearbook of the international Law Commission, 1978, Vol. II, Part Two.

⁷⁷ *Id.*

⁷⁸ *Id.*

⁷⁹ E. GAILLARD, *Establishing Jurisdiction Through a Most-Favored-Nation Clause* in *New York Law Journal*, 2005, available at http://www.shearman.com/~media/Files/NewsInsights/Publications/2005/06/Establishing-Jurisdiction-Through-a-MostFavoredN_/Files/Download-PDF-Establishing-Jurisdiction-Through-a_/FileAttachment/IA_060205.pdf.

⁸⁰ *Id.*

search of compensation, could only seek diplomatic protection.⁸¹ Consequently States would only select to honor claims motivated by political concerns.⁸² Thus the claim for expropriation expanded in line with the proliferation of investment treaties.⁸³

One of the main concerns about expropriation is identifying it. It is generally defined as a governmental taking of property for which compensation is required.⁸⁴ In addition to tangible property, intangible property rights, such as shareholder and contractual rights, can also be expropriated.⁸⁵ Thus, in *SPP v. Egypt*, the tribunal rejected the argument that the term ‘expropriation’ applies only to property rights.⁸⁶ The problem is that the definitions of expropriation provided for in investment treaties are so general that they are not useful for the purposes of tribunals.⁸⁷

The model Canada BIT contains a typical provision that prohibits expropriation without just compensation.⁸⁸ Article 13.1 of the model Canada BIT provides that a

⁸¹ C. SCHREUER, *Investment Protection and International Relations*, at 1 available at http://www.univie.ac.at/intlaw/wordpress/pdf/87_investment_protect.pdf; T. WEILER, *International Investment Law and Arbitration: Leading Case From The Icsid, Nafta, Bit, Customary International Law*, Cameron, 2005, p. 607 (addressing the problem of the diplomatic protection for investments).

⁸² C. SCHREUER, *op. cit.*; T. WEILER, *op.cit.* (explaining the investor’s protection in the past).

⁸³ C. SCHREUER, *op. cit.*; T. WEILER, *op.cit.* (noting that the expropriation claims increased along the growth of the international investment agreements).

⁸⁴ B. ATTAR, B. LI, D. KESSLER, M. BURNIER, *Expropriation Clauses In International Investment Agreements And The Appropriate Room For Host States To Enact Regulations: A Practical Guide For States And Investors*, Geneva, 2009, p. 5; C. MCLACHLAN, L. SHORE, M. WEINIGER, *op.cit.*, 266; UCHKUNOVA, *op.cit.* (defining the concept of expropriation).

⁸⁵ *Southern Pacific Properties (Middle East) Limited Arab Republic of Egypt*, ICSID Case No. ARB/84/3, Award ¶ 164 (May 20, 1992) (explaining which rights can be subject to expropriation).

⁸⁶ *Id.* (quoting the tribunal in *SPP v. Egypt*).

⁸⁷ It has been said of NAFTA, art. 1110 (1) that its “language is of such generality as to be difficult to apply in specific cases” *Fieldman v. United Mexican States*, ICSID Case No. ARB(AF)/99/1, Award (Dec. 16, 2002).

⁸⁸ CANADA MODEL BIT.

State cannot expropriate an investment, except for a public purpose, in accordance with due process of law, in a non-discriminatory manner and on prompt, adequate and effective compensation.⁸⁹ As such, a state as a sovereign entity has the right to expropriate but it can do so only respecting the four criteria previously mentioned. If the State does not, it will be considered an unlawful expropriation. Distinguishing between the consequences of a lawful and unlawful expropriation is problematic.⁹⁰ Some authorities believe illegal takings require higher compensation, including damages.⁹¹

The intent to expropriate is not usually considered a requirement in order to identify an expropriation (the sole effective doctrine).⁹² This means that it does not matter if the State meant to expropriate or not. Rather, relevance is placed on the effect on the investor's right. Moreover, it is important to distinguish between nationalization and expropriation: usually, nationalization means a large-scale, industry-wide taking, while expropriation refers to single State acts.⁹³

Expropriation is usually distinguished as being either direct or indirect; direct expropriation means a mandatory legal transfer of the title to the property or its outright physical seizure operated by a formal law or decree or physical act.⁹⁴ On

⁸⁹ *Id.*

⁹⁰ T. WEILER, *op.cit.*, 631; C. MCKENNA, *Tribunal weighs on unlawful expropriation*, in *Lexology*, Global, 2015, available at <http://www.lexology.com/library/detail.aspx?g=1d18d9b9-778a-4041-ab4b-5ec6c4db6871> (noting that there is a difference between lawful and unlawful expropriation).

⁹¹ C. SCHREUER, *op. cit.*; T. WEILER, *op.cit.* (addressing the difference between lawful and unlawful expropriation).

⁹² T. WEILER, *op.cit.*, 615; C. MCLACHLAN, L. SHORE, M. WEINIGER, *op.cit.*, 270 (clarifying that the intent to expropriate is not necessary to identify an expropriation).

⁹³ T. WEILER, *op.cit.*, 607 ff.; C. MCLACHLAN, L. SHORE, M. WEINIGER, *op.cit.*, 296. (describing the difference between expropriation and nationalization).

⁹⁴ H. NIKIEMA, *Best Practices Indirect Expropriation*, 2012, available at http://www.iisd.org/pdf/2012/best_practice_indirect_expropriation.pdf (defining direct expropriation).

the contrary, indirect expropriations do not have a clear or unequivocal definition, but they materialize through actions or conduct which do not explicitly express the purpose of depriving one of rights or assets, but actually have that effect.⁹⁵ ICSID tribunals held that there is no expropriation when there is only an omission, a theologically driven action must occur.⁹⁶ Moreover, there is no expropriation when the investor consented to the expropriatory measure, as expropriation must be a compulsory transfer.⁹⁷

There are different forms of indirect expropriation, such as creeping expropriation and measures tantamount to expropriation.⁹⁸ Creeping expropriation is not the result of a single act of State, but results from a number of actions that gradually result in expropriation.⁹⁹ A measure tantamount to expropriation is considered a type of expropriation.¹⁰⁰ According to the arbitral decision in *S.D. Meyers v. Canada*, “*The primary meaning of the word ‘tantamount’ given by the Oxford English Dictionary is ‘equivalent,’ both words require a tribunal to look at the substance of what has occurred and not only the form.*”¹⁰¹

⁹⁵ *Tecnicas Medioambientales Tecmed S.A. V. The United Mexican States*, ICSID CASE No. ARB (AF)/00/2, Award ¶ 114 (May 29 2003).

⁹⁶ *Eudoro Armando Olguin v. Republic of Paraguay*, ICSID Case No. Arb/98/5 Award ¶ (Jul.26 2001).

⁹⁷ *Tradex Hellas Sa v. Republic of Albania*, ICSID Case No. ARB/94/2, Jurisdiction, ¶ 135(Dec. 24 1996).

⁹⁸ P. D. ISAKOFF, *Defining the Scope of Indirect Expropriation for International Investments in Global Bis. L. Rev.* 2013, p. 82; C. SCHREUER, *The Concept of Expropriation under the ETC and other Investment Protection Treaties*, 2005, p. 5, available at http://www.univie.ac.at/intlaw/pdf/csunpublpaper_3.pdf (listening the different forms of indirect expropriation).

⁹⁹ P. D. ISAKOFF, *op.cit.*, 195; C. SCHREUER. *op.cit.*, 4 (defining the creeping expropriation).

¹⁰⁰ P.D. ISAKOFF, *op.cit.*, 82; C. SCHREUER. *op.cit.*, 5 (giving the definition of measure tantamount to expropriation).

¹⁰¹. *S.D. Myers, Inc. v. Government of Canada*, UNCITRAL/NAFTA, First Partial Award, ¶ 285 (Nov. 13, 2000).

One of the main issues concerning expropriation is how to differentiate situations in which the deprivation of the rights of the investor gives rise to a real expropriation and as such it requires compensation and when the state action can be justified by its police powers. Consequently, not all government measures entitle the investor to compensation.

The regulatory actions do not amount to expropriation but are measures that, even depriving the owner of the right, do not need compensation because the state acts in its police power to protect the public health, environment, safety etc. The main issue is that the extension of all these concepts is very difficult to identify. After decades there is no still a precise theory on how to determine the line between expropriation and regulation, a clear distinction does not exist in international law, but in general, if the deprivation of ownership is not radical, fundamental, in significant part, substantial, or serious, no compensation can be claimed because the act represents simply a regulatory measure.¹⁰²

When a foreign national invests in a State, the State usually concludes a contract with an investor. This means that there is a double protection for the investor: the contract and the treaty, but not every breach of contract constitutes an expropriation.¹⁰³ The most important criterion for distinguishing between a simple breach of contract and the expropriation of contract rights is whether the State acts in its commercial role as a party to the contract or in its sovereign capacity.¹⁰⁴

¹⁰²T. WEILER, *op.cit.*, 621; A. P. NEWCOMBE, *Regulatory Expropriation, Investment Protection and International Law: When Is Government Regulation Expropriatory and When Should Compensation Be Paid?*, 1999, p. 73, available at <http://www.italaw.com/documents/RegulatoryExpropriation.pdf>; Concerning the erosion of regulatory powers, A. Del Vecchio, *New International Tribunals and New International Proceedings*, in Del Vecchio, Milano, 2006 p. 9 (addressing the notion of regulatory measure).

¹⁰³ C. SCHREUER. *op.cit.*, 1 (outlining a difference between a breach of a contract and an expropriation).

¹⁰⁴ C. SCHREUER. *op.cit.*, 1 (explaining how to identify when a breach of contract implies an expropriation).

Nowadays most investment treaties contain an “umbrella clause”, in which the host State agrees to comply with any obligation undertaken with respect to investments from the investing State; the effect is to elevate contract breach to treaty violation.¹⁰⁵

It is fundamental to distinguish between contract claims and treaty claims.¹⁰⁶ The contract claims arise when there is a breach of contract; the treaty claims arises when there is a violation of a treaty.¹⁰⁷ Not only will the jurisdiction differ for each claim, but the applicable law will also vary.¹⁰⁸ In contract claims, the tribunal will apply the applicable law for the contract, which was chosen by the parties; whereas in treaty claims, the tribunal will apply international law.¹⁰⁹ Moreover, the tribunal may be jurisdictionally limited in determining claims of treaty breach, or may have jurisdiction to the contractual rights if the parties agree to it.¹¹⁰ This distinction is not present if a treaty contains the so called “umbrella clause.”¹¹¹ For instance, Article II.2(c) of the US-Argentina BIT provides that “[e]ach party shall observe

¹⁰⁵ *Société Générale de Surveillance S.A. v. Islamic Republic of Pakistan*, ICSID Case No. ARB/01/13, Objection to Jurisdiction ¶ 163 (Aug. 6 2003); C. MCLACHLAN, L. SHORE, M. WEINIGER, *op.cit.*, 92(defining the umbrella clause).

¹⁰⁶ C. MCLACHLAN, L. SHORE, M. WEINIGER, *op.cit.*, 127 (specifying that there is a difference between contract claims and treaty claims).

¹⁰⁷ J. O. VOSS, *The Impact of Investment Treaties on Contracts between Host States and Foreign Investors*, 2010, p. 166; C. SCHREUER. *op.cit.*, 133. (discussing the difference between contract claims and treaty claims).

¹⁰⁸ J. O. VOSS, *op.cit.*, 165 ff.; C. SCHREUER. *op.cit.* (articulating the consequences of the difference between contract claims and treaty claims).

¹⁰⁹ J. O. VOSS, *op.cit.*, 165 ff.; C. SCHREUER. *op.cit.* (discussing the applicable law).

¹¹⁰ J. O. VOSS, *op.cit.*, 165 ff.; C. SCHREUER. *op.cit.* (referring to the jurisdiction of the tribunal).

¹¹¹ C. MCLACHLAN, L. SHORE, M. WEINIGER, *op.cit.*, 92.; PATRICIO GRANÉ, *op.cit.* (specifying the function of the umbrella clause).

any obligation it may have entered into with regard to investments.”¹¹² However, there is no consistency in how these cases have been decided.¹¹³

In *SGS v. Pakistan*, the tribunal rejected the notion that a contract claim could be transformed into a treaty claim by virtue of an umbrella clause.¹¹⁴ A few months later, the same tribunal made a conflicting judgment, interpreting another umbrella clause differently in *SGS v. Philippines*, to “say, and to say clearly, that each Contracting Party shall observe any legal obligation it has assumed, or will in the future assume, with regard to specific investments covered by the BIT.”¹¹⁵ Arbitral tribunals generally interpret each clause differently, so it is likely that umbrella clauses will remain one of the most controversial areas of international investment law.¹¹⁶

In conclusion, the BITs give to the investor a set of standard protections that he can assert before a tribunal. The strongest claim is the expropriation of the right of the investment but the fair and equitable treatment, the most favored nation, the full protection and security and the national treatment guarantee to the investor a strong protection even if he has not been completely deprived from his right.

1.1.3. DEFENSES

¹¹² Treaty between United States of America and the Argentine Republic concerning the reciprocal encouragement and protection of investment, U.S-Arg., art. 2(c) Nov,14,1991 available at <http://www.state.gov/documents/organization/43475.pdf>.

¹¹³ A. D. GRAMONT & M. GRITSENKO, *op. cit.*, 51; C. MCLACHLAN, L. SHORE, M. WEINIGER, *op.cit.*, 111(addressing a problem related to the umbrella clause).

¹¹⁴ *Société Générale de Surveillance S.A. v. Islamic Republic of Pakistan*, ICSID Case No. ARB/01/13, Objection to Jurisdiction, 167 (Aug. 6 2003).

¹¹⁵ *Société Générale de Surveillance S.A. v. Republic of the Philippines*, ICSID Case No. ARB/02/6, Decision of the Tribunal on Objections to Jurisdiction, 115, 119 (Jan. 29, 2004).

¹¹⁶ PATRICIO GRANÉ, *op.cit.*; A. D. GRAMONT & M. GRITSENKO, *op. cit.*, 53 (noting that the umbrella clause represents an issue in investment arbitration).

In investor-state arbitration, the investor is the only party that can start a procedure, challenging an action of the host state. The State can reply affirming that its conduct does not constitute a violation of international law or national law. Considering the differences between contract and treaty claims, defenses can be derived not only in the applicable law of the contract but also under general international law.¹¹⁷

Concerning the defenses under the contract, it is necessary to refer to the applicable law of the contract that, unless otherwise established, is represented by the host state law. As regards the international law defenses, the International Law Commission has recognized that there are six circumstances that preclude wrongfulness: consent (art 20), self- defense (art 21), countermeasures (art 22), *force majeure* (art 23), distress (art 24) and necessity (art 25).¹¹⁸

The present paragraph will discuss some defenses that are often used in investor-state arbitration, in particular, force majeure, as opposed to hardship, and necessity, as opposed to the essential security interest.

Force majeure is considered a defense under international law and national law, at least in civil law countries.¹¹⁹ Under art 7.1.7 of the UNIDROIT Principles, a state can be excused from the non performance if it proves the existence of an impediment that was beyond its control and that could not reasonably be expected before. Force majeure must be distinguished by hardship, where the performance of a contract becomes more onerous for one of the parties¹²⁰ Under article 6.2.2 of the UNIDROIT principle there is a hardship where the occurrence of events alters

¹¹⁷ A. P. NEWCOMBE, *op.cit.* 482; R. D. BISHOP, J. CRAWFORD, W. MICHAEL REISMAN, *Foreign Investment Disputes: Cases, Materials, and Commentary*, The Hague, 2005, p.1372.

¹¹⁸ Yearbook of the International Law Commission 2001, Volume 2, Parte 2.

¹¹⁹ R. D. BISHOP, J. CRAWFORD, W. MICHAEL REISMAN, *op.cit.*, p. 1171.

¹²⁰ UNIDROIT Principles of International Commercial Contracts (2010), art 6.2.1 available at <http://www.unidroit.org/english/principles/contracts/principles2010/integralversionprinciples2010-e.pdf>.

the equilibrium of the contract. This could mean that the cost of a party's performance has increased or the value of the performance a party receives has diminished.

It is important to distinguish between force majeure and hardship because only in the first case the State is excused, while the only effect of hardship is that the disadvantaged party, that is, the investor, is entitled to request renegotiations of the contract.¹²¹

One of the main defenses usually affirmed by States is necessity. Necessity is defined under Article 25 of the "*Articles on Responsibility of States for Internationally Wrongful Acts*" and it is considered a ground for precluding the wrongfulness of an act only if the State act represents the sole mean to safeguard an essential interest against a grave and imminent peril. Moreover, necessity cannot be invoked if the State has contributed to the situation of necessity.¹²²

A hallmark case concerning necessity is the Gabčíkovo-Nagymaros case that describes the significance of article 25. In particular, in that circumstance the International Court of Justice affirmed that Hungary could not invoke Article 33 (today Article 25) because, even if the State wanted to safeguard an essential interest (natural environment), the peril was not imminent because Hungary could use other means than the suspension and abandonment of works.¹²³

In recent years the necessity defenses have been widely invoked by Argentina. During the Argentine crisis, the State resorted to actions often established as violations of the BITs in force and Argentina often invoked as justification the

¹²¹ *Id.*

¹²² Draft articles on Responsibility of States for Internationally Wrongful Acts, with commentaries 2001 available at http://legal.un.org/ilc/texts/instruments/english/commentaries/9_6_2001.pdf.

¹²³ Case Concerning the *Gabčíkovo-Nagymaros Project* (Hungary/ Slovakia), Judgment of 25 September 1997, 1997 ICJ 7 ¶ 49-57.

necessity defense. Even if numerous cases have been decided, this area of investor-state arbitration remains unclear and full of contradictions.

The main problem is represented by the fact that the BITs subject to analysis did not contain a necessity clause but referred to another concept: the essential security interest and the public order.

Some ICSID tribunals recognized the two provisions as the same, others distinguished them but never identifying the real meaning of the essential security interest clause. Other tribunals stated that, even if necessity was not openly established in the BITs, Argentina could invoke it under customary international law.

Considering the essential security interest and the necessity as two different concepts, it seems that tribunals consider the requirements of the latter to be more difficult to fulfill. In particular, in order to invoke necessity, a State has to prove that such an action represented the only mean to safeguard a State interest, while in the case of essential security interest the State has only to show that beyond its actions there was at least an intent to develop a plan to safeguard a State interest, like environment, public health, the financial stability. In the Argentinian cases, however, some ICSID tribunals, particularly the annulment of arbitral awards, showed that the necessity defenses were not successfully invoked by Argentina because it contributed to the economic and financial crisis of the country.¹²⁴

1.1.4. PARALLEL PROCEEDINGS

If the treaty does not expressly provide for it, there is no requirement to exhaust local remedies as condition precedent to the invocation of the tribunal's

¹²⁴ *Continental Casualty v. The Argentine Republic*, ICSID Case No. ARB/03 /9, Award ¶ 253.

jurisdiction.¹²⁵ As such, an investor does not have to go before the host state courts before invoking investor-state arbitration. It has also been discussed whether or not an exhaustion of local remedies clause makes sense since the original idea behind arbitration was specifically to avoid the domestic court.

Moreover, in the case in which the exhaustion of local remedies is not included in the BIT, the pursuit of local remedies will not preclude the investor from subsequent invocation of a treaty claim unless there is an express treaty provision.¹²⁶ On the contrary, a specific provision in the treaty could require an election in remedies, the so-called fork in the road, to be made, or a treaty provision requiring the waiver of all claims as a condition of valid invocation of treaty arbitration.¹²⁷

Sometimes agreements contain a “Cooling Off Period” provision¹²⁸ This is intended to encourage disputants to engage in consultation and negotiation for a period of three to six months, and to give them the opportunity to amicably and confidentially reach a possible solution on their own.¹²⁹ However, the cooling off period clause presents the issue that it is very difficult to verify whether the parties actually tried to solve the dispute through amicable discussion or not before invoking arbitration.

¹²⁵ B. YIMER, N. CISNEROS, L. BISIANI, R. DONDE, *Application Of International Investment Agreements By Domestic Courts*, Geneva, 2011, p. 9; C. MCLACHLAN, L. SHORE, M. WEINIGER, *op.cit.*, 128(specifying that the exhaustion of local remedies is usually not required).

¹²⁶ L. E. SALLES, *Forum Shopping In International Adjudication: The Role Of Preliminary Objections*, Cambridge, 201, p. 245; C. MCLACHLAN, L. SHORE, M. WEINIGER, *op.cit.*, 129 (defining the fork in the road and the waiver).

¹²⁷ L. E. SALLES, *op.cit.*, 127; C. MCLACHLAN, L. SHORE, M. WEINIGER, *op.cit.*, 29.

¹²⁸ J. DAHLQUIST, *Emergency Arbitrators in Investment Treaty Disputes* in *Kluwer Arbitration blog*, 2015 available at <http://kluwerarbitrationblog.com/2015/03/10/emergency-arbitrators-in-investment-treaty-disputes/>; B. YIMER, N. CISNEROS, L. BISIANI, R. DONDE, *op.cit.*, 12(introducing the cooling off period).

¹²⁹ J. DAHLQUIST *op.cit.*; B. YIMER, N. CISNEROS, L. BISIANI, R. DONDE, *op.cit.*, 12 (defining the cooling off period).

It is also possible that the same underlying dispute gives rise to claims under two different investment treaties before different tribunals; each tribunal could be faced with a potential problem of parallel proceedings within the same legal order: *res judicata* and *lis pendens*.¹³⁰ The doctrine of *res judicata* applies to the decisions of international arbitral tribunals as a general principle of law common to civilized nations.¹³¹ In applying the doctrine to another arbitral award, the tribunal must consider whether there is sufficient identity of parties, subject matter, and cause of action.¹³² Concerning the concept of *lis pendens*, the existence of proceedings before another international tribunal, in which substantially the same matter is raised for determination, entitles the tribunal to stay its proceedings as an exercise of its discretion.¹³³

1.2. MULTILATERAL INVESTMENT TREATIES IN FORCE

Even if globalization has created many global organizations and agreements, there is still no multilateral agreement on foreign investment in force. This represent a gaping hole in the current global economic architecture.

In the past, a multilateral investment agreement (MIA) was discussed but no agreement was ever concluded. In Bretton Woods, the creation of an International Trade Organization (ITO) was recommended as a complement of the World Bank

¹³⁰ P. J. MARTINEZ-FRAGA, H. J. SAMRA, *A Defense of Dissents in Investment Arbitration*, in *U. Miami Inter-Am. L. Rev.*, 2012; C. MCLACHLAN, L. SHORE, M. WEINIGER, *op.cit.*, 130(addressing the problems of *res judicata* and *lis pendens*).

¹³¹ P. J. MARTINEZ-FRAGA, H. J. SAMRA, *op.cit.*; C. MCLACHLAN, L. SHORE, M. WEINIGER, *op.cit.*, 130 (clarifying the concept of *res judicata*).

¹³² P. J. MARTINEZ-FRAGA, H. J. SAMRA, *op.cit.*; C. MCLACHLAN, L. SHORE, M. WEINIGER, *op.cit.*, 130 (discussing the problem of *res iudicata* in investment arbitration).

¹³³ C. MCLACHLAN, L. SHORE, M. WEINIGER, *op.cit.*, 121; E. D'ALTERIO, *From Judicial Comity To Legal Comity: A Judicial Solution To Global Disorder?* in *Int'l J. Constitutional Law*, 2011, p. 404 (considering the concept of *lis pendens* and how it works in investment arbitration).

and the Monetary Fund. In 1948, negotiations on the ITO were completed in Havana, and it established liberal conditions for both trade and investment. However, the Havana Charter never came into force. Instead, in 1947, the General Agreement on Tariffs and Trade (GATT) was concluded in Geneva. The failure of the ITO blocked the development of an international organization for investment, since GATT only took care of trade issues.

Considering the lack of a multilateral investment treaty, this paragraph will focus on three free trade agreements (FTAs) that contain an investment chapter.¹³⁴

Consequently, it is important to specify the differences between BITs and FTA. A BIT is a treaty between only two states that governs the codification of rules and handling of investment disputes between a member state, a country party to an international agreement, and the individuals and companies of the other member state.¹³⁵

An FTA is a trade arrangement between two or more countries and serves to provide all parties to the deal preferential treatment in trade by removing tariffs and nontariff barriers between members of the agreement.¹³⁶ Consequently, while FTAs may often be similar in effect to BITs, the basic objectives of FTAs and BITs differ.¹³⁷ BITs seek to promote investment between a pair of countries by providing investors with confidence in foreign regulatory environments.¹³⁸ FTAs are

¹³⁴ C. MCLACHLAN, L. SHORE, M. MEINIGER, *op.cit.*

¹³⁵ R. THIRGOOD, *Bilateral Investment Treaties - providing unlimited opportunities in The Global Legal Post*, 2014, available at <http://www.globallegalpost.com/global-view/bilateral-investment-treaties---providing-unlimited-opportunities-58721287/>; M. WEAVER, *op.cit.*, 228 (stating that BITs are different from FTAs).

¹³⁶ R. THIRGOOD, *op.cit.*, 123; M. WEAVER, *op.cit.*, 228 (specifying what a FTA is).

¹³⁷ R. THIRGOOD, *op.cit.*, 123; M. WEAVER, *op.cit.*, 228 (noting that even if similar the BITs and the FTAs have different objectives).

¹³⁸ R. THIRGOOD, *op.cit.*, 123; M. WEAVER, *op.cit.*, 228 (discussing the scope of the BITs).

mechanisms for trade liberalization that aim to eliminate discrimination against imports by removing tariffs and other restrictions on the trade of goods.¹³⁹

In the past, BITs and FTAs were two separate and parallel legal instruments that had to address issues in different fields.¹⁴⁰ Nowadays, there are more and more FTAs being concluded and many of them have an investment chapter.¹⁴¹ Trade and investment are more integrated, encompassing various emerging elements of international commerce: exports, imports used in exports, use of foreign affiliates for sale, globalized production and distribution in foreign direct investments.¹⁴² Finally, this paragraph will focus on the ICSID Convention, that establishes the most important current investor-state mechanism.

1.2.1. ICSID CONVENTION

ICSID is the leading institution for the resolution of international investment disputes. It was established under the Convention on the Settlement of Investment Disputes and it is one of the five international organizations of the World Bank Group.¹⁴³

The purpose of the Centre is to provide facilities for conciliation and arbitration of investment disputes between Contracting States and nationals of other Contracting States.¹⁴⁴

¹³⁹ R. THIRGOOD, *op.cit.*, 123; M. WEAVER, *op.cit.*, 228 (describing the general scope of FTAs).

¹⁴⁰ L. E. TRAKMAN, N. W. RANIERI, *Regionalism in International Investment Law*, Oxford, 2013, p. 22 (discussing how BITs and FTAs were considered in the past).

¹⁴¹ L. E. TRAKMAN, N. W. RANIERI, *op.cit.*, 22 (considering that the content of FTA has changed).

¹⁴² L. E. TRAKMAN, N. W. RANIERI, *op.cit.*, 22 (stating that trade and investments are two connected subject).

¹⁴³ ICSID.

¹⁴⁴ ICSID, art. 1(2).

The Administrative Council is composed of one representative of each Contracting State.¹⁴⁵ The Chairman of the Administrative Council is the President of the World Bank.¹⁴⁶

Persons designated to serve on the Panels must be persons of high moral character and recognized competence in specific fields, like law, commerce, industry or finance.¹⁴⁷

The jurisdiction of the Centre covers any legal dispute arising directly out of an investment, between a Contracting State (or subdivision or agency of a State designated to the Centre by that State) and a national of another Contracting State.¹⁴⁸ The parties must give consent in writing to submit to the Centre and the consent cannot be withdrawn unilaterally.¹⁴⁹ A national is any natural person who had the nationality of a Contracting State other than the State party to the dispute on the date of the consent and on the date of the request registration.¹⁵⁰ A national is also any juridical person with the nationality of a Contracting State other than the State party to the dispute on the date of the consent and any juridical person with the nationality of the Contracting State party to the dispute on that date, that the parties agreed to treat as a national of another Contracting State because of foreign control.¹⁵¹

Consent of the parties to arbitration under this convention usually excludes other remedies unless otherwise stated.¹⁵² A Contracting State may require the

¹⁴⁵ ICSID, art. 4 (1).

¹⁴⁶ ICSID, art. 5.

¹⁴⁷ ICSID, art. 14(1).

¹⁴⁸ ICSID, art. 25.

¹⁴⁹ *Id.*

¹⁵⁰ *Id.*

¹⁵¹ *Id.*

¹⁵² ICSID, art 26.

exhaustion of local remedies as a condition of its consent to arbitration under this Convention.¹⁵³

The proceeding in ICSID starts when the Secretary-General sends a copy of the request to the tribunal to the other party. The request contains the issues in dispute, the identity of the parties and the parties' consent to arbitration. The Secretary-General will register the request unless the dispute is manifestly outside the jurisdiction of the Centre.¹⁵⁴

The Tribunal can consist of a sole arbitrator or a number of arbitrators appointed at the discretion of the parties. If the parties do not agree, there will be three arbitrators, one appointed by each party and the third appointed by agreement of the parties.¹⁵⁵

The award shall be binding on the parties and shall not be subject to any appeal or to any other remedy except those provided for in the Convention.¹⁵⁶ The Convention gives the possibility to request annulment of the award on one of the following grounds: the Tribunal was not properly constituted; the Tribunal has manifestly exceeded its powers; there was corruption on the part of a member of the Tribunal; there has been a serious departure from a fundamental rule of procedure; or the award has failed to state the reasons on which it is based.¹⁵⁷ Conciliation and arbitration proceedings are usually held at the seat of the Centre except if the parties agree otherwise.¹⁵⁸

¹⁵³ *Id.*

¹⁵⁴ ICSID, art. 36.

¹⁵⁵ ICSID, art. 37.

¹⁵⁶ ICSID, art. 53 (1).

¹⁵⁷ ICSID, art. 52.

¹⁵⁸ ICSID, art. 62.

Pursuant to Article 6 of the Convention, the Council adopted the Regulations and Rules that complement the provisions of the Convention.¹⁵⁹ In addition, the Council has adopted a set of Additional Facility Rules, which provide that the ICSID Secretariat is authorized to administer certain types of proceedings between States and foreign nationals that fall outside the scope of the ICSID Convention.¹⁶⁰ These include fact-finding proceedings for the settlement of investment disputes where either the State party to the dispute or the home State of the foreign national is not an ICSID Convention Contracting State.¹⁶¹

In conclusion, since investment treaties make available ICSID arbitration to protect investors, the ICSID Convention represents the most successful institution for investor state arbitration.¹⁶²

1.2.2. ASEAN INVESTMENT AGREEMENT

Brunei, Cambodia, Indonesia, Malaysia, Myanmar, the Philippines, Singapore, Thailand, Laos and Vietnam signed the Association of South-Eastern Asian Nations (ASEAN) in 1987.¹⁶³ The ASEAN agreement resembles a BIT and Article II presents a notable difference to standard BITs as it requires an investment to be specifically approved in writing and registered by the host country to obtain coverage.¹⁶⁴ Moreover, corporations must have their effective management in the

¹⁵⁹ ICSID, art. 6.

¹⁶⁰ ADDITIONAL FACILITIES RULES.

¹⁶¹ ADDITIONAL FACILITIES RULES.

¹⁶² A. DEL VECCHIO, *I Tribunali Internazionali Tra Globalizzazione E Localismi*, Bari, 2009, p. 64 ff.

¹⁶³ ASEAN Agreement.

¹⁶⁴ C. MCLACHLAN, L. SHORE, M. WEINIGER, *op.cit.*

territory of a contracting party in order to qualify as a “company” of a contracting party.¹⁶⁵

On 26 February 2009 a new Comprehensive Investment Treaty has been signed by the same members of the previous agreement. The intention is to intensify economic cooperation between and among the Member States. This treaty superseded, at its entry into force in 2012, the earlier Agreement for the Promotion and Protection of Investments signed in 1987.

The treaty grants most of the protections contained by bilateral and multilateral investment treaties, including the assurances of national treatment, most-favored nation treatment, fair and equitable treatment, full protection and security and provisions in respect of expropriation and compensation. One valuable component of the ACIA is its Investor-State Dispute Settlement mechanisms and the promotion of alternative dispute resolution methods. ASEAN investment disputes can be resolved by using domestic courts and tribunals, through international arbitration including ICSID, UNCITRAL, ad hoc arbitration, and by means of alternative dispute methods: mediation, conciliation, and consultation & negotiation.¹⁶⁶

ASEAN’s investment treaties show a strong commitment to the promotion of investment through the liberalization of investment rules and the provision of protection for investors through international treaty commitments, confirmed by the ASEAN Plus agreements made by the ASEAN member with other countries.¹⁶⁷

¹⁶⁵ *Yaung Chi Oo Trading Pte Ltd v. Government of the Union of Myanmar*, ICSID Additional Facility Rules Case No. ARB/01/1 (31 March 2003), 42 ILM 540 (2003).

¹⁶⁶ ACIA OVERVIEW, <http://www.dejudomlaw.com/asean-law/the-asean-comprehensive-investment-agreement-an-overview/>.

¹⁶⁷ V. BATH, L. R. NOTTAGE, *The ASEAN Comprehensive Investment Agreement and ‘ASEAN Plus’ – The Australia-New Zealand Free Trade Area (AANZFTA) and the PRC-ASEAN Investment Agreement* (September 26, 2013); M. BUNGENBERG, J. GRIEBEL, S. HOBE, A. REINISCH, *International Investment Law: A Handbook*, eds., Nomos Verlagsgesellschaft: Germany, 2015.

1.2.3. ENERGY CHARTER TREATY (ECT)

In order to develop the energy cooperation between Eastern and Western Europe, the Energy Charter treaty was realized. The treaty was opened for signature in 1994 and Signatories include all countries of the Former Soviet Union, Central and Eastern European States, Japan, Australia, the European Union and its member states.¹⁶⁸

The ECT is a multilateral treaty limited in its scope to the energy sector. The purpose of the ECT, under Article 2, is to ‘promote long-term co-operation in the energy field, based on complementarities and mutual benefits, in accordance with the objectives and principles of the Charter’. The ECT includes provisions regarding investment protection, provisions on trade, transit of energy, energy efficiency and environmental protection and dispute resolution.

The aim of the foreign investment regime is to create a ‘level playing field’ for investments in the energy sector and to minimize the non-commercial risks associated with such investments. Under the ECT there is a distinction between the pre-investment phase and the post-investment phase. While the provisions concerning the pre-investment phase set up a ‘soft’ regime, the ECT creates a ‘hard’ regime for the post-investment phase with binding obligations for the contracting states similar to the investment protection provisions of the NAFTA and bilateral investment treaties BITs. Under the Energy Charter Treaty, once the cooling-off period has come to an end, an investor can choose between a domestic court of the contracting party, ICSID or international arbitration under the UNCITRAL or Stockholm Chamber of Commerce Rules.

¹⁶⁸ Energy Charter Treaty.

The final awards issued between former shareholders of Yukos and the Russian Federation are among the most discussed cases in the investor-state dispute settlement. Under the Energy Charter treaty, since the commencement of the first arbitration on 25 April 2001, 61 cases arose and this shows that the Energy Charter Treaty is considered to be a successful and well-functioning legal instrument thus far.¹⁶⁹

1.2.4. NAFTA

Canada, Mexico and United States signed the North American Free Trade Agreement (NAFTA) in 1992. One of NAFTA's most unique features is chapter 11, dedicated to the protection of foreign investors. NAFTA is one of the first international trade agreements where member states waive sovereign immunity and open themselves up to liability, allowing private investors to directly challenge host-nations through dispute resolution.

Investors complaining about unfair treatment by host nations may submit their disputes to binding arbitration. Article 1120 provides that the arbitral procedure is determined by the petitioner's choice between the ICSID Convention, the Additional Facility Rules of the ICSID Convention, or the arbitral rules of the United Nations Commission on International Trade Law (UNCITRAL).¹⁷⁰

Regarding the definitions, the definition of investment under NAFTA is similar to those definitions in the modern BITs, but NAFTA contains a brief list of assets that do not fall within the common definition (commercial contracts for the sale of

¹⁶⁹ R. BAMFORTH, *A look at the Energy Charter Treaty ten years on*, 2008, available at <http://www.olswang.com/articles/2008/06/a-look-at-the-energy-charter-treaty-ten-years-on/>.

¹⁷⁰ J. HARBINE, *Nafta Chapter 11 Arbitration: Deciding The Price Of Free Trade*, in *Ecology Law Quarterly*, 2002.

goods or services, for example).¹⁷¹ At the same time, the definition of investor specifically excludes a corporation with no substantial existence in the territory.¹⁷²

Concerning substantial rights, and in particular expropriation, under Article 1110 parties may not expropriate investments, neither directly nor indirectly, nor through any measures tantamount to expropriation, unless such expropriation is non-discriminatory, is established in pursuit of a public purpose, meets international minimum standards of treatment, and is accompanied by compensation at fair market value.¹⁷³

One characteristic of the treaty that distinguishes it from other multilateral trade agreements is the power of a commission, the NAFTA Free Trade Commission, to issue binding interpretations of NAFTA provisions where parties agree to be bound.¹⁷⁴

NAFTA allows two categories of claims: a claim by an investor of a party arising out of loss or damage suffered as result of another NAFTA party breaching an obligation; a claim by an investor of a party on behalf of an enterprise with a different NAFTA nationality.¹⁷⁵

In conclusion, NAFTA represents one of the most important free trade agreements, the first one between one developing country (Mexico) and two developed countries (United States and Canada) and as such, especially chapter 11 has drawn a number of concerns regarding whether or not the Chapter is overly

¹⁷¹ See NAFTA, CHAPTER 11, art 1139.

¹⁷² NAFTA, CHAPTER 11, art 1139.

¹⁷³ NAFTA, CHAPTER 11, art 1110.

¹⁷⁴ NAFTA, CHAPTER 11, art 1131(2).

¹⁷⁵ NAFTA, CHAPTER 11, art. 1116-1117.

protective of investors and, as a result, inappropriately infringes on a state's ability to regulate investment within its borders.¹⁷⁶

¹⁷⁶ M. A. VILLARREAL, I. F. FERGUSON, *The North American Free Trade Agreement (NAFTA)*, 2015, available at <https://www.fas.org/sgp/crs/row/R42965.pdf>.

CHAPTER 2 - THE EUROPEAN UNION COMPETENCE IN THE INVESTMENTS AND EU PRACTICE IN THE CONDUCT OF TRADE NEGOTIATIONS

ABSTRACT: 2.1. COMPETENCE OF THE EUROPEAN UNION IN INVESTMENT- 2.1.1 SITUATION BEFORE THE LISBON TREATY ENTERED INTO FORCE- 2.1.2. SITUATION AFTER THE LISBON TREATY- 2.2. EUROPEAN UNION AND THE DECISION MAKING PROCESS IN THE NEGOTIATION OF FREE TRADE AGREEMENTS

The Union during the last years has reached a lot of achievements in the sphere of its investment policy: in 2009 the Union integrated Article 207 of the Treaty on the Functioning of the European Union (TFEU), in 2013 the Grandfathering regulation settled different issues concerning the old and the new Member State BITs in the EU legal system and in 2014, the last outstanding cornerstone, the Financial Responsibility Regulation was adopted.¹⁷⁷

Moreover, since 2010, on the basis of the new article 207 TFEU, the Commission sets out an agenda for EU trade negotiations that included investment chapters: thus EU-Canada, EU-India, EU-Singapore and EU-Mercosur. As affirmed by the Commission, these agreements will contain ISDS provisions and the Commission will deal with them in line with its exclusive competence.¹⁷⁸

¹⁷⁷ See *infra* Chapter 2.1 (summarizing the most important development in the EU investment policy).

¹⁷⁸ EUROPEAN COMMISSION, *Towards a comprehensive European international investment policy*, 2010, available at http://trade.ec.europa.eu/doclib/docs/2010/july/tradoc_146307.pdf; C. BROWN, I. NAGLIS, *Dispute Settlement in Future EU Investment Agreements in EU and Investment Agreements*, Zurich, 2010, p. 23 (referring to the EU negotiations in the investment and trade area).

This Chapter will give a background of the investment competence before the Lisbon Treaty, then analyze the actual situation and some possible developments. Finally, it will describe the method of negotiations of the aforementioned agreements.

2.1. COMPETENCE OF THE EUROPEAN UNION IN INVESTMENT

The investor-state arbitration mechanisms are born in order to protect foreigners that invest in other states.¹⁷⁹ Consequently, it is pivotal to define what a foreign investment consists of, making a distinction between foreign direct investments and other kind of investments, in particular portfolio investments.

There is a foreign investment when a transfer of tangible or intangible assets from one country to another is made in order to generate wealth in that country.¹⁸⁰ If the transfer consists of tangible assets, such as equipment or physical property it is clear that a foreign direct investment is made.¹⁸¹

This can be contrasted by a portfolio investment, usually represented by a movement of money for the purposes of purchasing shares in a foreign company.¹⁸² In portfolio investment, the investor usually takes the risk involved in order to make the investment.¹⁸³

¹⁷⁹ *See generally* Paragraph 1.1. (clarifying the scope of the investor-state arbitration).

¹⁸⁰ M. SORNARAJAH, *The International Law on Foreign Investment*, Cambridge, 2010, p. 8 (giving a definition of foreign investment).

¹⁸¹ *Id.* (describing foreign direct investment).

¹⁸² *Id.* (analyzing portfolio investment).

¹⁸³ *Id.* (illustrating the difference between portfolio investment and foreign direct investment).

A minority view accepts that customary international law protects not only foreign direct investment but also portfolio investment, as risk is assumed in making both types of investment.¹⁸⁴

However, the majority view believes that only foreign direct investments are protected by international law.¹⁸⁵ This is primarily because, only in the case of foreign direct investment, the host state court expressly accepts the investment.¹⁸⁶ On the contrary, in portfolio investments there is no responsibility on the host state because it does not know the source of the investment created by the sale of shares around the world.¹⁸⁷

In conclusion, the trend is that portfolio investments are not protected, unless expressly included in the definition of foreign investments in the relevant treaty.¹⁸⁸

After a long process, the Treaty of Lisbon entered into force in 2009 and it completely innovated the powers of the European Union in the investment policy. Paragraph 2.1.1 discusses the situation in the investment area before the Lisbon Treaty entered into force and all the steps that brought to the innovation of 2009. Paragraph 2.1.2 analyzes the complicated situation after the amendment of the article 207 TFEU and which will probably be the future developments in the area.

2.1.1. SITUATION BEFORE THE LISBON TREATY

¹⁸⁴ *Id.* (referring to a minority view in international law).

¹⁸⁵ *Id.* (affirming that generally only foreign direct investments are protected in international law).

¹⁸⁶ *Id.* (explaining the basis for the majority view).

¹⁸⁷ *Id.* (clarifying why portfolio investments are usually excluded from protection).

¹⁸⁸ *Id.* (summarizing the main point on foreign investments).

Since the first bilateral investment treaty in 1957 between an EU Member State (Germany-Pakistan BIT), an era characterized by bilateral investment treaties started. By the time the Lisbon Treaty entered into force, more than 1,200 bilateral investment treaties had been concluded by EU Member States with third countries.¹⁸⁹ By the end of 2011, there were 436 known investment disputed cases under ISDS mechanisms included in the BITs.¹⁹⁰

While the Member States have tried to ensure the protection of their foreign investors and attraction of investment since the 50's, the Treaty establishing the European Economic Community limited the competence for the Common Commercial Policy to trade in goods.¹⁹¹

In 1994 the European Court of Justice (ECJ) issued the Opinion 1/94 that ruled that the EC had competence in relation to the cross-border mode of supply of services. After the amendments of the Treaty of Amsterdam (1997) and Nice (2001), the European Union's competence in services was expanded and it was confirmed by the Opinion 1/08, issued by the ECJ the day before the Treaty of

¹⁸⁹ EUROPEAN COMMISSION, *Towards a comprehensive European international investment policy*, 2010, available at http://trade.ec.europa.eu/doclib/docs/2010/july/tradoc_146307.pdf (indicating some data on BITs in EU).

¹⁹⁰ 390 cases mentioned in UNCTAD, *Non-Equity Modes of International Production and Development*, 2011, available at http://unctad.org/en/PublicationsLibrary/wir2011_en.pdf (referring to the known investor-state arbitration in EU).

¹⁹¹ Article 113 ECC affirmed that: “1. *After the expiry of the transitional period, the common commercial policy shall be based on uniform principles, particularly in regard to tariff amendments, the conclusion of tariff or trade agreements, the alignment of measures of liberalisation, export policy and protective commercial measures including measures to be taken in cases of dumping or subsidies.* 2. *The Commission shall submit proposals to the Council for the putting into effect of this common commercial policy.* 3. *Where agreements with third countries require to be negotiated, the Commission shall make recommendations to the Council, which will authorize the Commission to open the necessary negotiations. The Commission shall conduct these negotiations in consultation with a special Committee appointed by the Council to assist the Commission in this task and within the framework of such directives as the Council may issue to it.* 4. *The Council shall, when exercising the powers conferred upon it by this Article, act by means of a qualified majority vote.*” (describing the policy of the EU).

Lisbon came into force, which impliedly stated the Community had already competence for investment in the service sector before the Lisbon Treaty.¹⁹²

Outside the sector of services, before the Lisbon Treaty, investment was considered to be an area of mixed competence. This means that both the Union and the Member States could legislate and adopt legally binding acts in the investment area. However, the Member States should have only exercised their competence to the extent the Union has not exercised its competence. The Union had the regulatory power to curtail the scope for exercising national regulatory power with respect to the same sector.¹⁹³

The European Union had a shared competence in international investment matters because the European Union had not authorized either express or implied exclusive competence in the area.¹⁹⁴

In particular, in Opinion 2/92, the Court held that the national treatment provision, that is related to foreign direct investments, is related only partially to

¹⁹² Opinion of the Court (Grand Chamber) of 30 November 2009. Opinion pursuant to Article 300(6) EC - General Agreement on Trade in Services (GATS) - Schedules of specific commitments - Conclusion of agreements on the grant of compensation for modification and withdrawal of certain commitments following the accession of new Member States to the European Union - Shared competence - Legal bases - Common commercial policy - Common transport policy. Opinion 1/08 available at <http://curia.europa.eu/juris/liste.jsf?language=en&num=C-1/08> (analyzing the competence of EU in the investment of services).

¹⁹³ A. DASHWOOD, M. DOUGAN, D. RODGER, B., E. SPAVENTA, D. WYATT, *Wyatt and Dashwood's European Union Law*, Oxford, 2011 p. 100; BROWN, I. NAGLIS *op.cit.*, 18 ff. (clarifying the concept of shared competence).

¹⁹⁴ Exclusive competence might also be established on the basis of the nature of the measure to be adopted, as established in Opinion 1/76 [1977] ECR 741. However, as confirmed by the ECJ in its Opinions 1/94 and 2/92, this principle does not apply to international investment treaty-making: see Opinion 1/94, WTO [1994] ECR I-5267, at paras 84-86; Opinion 2/92, OECD-National Treatment Investment [1995] ECR I-521, at para. 32 (explaining the reasoning behind the shared competence).

international trade and therefore Article 113 of the EEC could not be used as the legal basis for the exclusive Community competence in investments.¹⁹⁵

In 2006, the European Commission published its ‘Communication Global Europe: Competing in the World.’ ‘Global Europe’ stressed the need to pursue a “far-reaching liberalization of services and investment”.¹⁹⁶ In particular, in that occasion, the European Commission clearly affirmed its will to commit to FTAs “*by going further and faster in promoting openness and integration, by tackling issues which are not ready for multilateral discussion and by preparing the ground for the next level of multilateral liberalization. Many key issues, including investment, public procurement, competition, other regulatory issues and IPR enforcement, which remain outside the WTO at this time can be addressed through FTAs.*”¹⁹⁷

This shared competence brought in 2006 to the Minimum Platform on Investment for EU Free Trade Agreements (MPoI), and a few cases before the European Courts, regarding BITs between EU Member States and third states and BITs between different EU Member States.

The Minimum Platform on Investment for EU FTAs was adopted by the Council of the EU on 27 November 2006.¹⁹⁸ With this proposal the Commission has sent a signal that it wants to acquire all the competence to negotiate future

¹⁹⁵ Opinion 2/92, OECD-National Treatment Investment [1995] ECR I-521, at paras. 18-28 (stating the position of the Court on the EU competence in investments).

¹⁹⁶ EUROPEAN COMMISSION, *Competing in the World*, 2006 available at http://trade.ec.europa.eu/doclib/docs/2006/october/tradoc_130376.pdf (describing the position of the Commission of the EU competence in investments).

¹⁹⁷ *Id.* (describing the intention of the Commission to negotiate FTA with investment chapters).

¹⁹⁸ EUROPEAN COMMISSION, *Minimum platform on investment for EU FTAs – Provisions on establishment in template for a Title on “Establishment, trade in services and e-commerce.* European Commission 38/06. http://www.iisd.org/pdf/2006/itn_ecom.pdf (introducing the Minimum Platform on Investment).

investment agreements and it tries to satisfy the need of an accord on investment chapter when a potential FTA will be under negotiation.¹⁹⁹

The MPoI had to represent the basis on which ‘an ambitious investment policy’ had to be constructed.²⁰⁰ It was the first formalized EC approach towards the international investment sector.²⁰¹ However, legally it was only a negotiation scheme which had not been formally published, it did not represent a formal EU regulation. Clearly after the MPoI, foreign investment remained an area of shared competence between the Union and its Member States.

However, the negotiating mandates authorizing the Commission to negotiate with third parties contained clear references to the Platform reflected in, amongst others, the EU Cariforum European Partnership Agreement (EPA), the EU-Korea FTA and the negotiating mandate of the agreement between the EU and India.²⁰²

In addition, the Commission's effort to assert investment competence is visible in some cases, such as the cases against Sweden, Austria, and Finland before the European Court of Justice.

In 2004, the Commission notified Austria, Finland, Sweden, and Denmark that some of their BITs with non-EU countries, guaranteeing the free movement of investment-related transfers, could have been in conflict with the powers reserved

¹⁹⁹ N. MAYDELL, *The European Community's Minimum Platform on Investment or the Trojan Horse of Investment Competence*, in *International Investment Law in Context*, Vienna, 2007, p. 75 (describing the intention of the Commission to acquire competence in investments).

²⁰⁰ See ‘Remarks’ in the draft ‘Minimum Platform on Investment for EU Free Trade Agreements’, by the Commission for the discussion of the 133 Committee, 28 July 2006, available at www.iisd.org/pdf/2006/itn_ecom.pdf (referring to the value of the Commission proposal).

²⁰¹ N. MAYDELL, *op.cit.*, 73 (stating the value of the Commission proposal).

²⁰² R. VAN OS, *Pre-Lisbon external investment policy of the Eu*, in *SOMO*, 2010, available at <http://focusweb.org/sites/www.focusweb.org/files/EU%20policy%20on%20FDI%20after%20Lisbon.pdf> (affirming the value of the Minimum Platform, even if it was not binding).

for the EU.²⁰³ The EC considered that the BITs in question might hinder the application of the restrictive measures that the Council of Ministers, in exceptional circumstance, in the free movement of capital can take. According to the Article 307 of the EC Treaty, Community law does not automatically prevail on international agreements concluded by Member States before the date of their accession. However, by virtue of that same Article, Member States are obliged to take all appropriate steps to eliminate possible incompatibilities contained in such prior international agreements.²⁰⁴

After that, Member States, except Denmark, rejected the EC's request for BIT modification, and the Commission took Sweden and Austria to the ECJ in 2006 and started a similar proceeding against Finland later.²⁰⁵

The ECJ ruled that Austria and Sweden had not fulfilled their obligations under Article 307 TEC.²⁰⁶ Importantly, the ECJ explicitly held that its findings were 'not limited to the Member State which is the defendant in the present case'.²⁰⁷ This could have been a suggestion that all the EU Member State BITs may also have been deemed to be in violation of the EC Treaty to the extent that they

²⁰³ D. VIS-DUNBAR, *European Governments defend BITs in lawsuit brought by EU executive branch*, in *Investment Treaty News*, 2007, available at: www.iisd.org/pdf/2007/itn_mar16_2007.pdf (introducing some cases concerning BITs between Member States and non-Member States)

²⁰⁴ EC Treaty, art. 307 (introducing the problem of possible incompatibilities between the BITs and the European Union law).

²⁰⁵ D. VIS-DUNBAR, *European Court of Justice rules that certain Swedish and Austrian BITs are incompatible with the EC Treaty*, in *Investment Treaty News*, 2009, available at: www.investmenttreatynews.org/cms/news/archive/2009/03/04/european-court-of-justice-rules-that-certain-swedish-and-austrian-bits-are-incompatible-with-the-ec-treaty.aspx (describing the action of the Commission against Sweden and Austria).

²⁰⁶ *Id.* (stating the holding of the ECJ).

²⁰⁷ Case C-249/06, EC Commission v. Sweden, judgment of 3 Mar. 2009, at para. 43, (stressing the extend of the holding of the ECJ).

contained similar provisions. On 19 November 2009, a similar ruling was delivered in *Commission v. Finland*.²⁰⁸

These cases have stated the supremacy of EC (now EU) law over national law, since BITs of Member States can be considered as part of the national legal order. It also demonstrates that the Union has competence in foreign investment matters.

In addition to the aforementioned ECJ cases related to BITs between EU Member States and non-EU states, the Commission has also started proceedings over BITs between EU Member States, on the grounds that they overlap with EC law.

In 2006, the Commission addressed a note to the Economic and Financial Committee of the Council (EFC) of the EU concerning the intra-EU BITs. The Commission suggested in that note 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. It would appear that most of their content is superseded by Community law upon accession of the respective Member State.”*²⁰⁹ The Commission also warned of probable issues: investors could try to avoid national courts by submitting claims to BIT arbitration (forum shopping) with the possible outcome of an unequal treatment of investors among Member States.²¹⁰

²⁰⁸ Case C-118/07, *Commission v. Finland*. See PLC Arbitration, ‘ECJ finds Finland’s BITs breach article 307 of the EC Treaty’, available at: <http://arbitration.practicallaw.com/1-500-8076> (referring to a case with a similar holding).

²⁰⁹ D. VIS-DUNBAR, *EU Members review intra-European BITs in light of potential overlap with EU law*, in *Investment Treaty News*, 2007, available at: www.iisd.org/pdf/2007/itn_june30_2007.pdf (stating the Commission opinion on intra-EU BITs).

²¹⁰ D. VIS-DUNBAR, *EU member states reject the call to terminate intra-EU bilateral investment treaties*, in *Investment Treaty News*, 2009, available at: www.investmenttreatynews.org/cms/news/archive/2009/02/10/eu-member-states-reject-the-call-to-terminate-intra-eu-bilateral-investment-treaties.aspx (addressing a problem stated by the Commission).

However, the EFC wrote in February 2009 to the President of the Council of the European Union that '*[m]ost member states did not share the Commission's concern regarding arbitration risks and discriminatory treatment of investors and a clear majority of member states preferred to maintain the existing agreements*'.²¹¹

In some investment arbitration cases involving this problem, arbitrators have affirmed that intra-EU BITs were not implicitly terminated when those countries acceded to the EU.²¹²

However, different EU Member States, such as Czech Republic, Slovenia, Malta and Italy, have announced their plans to terminate their intra-EU BITs.²¹³ On the contrary, other EU Member States, such as Belgium, Germany, the Netherlands, and the United Kingdom do not agree with these nations' approach.²¹⁴

Finally, the Commission successfully applied to intervene in two investment treaty arbitration cases, both to Hungary.²¹⁵ The claims were targeted at Hungarian government requirements to make changes to long-term contracts in the electricity

²¹¹ *Id.* (stating how the Council answered the issue addressed by the Commission).

²¹² In *Eastern Sugar BV (Netherlands) v. The Czech Republic*, SCC No. 088/2004.

²¹³ D. VIS-DUNBAR, *Czech Republic pursues shake-up of its bilateral investment treaties*, in *Investment Treaty News*, 2005, available at: www.iisd.org/pdf/2005/investment_investsd_nov21_2005.pdf; See 'Italy, Slovenia and Malta concur with Czech Republic on lack of necessity for intra-EU BITs; Italy-Czech treaty has been terminated' and 'Denmark and Czech Republic working to terminate investment treaty; not all EU member-states agree with the Czech view that intra-EU treaties are unnecessary', *Investment Arbitration Reporter*, 6 Aug. 2009 and 17 July 2009; 'Italy, Slovenia and Malta concur with Czech Republic on lack of necessity for intra-EU BITs; Italy-Czech treaty has been terminated', *Investment Arbitration Reporter*, 6 Aug. 2009.

²¹⁴ See the articles, *supra* note 205,206,207 (clarifying the approach of Member States on intra-EU BITs).

²¹⁵ *AES Summit Generation Limited and AES-Tisza Erömü Kft v. Republic of Hungary* (ICSID Case No. ARB/07/22), award of 23 Sept. 2010, available at: http://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=showDoc&docId=DC1730_En&caseId=C114 (accessed on 10 Oct. 2010); and *Electrabel SA v. Republic of Hungary* (ICSID Case No. ARB/07/19) (describing the action taken by the Commission).

field, before Hungary's accession to the EU.²¹⁶ In both cases, the Commission, filing non-party submissions, intervened to defend Hungary's actions as being required by EU law.²¹⁷ The Commission challenged the jurisdiction of the tribunal on the ground that the dispute arisen was subject to EU law, and therefore within the jurisdiction of the Commission.²¹⁸

In conclusion, it is visible that there has been a wide practice relating to the international investment competence of the EU before the Treaty of Lisbon and the Commission has been making efforts to affirm and expand its foreign investment competence. However, the European Courts and the international arbitration tribunals have adopted opposite views. While the ECJ cases upheld the Commission's power to intervene into some provisions of the BITs, the arbitration tribunals ruled that the accession to the EU of one Member State did not implicitly terminate the BITs, because the BITs should be interpreted in accordance with principles of international law.²¹⁹

The two sets of cases strengthened the call for a common investment policy.²²⁰ In particular, the ECJ cases served as a positive confirmation of the power the EU already had in foreign investment matters; the arbitration decisions demonstrate from a negative perspective what complications the EU and its

²¹⁶ This is because they “constitute[d] unlawful and incompatible state aid to the power generators”, and because they unduly restricted competition by preventing new entrants: see L. E. PETERSON, *European Commission seeks to intervene as amicus curiae in ICSID arbitrations to argue that long-term power purchase agreements between Hungary and foreign investors are contrary to European Community Law* in *Investment Arbitration Reporter*, 2008 (describing the issues of the case).

²¹⁷ L. E. PETERSON, *ICSID tribunal will permit European Commission to file legal brief in Energy Charter Treaty arbitration*, in *Investment Arbitration Reporter*, 2008 (explaining the Commission's position in the case in question).

²¹⁸ *Id.* (addressing the Commission's claim).

²¹⁹ BROWN, I. NAGLIS *op.cit.*, 18 ff. (summarizing the precedent points).

²²⁰ A. SHAN, S. ZHANG, *The Treaty of Lisbon: Half Way toward a Common Investment Policy* in *European Journal of International Law*, 2010, p. 623 ff. (affirming the value of the cases).

Member State had to face without a common investment policy at the Union level.²²¹

In general, it appears that EC was in part officially mandated to act on foreign direct investment, anticipating the future Treaty of Lisbon.²²²

2.1.2. SITUATION AFTER THE LISBON TREATY

After the entry into force of the Lisbon Treaty, the article 207 TFEU includes “foreign direct investment” in the scope of the Common Commercial Policy.²²³ By virtue of the Article 3 (1)(e) TFEU, foreign direct investments are now part of the “exclusive competence” of the Union.²²⁴ Consequently, in such area, only the Union may legislate and adopt legally binding acts, while the Member States can legislate or implement the Union acts only if so empowered by the Union.²²⁵

In addition, Article 206 of the TFEU now provides that the Union has to develop not only trade but also foreign direct investment, with the abolition of restrictions.²²⁶

²²¹ A. SHAN, S. ZHANG, *op.cit.* (clarifying the problems concerning a shared competence).

²²² R. VAN OS, *op.cit.* (ruling that the competence of the EU in investment was in part anticipated before the Lisbon Treaty).

²²³ TFEU, art. 207: “*The common commercial policy shall be based on uniform principles, particularly with regard to changes in tariff rates, the conclusion of tariff and trade agreements relating to trade in goods and services, and the commercial aspects of intellectual property, foreign direct investment, the achievement of uniformity in measures of liberalisation, export policy and measures to protect trade such as those to be taken in the event of dumping or subsidies. The common commercial policy shall be conducted in the context of the principles and objectives of the Union’s external action.*” (introducing the amendment to article 207 TFEU).

²²⁴ TFEU, art. 3.

²²⁵ TFEU, art. 2.

²²⁶ TFEU, art. 206: “*By establishing a customs union in accordance with Articles 28 to 32, the Union shall contribute, in the common interest, to the harmonious development of world*

If the new provision of article 207 of the TFEU transfers the exclusive competence on FDI to the EU, how this will affect BITs concluded by Member States and whether they become incompatible with EU law, represents a complex issue.²²⁷

In fact, according to the Commission, most of the matters in BITs (standards of protection in the post-investment phase and unlawful expropriation) directly fall within the scope of the EU exclusive competence under the new Article 207 of the TFEU.²²⁸

In order to replace the existing BITs concluded by the Member States, the Commission proposed the ‘Grandfathering Regulation’. This regulation was later adopted by the Council and it establishes transitional arrangements for BITs between Member States and third countries and entered into force in January 2013.²²⁹ Not only does the ‘Grandfathering Regulation’ cover the FDI but it also disciplines the protection of investment and portfolio investments.²³⁰

According to the Regulation, the agreements made by Member States in the area of international law remain binding but the commitments should be addressed from the perspective of the new EU's exclusive competence on foreign direct investment.²³¹

trade, the progressive abolition of restrictions on international trade and on foreign direct investment, and the lowering of customs and other barriers.”

²²⁷ BROWN, I. NAGLIS *op.cit.*, 20 ff. (introducing possible incompatibilities between the EU law and the pre-existent BITs).

²²⁸ *Id.* (stating the Commission’s position on the extent of the exclusive competence in investments).

²²⁹ Regulation (EU) No. 1219/2012 of the European Parliament and of the Council of 12 Dec. 2012, OJ 2012, L 315/40, <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2012:351:0040:0046:En:PDF>.

²³⁰ *Id.*

²³¹ Preamble, Regulation (EU) No. 1219/2012 of the European Parliament and of the Council of 12 Dec. 2012, OJ 2012, L 315/40, <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2012:351:0040:0046:En:PDF>.

Since there is no explicit transitional regime in the TFEU clarifying the status of these agreements, the regulation authorizes all investment agreements currently in force between Member States and third countries to continue to exist.²³²

The Member States may be required to amend or modify the agreements in order to bring them in compliance with Treaty obligations and for this reason the regulation establishes the conditions to empower Member States to enter into negotiations with a third country.²³³ The same framework is available to allow Member States to negotiate and conclude new bilateral agreements with third countries.²³⁴

The main aim of the proposal is to avoid that the rights and the benefits available to investors and investments under international investment agreements will be eroded.²³⁵

In order to establish legal certainty, Member States have to notify to the Commission of all agreements that they wish to maintain under the terms and conditions of the Regulation.²³⁶

On June 21st, 2012 the Commission issued the Proposal on Financial Responsibility Regulation.²³⁷ The Proposal dealt with situations where the EU is

²³² *Id.*

²³³ *Id.*

²³⁴ Article 7 of Regulation (EU) No. 1219/2012 of the European Parliament and of the Council of 12 Dec. 2012, OJ 2012, L 315/40, <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2012:351:0040:0046:En:PDF>

²³⁵ BROWN, I. NAGLIS *op.cit.*, 20 ff. (stating the aim of the Regulation).

²³⁶ Article 2 of Regulation (EU) No. 1219/2012 of the European Parliament and of the Council of 12 Dec. 2012, OJ 2012, L 315/40, <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2012:351:0040:0046:En:PDF>.

²³⁷ COM (2012)335. Commission Proposal of 21 July for a Regulation of the European Parliament and of the Council establishing a framework managing financial responsibility linked to investor-state dispute settlement tribunals established by international agreements to which the European Union is party.

sued by a foreign investor in accordance with an agreement concluded by the EU and containing an investor-state arbitration clause.²³⁸

The Proposal concerned three main issues: who will be deemed financially responsible, who will be respondent and the system of payment.²³⁹

The document outlined a mechanism that did not strictly reflect the application of the rules on competence.²⁴⁰ This means that it is not the Union that will defend the case concerning the treatment of a Member State but the Member State itself.²⁴¹ The Commission adopted this approach in order to avoid a situation where the Union budget could unfairly suffer because of the action of particular Member States.²⁴² Why would Ireland be predisposed to contribute to the payment for violations of other Member States if it does not have a single BIT?²⁴³

The Proposal has been accepted and amended by the European Parliament and the European Council that issued in 2014 the Regulation No 912/2014.²⁴⁴

The Regulation will be applied to investor-state disputes arisen under agreements to which the European Union is itself a party and which include an

²³⁸ *Id.*

²³⁹ *See generally* COM (2012)335. Commission Proposal of 21 July for a Regulation of the European Parliament and of the Council establishing a framework managing financial responsibility linked to investor-state dispute settlement tribunals established by international agreements to which the European Union is party.

²⁴⁰ *Id.*

²⁴¹ *Id.*

²⁴² BROWN, I. NAGLIS *op.cit.*, 20 ff. (stating the rationale for the Commission adopting the Regulation).

²⁴³ *Id.* (pointing out that some Member States could be unfairly burdened if the EU were to have financial responsibility).

²⁴⁴ REGULATION (EU) No 912/2014 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 23 July 2014, establishing a framework for managing financial responsibility linked to investor-to-state dispute settlement tribunals established by international agreements to which the European Union is party [hereinafter Regulation on Financial Responsibility].

Investor State Dispute Settlement mechanism.²⁴⁵ Such agreements include the Energy Charter Treaty and the several bilateral investment treaties between the EU and third states that are in the process of being negotiated.²⁴⁶

One of the main principles of the regulation is that the financial responsibility lies with the actor.²⁴⁷ This principle is explained in article 3, which provides that the Union shall pay if the treatment was afforded by the institutions, bodies, offices or agencies of the Union.²⁴⁸ The Union will bear the financial responsibility in cases where a Member State has afforded the treatment and such treatment was required by Union law, unless the Member State concerned is required to act pursuant to Union law in order to remedy the inconsistency with Union law of a prior act.²⁴⁹

On the contrary, the Member State will bear the financial responsibility arising from treatment afforded by that Member State or if the state decides to settle the claim.²⁵⁰

The determination on who bears the financial responsibility would lie on the Commission that shall adopt a decision determining it. The European Parliament and the Council shall be informed of such a decision.²⁵¹

Considering the defense of the case, it is also linked to who has afforded the treatment. According to article 4 of the Regulation, the Union will defend only if

²⁴⁵ M. WEINGER, J. GREENAWAY, *New regulation sets out financial responsibility for investor-state disputes between the European Union and third countries*, available at <http://hsfnotes.com/arbitration/2014/09/17/new-regulation-sets-out-financial-responsibility-for-investor-state-disputes-between-the-european-union-and-third-countries/> (stating the area of the Regulation).

²⁴⁶ *Id.* (specifying which BITs and Treaty will be affected by the Regulation).

²⁴⁷ Article 3 of the Regulation on Financial Responsibility.

²⁴⁸ *Id.*

²⁴⁹ *Id.*

²⁵⁰ Article 14 of the Regulation on Financial Responsibility.

²⁵¹ *Id.*

the dispute concerns solely the treatment afforded by the institutions, bodies, offices or agencies of the Union.²⁵²

When the dispute concerns treatment afforded by the Member State partially or fully, the Commission and the Member State concerned shall defend and protect the interests of the Union and of the Member State concerned.²⁵³ Firstly, the Commission and the Member State in question shall enter into consultations on how to manage the disputes pursuant to this Regulation and its deadlines, and they shall share any relevant information.²⁵⁴ Secondly, consultations among the investor and the particular Member State and the Union will take place.²⁵⁵ If the Commission or the Member State receive a request for consultations from a claimant, it shall immediately notify the Member State concerned or the Commission.²⁵⁶ The consultation will take place between the investor and the respondent, represented by representatives of the Member State and a delegation from the Union.²⁵⁷

If the consultations do not conclude a satisfactory result, the investor may request arbitration proceedings. If the Commission or the Member State concerned receives notice that the investor wants to initiate arbitration proceedings, it shall immediately notify the Member State concerned or the Commission.²⁵⁸

The general rule on the arbitration proceeding laid down by the regulation is that the Member State concerned must act as respondent unless: (a) if the

²⁵² Article 4 of the Regulation on Financial Responsibility.

²⁵³ Article 6 of the Regulation on Financial Responsibility.

²⁵⁴ Article 7 of the Regulation on Financial Responsibility.

²⁵⁵ *Id.*

²⁵⁶ *Id.*

²⁵⁷ *Id.*

²⁵⁸ Article 8 of the Regulation on Financial Responsibility.

European Commission decides to act as respondent; (b) if the Member State concerned notifies the Commission that it does not intend to act as respondent.²⁵⁹

The Commission may decide to act as respondent where the Union would bear at least part of the potential financial responsibility or is partially responsible for the treatment afforded and where similar treatment is being challenged in a related claim against the Union in the WTO and the Union wants to ensure a consistent argumentation in the WTO case.²⁶⁰

In any case, the European Commission and the Member States shall act in accordance with the principle of sincere co-operation in order to defend and protect the interests of both the Union and the Member State.²⁶¹

If the Union acts as the respondent, the Commission shall consult the Member State concerned on any pleading or observation prior to the finalization and submission thereof.²⁶²

This provision is important because it guarantees that the principle of the unity of external representation of the Union will be respected. In this way the Member State will not advocate interpretations of the agreement that might be beneficial to their position but inconsistent with the intentions of the negotiators and that could be detrimental to other Member States.²⁶³

While it is normal that in any litigation there is the chance of a settlement, in the case in which the Union is being part of the investor state mechanism the process requires specific provisions.²⁶⁴

²⁵⁹ Article 9 of the Regulation on Financial Responsibility.

²⁶⁰ *Id.*

²⁶¹ Article 6 of the Regulation on Financial Responsibility.

²⁶² Article 9 of the Regulation on Financial Responsibility.

²⁶³ BROWN, I. NAGLIS *op.cit.*, 32.

²⁶⁴ BROWN, I. NAGLIS *op.cit.*, 32.

If the treatment is afforded by the Union, the Commission may adopt an implementing act to approve the settlement.²⁶⁵ On the contrary, if the Union is the respondent in a dispute concerning treatment afforded, whether fully or in part, by a Member State, and the Commission considers that the settlement of the dispute would be in the financial interests of the Union, the Commission shall first consult with the Member State concerned.²⁶⁶

The regulation includes rules for the for the payment of the final award or settlement.²⁶⁷ However, in any case, the EU and the Member State concerned should reach an agreement with regard to financial responsibility, unless the Member State defends the case.²⁶⁸ In fact, in that case, it bears the entire financial responsibility of the award.

This agreement between the EU and the Member State is relevant because, it is “*appropriate to put forward pragmatic solutions which ensure legal certainty for the investor and provide all the necessary mechanisms to allow for the smooth conduct of arbitration and, eventually, the appropriate allocation of financial responsibility*”.²⁶⁹ If the EU is held liable, the claimant may present a request to the Commission for payment of the award.²⁷⁰ There are no cases of the Union or its Member States refusing to respect an award.²⁷¹

It seems that the regulation on financial responsibility will not be applied to BITs concluded by Member States, if they are not agreements to which the EU is

²⁶⁵ Article 13 of the Regulation on Financial Responsibility.

²⁶⁶ Article 14 of the Regulation on Financial Responsibility.

²⁶⁷ *Id.*

²⁶⁸ *Id.*

²⁶⁹ European Commission stated in the Explanatory Memorandum (COM(2012)335).

²⁷⁰ Article 19 of the Regulation on Financial Responsibility.

²⁷¹ R. CAFANI PANICO, *op.cit.* (clarifying the area of the Regulation).

a party.²⁷² However, considering the article 64 of the ILC's articles on the international responsibility of international organizations, it is possible the EU may be considered internationally responsible for the conduct of a Member State that causes an injury to a foreign investor of a non- Member State.²⁷³ In particular, if a Member State violates a right granted to the foreign investor by the BIT because it has to comply with EU law, it is possible that the international responsibility may be attributable to the EU.²⁷⁴ This approach can be confirmed by the position adopted by the European Commission, according to whom "*the Union bears, in principle, international responsibility for the breach of any provision within the Union's competence*" (COM(2012)335).²⁷⁵

Moreover, the European Parliament expressed a similar opinion, affirming that "*International responsibility for treatment subject to dispute settlement follows the division of competences between the Union and the Member States. As a consequence, the Union will in principle be responsible for defending any claims alleging a violation of rules included in an agreement which fall within the Union's exclusive competence, irrespective of whether the treatment at issue is afforded by the Union itself or by a Member State*".²⁷⁶

Should this interpretation of the international responsibility of the EU be right, both the EU and Member States could be brought before an ISDS tribunal to respond to an investor's claim.²⁷⁷

The Explanatory Memorandum of the Proposal on Financial Responsibility for ISDS affirms that:

²⁷² *Id.* (introducing a different approach).

²⁷³ *Id.* (discussing how the EU could be held responsible).

²⁷⁴ *Id.*

²⁷⁵ *Id.*

²⁷⁶ Recital (3) Proposal Regulation on Financial Responsibility.

²⁷⁷ R. CAFANI PANICO, *op.cit.*

*“The Commission takes the view that the Union has exclusive competence to conclude agreements covering all matters relating to foreign investment, that is both foreign direct investment and portfolio investment.”*²⁷⁸

Even if the Commission clearly took positions on the dimension of the new article 207 TFEU, the amendment has been subject to a big academic debate.²⁷⁹ Scholars continue to debate the possible interpretations of the Lisbon Treaty, but it is the decisions taken by the EU institutions that will determine the new investment policy framework of the EU.

Some scholars argued that the EU’s investment powers would not extend to traditional investment protection but would be limited to aspects concerning the admission of investments.²⁸⁰ Others affirmed that the EU’s powers to FDI excluded portfolio investments.²⁸¹ In both situations, this would lead to a *de facto* shared control between the EU and its Member States, and consequently they would require the conclusion of the mixed agreements, negotiated and concluded by both the EU and its Member States.²⁸²

Considering the issue on the extent of the protection of the investment, the problem is whether or not the EU’s exclusive competence in FDI cover protection of investment once an investment has been made.

²⁷⁸ Proposal for a REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL establishing a framework for managing financial responsibility linked to investor-state dispute settlement tribunals established by international agreements to which the European Union is party available at <http://www.italaw.com/sites/default/files/archive/ita1036.pdf>.

²⁷⁹ BROWN, I. NAGLIS *op.cit.*, 21.

²⁸⁰ A. REINISCH, *The EU on the Investment Path – Quo Vadis Europe? The Future of EU BITs and other Investment Agreements*, 2013. available at <http://law.scu.edu/wp-content/uploads/investment/Reinisch-EU-Investment-Law-Quo-Vadis-26-01-2013.pdf> (referring to the main concern about the article 207 TFEU).

²⁸¹ *Id.* (stating a different position on the article 207 TFEU).

²⁸² *Id.* (referring to the consequences of the different interpretation of article 207 TFEU).

This question has become urgent because the EU-Singapore Free Trade Agreement (EUSFTA), unlike many previous FTA, like the FTA between South Korea and the EU and its Member States, for example deals with protection of investment.²⁸³

The investment chapter of the FTA between EU and Singapore particularly focuses on the investment protection rules, such as fair and equitable treatment or indirect expropriation, and it refers to the dispute settlement system as well, and in particular to the breaches of the investment protection provisions, transparency, binding code of conduct, safeguards for the parties.²⁸⁴

The Commission believes that the reference to FDI in Article 207 of the TFEU covers not only the liberalization of investment but also protection of investment.²⁸⁵

In 2010, in the communication ‘*Towards a comprehensive European international investment policy*’, the Commission stated that: “*a common international investment policy not only enables the execution of a direct investment itself – the acquisition of a foreign enterprise or the establishment of one - but also that it enables and protects all the operations that accompany that investment and make it possible in practice: payments, the protection of intangible assets such as Intellectual Property Rights, etc*”.²⁸⁶

On the contrary, certain academics, such as Krajewski, are convinced that the EU competence in FDI does not cover all aspects of protection of investment

²⁸³ Article 7.10 of the EU- South Korea FTA, <http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=OJ:L:2011:127:FULL&from=EN>.

²⁸⁴ Summary of the investment provisions in the EU-Singapore Free Trade Agreement, *see* http://trade.ec.europa.eu/doclib/docs/2014/october/tradoc_152845.pdf.

²⁸⁵ EUROPEAN COMMISSION, *Towards a comprehensive European international investment policy*, 2010, available at http://trade.ec.europa.eu/doclib/docs/2010/july/tradoc_146307.pdf.

²⁸⁶ *Id.*

(e.g., expropriation), which remain in the ambit of the Member States.²⁸⁷ The new article 217 should be understood to refer only to those areas of FDI which have a direct link to international trade agreements in order to avoid responsibility on the part of the Union for the renegotiation of old investment agreements concluded by Member States.²⁸⁸

In addition, the German Constitutional Court stated that the extension of the Common Commercial Policy to FDI does not give exclusive competence on the EU to the investment protection agreements that should be concluded as mixed agreements.²⁸⁹

Considering the question about whether or not the EU exclusive competence in FDI includes foreign portfolio investment, the Commission, in its Communication “*Towards a comprehensive European international investment policy*”, argued that the new article 207 TFEU implies an EU exclusive competence for foreign portfolio investments because they may affect common rules on the free movement of capital between Member States and third countries.²⁹⁰

On the contrary, Member States, supported by certain academics, stress that FDI does not include portfolio investments. According some authors, such as Reinisch, portfolio investments cannot be covered by Article 207 of the TFEU

²⁸⁷ M. KRAJEWSKI, *External Trade Law and the Constitution Treaty: Towards a Federal and More Democratic Common Commercial Policy?* in *Mkt L. Rev.* 2005: “This also suggests that foreign direct investment is only part of the common commercial policy as far as restrictions to foreign direct investment are concerned, but not investment protection against expropriation, which is traditionally an element of investment agreements” (referring to the position of other authors).

²⁸⁸ *Id.* (stating the Krajewski interpretation of article 207).

²⁸⁹ German Constitutional Court, 2 BvE 2/08 (30 Jun. 2009), ¶ 379.

²⁹⁰ EUROPEAN COMMISSION, *Towards a comprehensive European international investment policy*, 2010, available at http://trade.ec.europa.eu/doclib/docs/2010/july/tradoc_146307.pdf.

because FDI refers to long-term investment in a foreign country and the drafters of the Treaty of Lisbon wanted to limit the EU competence in FDI.²⁹¹

As previously affirmed, the problem became more important when, in October 2014, the negotiations on the EU-Singapore Free Trade Agreement (EUSFTA) were completed and they included different protection rules.²⁹²

Doubts arose concerning who in the EU was competent to approve these provisions.²⁹³ Because the potential approval by the EU institutions or the ratification by the twenty-eight Member States would have brought to very different situations in terms of years, the Commission decided to ask the EU Court of Justice (ECJ) to clarify the EU competence to sign and ratify the treaty.²⁹⁴

On October 30, 2014, the Commission issued a decision requesting the opinion of the EU Court of Justice pursuant to article 218(11) TFEU on the competence of the Union to sign and conclude a Free Trade Agreement with Singapore with regard to the extent and the nature of the Union's competence in respect of some elements of the chapters of the agreement on the protection of foreign investment, transport services, intellectual property, transparency and sustainable development.²⁹⁵

²⁹¹ A. REINISCH, *op.cit.*

²⁹² D. LEYS, *EU Competence in Foreign Direct Investment: Will the EU Court of Justice End the Controversy?* In *Global Trade And Customs Journal*, 2015, available at <http://media.mcguirewoods.com/publications/2015/EU-Competence-in-Foreign-Direct-Investment.pdf>.

²⁹³ *Id.* (discussing the issues on the EU-Singapore Free Trade Agreement).

²⁹⁴ *Id.* (introducing some consequences of the possible approval of the EU-Singapore Free Trade Agreement).

²⁹⁵ COMMISSION DECISION of 30.10.2014 requesting an opinion of the Court of Justice pursuant to article 218(11) TFEU on the competence of the Union to sign and conclude a Free Trade Agreement with Singapore available at <http://www.statewatch.org/news/2015/feb/eu-com-fta-cjeu-com-8218-14.pdf>; The article 218(11) affirms: “A Member State, the European Parliament, the Council or the Commission may obtain the opinion of the Court of Justice as to whether an agreement envisaged is compatible with the Treaties. Where the opinion of the Court

The questions that the Commission has asked to the Court are the following: Does the Union alone have the requisite competence to sign and conclude the Free Trade Agreement with Singapore? More specifically, which provisions of the agreement fall within the Union's exclusive competence? which provisions of the agreement fall within the Union's shared competence? Finally, is there any provision of the agreement that falls within the exclusive competence of the Member States?²⁹⁶

The formal procedure is that, after the submission, the President of the ECJ shall prescribe a time-limit within which a Member State, the European Parliament, or the Council may submit written observations.²⁹⁷ Later the President shall designate a Judge Rapporteur and the First Advocate General shall assign the case to an Advocate General.²⁹⁸ The ECJ could include also a hearing in the procedure.²⁹⁹ In the end, the Opinion, signed by the President, the Judges, and the Registrar, shall be delivered in open court and shall be served on all the Member States and on the European Parliament, the Commission, and the Council. If the Opinion of the ECJ is adverse, the agreement may not enter into force unless it is amended or the Treaties are revised.³⁰⁰

It is important to underline that, even if the ECJ will have the last word on the legal issue over the EU competence in FDI, Member States still have the last word on adoption of investment chapters in FTAs like the EUSFTA. In fact,

is adverse, the agreement envisaged may not enter into force unless it is amended or the Treaties are revised.”.

²⁹⁶ *Id.*

²⁹⁷ Article 196, §3 of the Rules of Procedure of the ECJ.

²⁹⁸ Article 197 of the Rules of Procedure of the ECJ.

²⁹⁹ Article 198 of the Rules of Procedure of the ECJ.

³⁰⁰ D. LEYS, *op.cit.*

according to Article 207(4) of the TFEU, the Member States, as part of the Council, can still veto the adoption of EU investment chapters in FTAs.³⁰¹

In conclusion, despite many years from the entry in force of the Lisbon Treaty, the article 207 TFEU is still very debated and it is probable that the discussion will continue for a long time. However, the opinion of the ECJ will represent a big step to understand the investment policy of the European Union.

2.2. EUROPEAN UNION AND THE DECISION MAKING PROCESS IN THE NEGOTIATION OF FREE TRADE AGREEMENTS

This Part describes the European Union's decision-making process in the negotiation of international trade agreements. After the Treaty of Lisbon, not only the international trade policy but also the international investment policy is governed by a supranational method, whereby the Member States have given the competence from the national to the EU level.³⁰²

After the EU has acquired an exclusive competence in the field of direct investment, it started an ambitious strategy to conclude Free Trade Agreements (FTAs) which included an investment chapter.³⁰³ The EU is currently negotiating

³⁰¹ Article 207(4) TFEU.

³⁰² Y. DEVUYST, *The European Union's Institutional Balance After the Treaty of Lisbon: "Community Method" and "Democratic Deficit" Reassessed*, in *Georgetown Journal of International Law*, 2008, p. 250 ff.

³⁰³ EUROPEAN COUNCIL, Conclusions P 4, Brussels (Sept. 16, 2010 EUCO 21/1/10), available at http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/116547.pdf; European Commission, *Trade, Growth and World Affairs: Trade Policy As a Core Component of the EU's 2020 Strategy*, at 9-10 COM (2010) 612 final (Nov. 9. 2010), available at http://trade.ec.europa.eu/doclib/docs/2010/november/tradoc_146955.pdf.

FTAs with different states, including the United States Canada, Malaysia, Vietnam, Thailand, Mercosur, Georgia, Armenia and Moldova.³⁰⁴

For this reason, it important to analyze the EU's inter-institutional and legal practice in the negotiation and conclusion of international trade agreements.

The European Commission is charged with requesting authorization to start international trade negotiations through a note that states the recommendations to the Council of Ministers that are necessary to open the negotiations.³⁰⁵ The Council is responsible for authorizing the opening of the negotiations, to establish negotiating directives and to nominate the negotiator.³⁰⁶ In the directives, the Council establishes the general objectives to be achieved and the Commission's guidelines during the negotiations.³⁰⁷ The negotiating directives are not legally binding.³⁰⁸ Generally, it is the Commission that presents draft directives to the Council when it submits recommendations to start negotiations and then the Council can approve them or modify their content.³⁰⁹

The non-involvement of the Parliament in the approval of the negotiating directives is considered one of the Treaty's limits, as it appears from the opinion of Parliament's Committee on International Trade on the Lisbon Treaty:

“[INTA e]xpressly depreciates the fact that the Treaty of Lisbon does not provide Parliament with the right to approve the mandate of the Commission to negotiate

³⁰⁴ *The Economy*, EUROPA.EU, http://europa.eu/about-eu/facts-figures/economy/index_en.htm
Living in the EU, EUROPA.EU, http://europa.eu/about-eu/facts-figures/living/index_en.htm);
WORLD TRADE ORG. [hereinafter WTO], WORLD TRADE REPORT 2012 23 (2012).

³⁰⁵ TFEU, art. 207(3).

³⁰⁶ TFEU art. 218(2).

³⁰⁷ See EUROPEAN COMMISSION, Factsheet: Trade Negotiations Step by Step 3, 2012. available at http://trade.ec.europa.eu/doclib/docs/2012/june/tradoc_149616.pdf.

³⁰⁸ P. EECKHOUT, *EU External Relations Law*, Oxford, 2011, p.197.

³⁰⁹ *Id.*

*a trade agreement and stresses the imbalance - regarding the role and powers of Parliament - between the internal and the external competence in the areas of the CCP.*³¹⁰

The Treaty states that the Council has the right to nominate the Union negotiator and that, for negotiations in the field of the CCP, the Commission conducts international negotiations.³¹¹

The Treaty also refers to a "negotiating team," that should be composed of both the Commission and the High Representative of the Union for Foreign Affairs and Security Policy.³¹² This team must be envisaged where a negotiation covers both significant aspects of CFSP and other EU policies (and where neither is purely ancillary to the other).³¹³

In the area of the CCP, the Commission conducts the negotiations on behalf of the EU.³¹⁴ It designates a Chief Negotiator, usually an official in its Directorate General for Trade.³¹⁵

Even if the Commission conducts the negotiations, the Council still has a role. Firstly, the Commission must conduct the negotiations in consultation with the Council's Trade Policy Committee. Secondly, the Commission has to respect

³¹⁰ R. CORBETT, I. MÉNDEZ, *Opinion of the Committee on International Trade on the Treaty of Lisbon*, in *European Parliament, Committee on Constitutional Affairs*, 2008, p. 84.

³¹¹ TFEU art. 207(3).

³¹² Council Decision authorizing the European Commission and the High Representative of the Union for Foreign Affairs and Security Policy to negotiate, on behalf of the European Union, the provisions of a Framework Agreement between the European Union and its Member States, of the one part, and Canada, of the other part, that fall within the competence of the European Union, Brussels (Nov. 30, 2010) 16964/10.

³¹³ TFEU art. 207(3).

³¹⁴ TFEU art. 207(3)

³¹⁵ Trade Negotiations Step by Step, at 4.

the directives that the Council may issue to it at the time of the launching of the negotiations or later.³¹⁶

It is important to underline that the Council is composed of 28 Member State with heterogeneous interests. Many Member States have big investment agendas and want to keep a high level of protection of the investor and the investment. On the contrary, other States prefer to have a “policy space” considering all the disputes that they have faced. Finally, a group of Member States is completely neutral to the investment policy.³¹⁷

However, many Member States share a common interest in the best practice of the BITs. For this reason, the Commission can simply base its policy on the best practice of the Member States’ BITs. This point has been expressly stated by both the Council and the Commission.³¹⁸

As regards the relationship between the Commission and the European Parliament during the negotiations, the Commission has to report, not only to the Trade Policy Committee, but also to the European Parliament, on the international trade negotiations developments.³¹⁹ In the Framework Agreement between Parliament and Commission of 2010, the Commission's duty of information is specified in the following terms: *“In the case of international agreements the conclusion of which requires Parliament’s consent, the Commission shall provide to Parliament during the negotiation process all relevant information that it also provides to the Council (or to the special committee appointed by the Council).”*

³¹⁶ Y. DEVUYST, *op.cit.*

³¹⁷ N. LAVRANOS, *The Remaining Decisive role of the Member States in Negotiating and Concluding EU investment agreements*, Zurich, 2010.

³¹⁸ Council Conclusion of 25 October 2010, available at http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/EN/foraff/117328.pdf; EUROPEAN COMMISSION, *Towards a comprehensive European international investment policy*, 2010, available at http://trade.ec.europa.eu/doclib/docs/2010/july/tradoc_146307.pdf.

³¹⁹ TFEU art. 207(3).

This shall include draft amendments to adopted negotiating directives, draft negotiating texts, agreed articles, the agreed date for initialing the agreement and the text of the agreement to be initialed. The Commission shall also transmit to Parliament, as it does to the Council (or to the special committee appointed by the Council), any relevant documents received from third parties, subject to the originator's consent. The Commission shall keep the responsible parliamentary committee informed about developments in the negotiations and, in particular, explain how Parliament's views have been taken into account."³²⁰

Concerning the relationship between the Council and the European Parliament during the negotiations, the Parliament has insisted in order to receive from the Council access to the adopted negotiating directives.³²¹ Informing the European Parliament during an international negotiation makes sense only if the Parliament uses this information to weigh on the substance of the process.³²²

In fact, the Parliament's Rules of Procedure specify that during the negotiations, the Parliament may adopt recommendations and require them to be taken into account before the conclusion of the international agreement.³²³ Generally, Parliament's resolutions are supportive of human rights and social and environmental standards.³²⁴

³²⁰ Framework Agreement, European Parliament - European Comm'n, 2010, O.J. (L 304) available at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2010:304:0047:0062:EN:PDF>.

³²¹ R. PASSOS, *The European Union's External Relations a Year after Lisbon: A First Evaluation from the European Parliament*, in *The European Union's External Relations A Year After Lisbon*, Panos Koutrakos, 2011, p. 52 ff.

³²² Committee on Civil Liberties, Justice and Home Affairs, European Parliament, Recommendation (05305/1/2010REV - C7-0004/2010 - 2009/0190(NLE)) (Feb. 5, 2010) (by Jeanine Hennis-Plasschaert) 10.

³²³ See TEU art. 10(4); European Parliament, Rules of Procedure, 7th parliamentary term, Mar. 2011, 2011 O.J. (L 116) r. 90(4).

³²⁴ See Resolution of 27 September 2011 *supra* note 288, PP.5-9; European Parliament, Resolution, Nov. 25, 2010 (2009/2219(INI)).

This happened, for example, in the case of the Free Trade Agreement with Korea, where not only did the Parliament obtain the inclusion of a clause on labor and environmental standards but it also succeeded in asking a formal Commission commitment to monitor and report on their implementation.³²⁵ Similarly, the Parliament had the same preoccupation in the context of the Free Trade Agreement with Colombia and Peru and it prompted it to propose a concrete follow-up mechanism.³²⁶

After the end of the substantive negotiations, lawyers have to review every detail of the draft.³²⁷ This process can take from three to nine months. Then, the Chief Negotiators can initial the text. This means that text of the agreement will be authentic and definitive.³²⁸ Obviously, the decisions of the Council to authorize the signing and the conclusion of international agreements must mention the legal basis that allows the EU to act.³²⁹

The Parliament's Rules of Procedure establish that the responsible Committee shall ascertain and verify the chosen legal basis for an international agreement at the time when the negotiations are scheduled to start.³³⁰ The actual determination of the legal basis of an international agreement must rely on

³²⁵ European Parliament, Resolution, Dec. 13, 2007, 2007 O.J. (C323 E/521), P 12; Committee on International Trade, European Parliament, Report, Feb. 9, 2011, (08505/2010 - C7-0320/2010 - 2010/0075(NLE) (by Robert Sturdy) 10; European Parliament, Resolution, Feb. 17, 2011, 2012 O.J. (C 188E) 94, Annex I: Commission Statement.

³²⁶ European Parliament, Resolution, June 13, 2012, 2012/2628(RSP), p. 22.

³²⁷ Trade Negotiations Step by Step, p. 5.

³²⁸ Y. DEVUYST, *op.cit.*

³²⁹ M. MARESCAU, *Bilateral Agreements concluded by the European Community*, Oxford, 2004 p. 154.

³³⁰ EUROPEAN PARLIAMENT, Rules of Procedure, r. 90(3), 37.

objective factors amenable to judicial review, which include the aim and content of that measure.³³¹

It is the Council, on proposal of the Commission, that decides to sign the agreement resulting from the negotiations. Even if not expressly affirmed in the Treaties, it seems that trade agreements should be signed by a Commission representative on behalf of the EU. With the signature the agreement's provisions are not legally binding. The signature simply indicates a political intention to move towards the agreement's ratification.³³² However, according to the Vienna Convention, the signing party had a duty to refrain from acts that would defeat the object and purpose of the agreement.³³³

If the Council decides in favor of the signature, it may also adopt a decision on the agreement's provisional application before the agreement enters into force.³³⁴ Parliament's Rules of Procedure specify that whether the Commission let the Council know of its intention to propose a provisional application the agreement, it should simultaneously notify Parliament.³³⁵ After a debate, the Parliament may issue recommendations on the subject.³³⁶ The decision on provisional application usually occurs when there is the signature and thus before its formal ratification and Parliament's official consent. Consequently, the issue is particularly sensitive to Parliament.³³⁷

³³¹ *European Parliament V. Council of the European Union*, 2008 (Court of Justice of the European Communities); Opinion 2/00, 2001 E.C.R. I-9713, ¶ 5.

³³² See Vienna Convention art. 12.

³³³ See Vienna Convention art. 12.

³³⁴ See TFEU art. 218(5).

³³⁵ EUROPEAN PARLIAMENT, Rules of Procedure, r. 91.

³³⁶ *Id.*

³³⁷ See TFEU art. 218(5), (6).

After the signature, the Council has to adopt another decision regarding the ratification of the agreement, called the "conclusion" by the EU Treaties.³³⁸ Through this ratification, the EU officially expresses its consent to be bound by the agreement.³³⁹

Before the conclusion of the agreement, the European Parliament must, as for international trade agreements, provide its consent.³⁴⁰ While the Treaty prescribes that the Council has to request Parliament's consent after the signing, but before the conclusion of the agreement, the Parliament's Rules of Procedure provide that a draft be submitted, when the negotiations are concluded, but before any agreement is signed.³⁴¹ Before expressing its consent, Parliament may seek an Opinion from the European Court of Justice on the compatibility of an international agreement with the Treaties.³⁴² Council Decisions authorizing the signing and the ratification of an agreement and the agreement in question are finally published in the EU's Official Journal.³⁴³

An important point is that if the EU's exclusive competence is beyond any doubt the aforementioned process will be followed, but the situation is different for broader trade agreements, such as the Free Trade Agreement with South Korea. This does not only cover questions within the CCP sphere, but also other EU policy fields and even areas covered by Member State competences.³⁴⁴ For this reason,

³³⁸ See TFEU art. 218(6).

³³⁹ Vienna Convention art. 14; TFEU art. 216(2).

³⁴⁰ See TFEU art. 218(6).

³⁴¹ EUROPEAN PARLIAMENT, Rules of Procedure, r. 5; TFEU art. 218(6).

³⁴² TFEU art. 218(11); EUROPEAN PARLIAMENT, Rules of Procedure, r. 6.

³⁴³ See generally Official Journal of the European Union (listing of the publications in the O.J. of Council Decisions authorizing the conclusion of international agreements) available at <http://eur-lex.europa.eu/oj/2014/04/direct-access.html?ojYear=2014>.

³⁴⁴ Council Decision 2011/265, 2011 O.J. (L 127) 1,8 (EU).

these mixed agreements also need to be signed by each of the Member States separately.³⁴⁵

Reading the article 207 TFEU, it seems that the role of the Member States regarding the negotiation and the conclusion of EU investment agreements or FTA with an investment chapter is totally eliminated. However, the Member states still have a decisive role in the various stages of the negotiations and conclusion of the agreements in the case in which the agreement will be concluded as mixed agreement.³⁴⁶ Firstly, the default mode for future EU Investment agreements is that they will be concluded as mixed agreements, whether or not Article 207 TFEU establishes an exclusive competence for foreign direct investment.³⁴⁷ As in the FTAs containing investments chapters, in the Investment agreements there are some areas that are in the competence of the Member States or are areas of shared competence, such as national procedural law, expropriation and compensation.³⁴⁸ For this reason, the role of the Member States is essential and will probably remain essential for the conclusion and ratification of future agreements.³⁴⁹ This is extremely important because if also one Member State fails to ratify the agreement, it will not enter into force.³⁵⁰ However, it could be possible to apply at least those parts that fall in the exclusive competence of the EU for a temporary period.³⁵¹

³⁴⁵ Y. DEVUYST, *op.cit.*

³⁴⁶ Y. DEVUYST, *op.cit.*; N. LAVRANOS, *op.cit.* 165 (introducing the role of the Member States in the negotiation of the International Investment Agreements).

³⁴⁷ Y. DEVUYST, *op.cit.* (referring to the default method of conclusion of agreements).

³⁴⁸ *Id.* (explaining the reason for choosing mixed agreements).

³⁴⁹ *Id.* (reaffirming the central role of Member States).

³⁵⁰ *Id.* (clarifying the consequences for which a Member State does not ratify the agreement).

³⁵¹ *Id.* (imagining a possible solution in the case in which a Member State fails to ratify the agreement).

The role of the Member States in the mixed agreements relates to the negotiation and in particular to the conclusion.³⁵² As previously mentioned, the Commission needs a negotiation mandate from the Council.³⁵³ This mandate can be also very detailed on the conditions that the Commission has to respect during the negotiation: MFN, National Treatment, umbrella clause etc.³⁵⁴ During this stage and throughout the entire negotiation the Member State can indicate if they are satisfied and if not, how the negotiation could be modified in a way that the Council will agree with it.³⁵⁵

The role of the Member States, of their parliaments and constitutional courts becomes more important when it comes to the conclusion and ratification phase.³⁵⁶ Assuming that the international agreement will be concluded as mixed agreement, it will have to be approved also by 28 national parliaments and this procedure will depend on the respective powers granted by the constitution of each Member state.³⁵⁷ In some Member States, national courts will have to review the constitutionality of the international agreement.³⁵⁸

In conclusion the role of the Member States is pivotal because, on one hand, the Council that gives the mandate for the negotiation and accepts the final texts and on the other hand, if the agreement will be ratified as mixed, domestic institutions will have a central role in the ratification process.

³⁵² *Id.* (discussing the role of the Member States during the negotiations of an International Investment agreement).

³⁵³ TFEU art. 218(2).

³⁵⁴ Y. DEVUYST, *op.cit.* (describing the mandate of the Council for negotiations).

³⁵⁵ *Id.* (analyzing the role of the Member States during negotiations).

³⁵⁶ *Id.* (introducing the role of national parliaments and courts).

³⁵⁷ *Id.* (analyzing the role of national parliaments).

³⁵⁸ *Id.* (referring to the role of national courts).

CHAPTER 3- OVERVIEW OF FREE TRADE AGREEMENTS AND OTHER TRADE NEGOTIATIONS OF THE EUROPEAN UNION

ABSTRACT: 3.1. THE COMPREHENSIVE ECONOMIC TRADE AGREEMENT (CETA) - 3.1.1. OVERVIEW ON THE CETA – 3.1.2. INVESTOR-STATE ARBITRATION IN THE CETA- 3.2. FTA WITH VIETNAM – 3.3. TRANSATLANTIC TRADE AND INVESTMENT PARTNERSHIP BETWEEN UNITED STATES AND EUROPEAN UNION (TTIP)- 3.3.1. OVERVIEW ON THE TTIP - 3.3.2. EUROPEAN UNION AND UNITED STATES APPROACHES DURING THE NEGOTIATIONS OF THE TTIP- 3.3.3. EUROPEAN UNION AND UNITED STATES APPROACHES DURING THE NEGOTIATIONS OF THE TTIP - 3.4. THE INVESTMENT COURT SYSTEM- 3.4.1 THE INVESTMENT COURT SYSTEM IN THE PROPOSAL OF THE COMMISSION- 3.4.2. THE INVESTMENT COURT SYSTEM IN THE PROPOSAL, CETA AND THE AGREEMENT WITH VIETNAM- 3.4.3. EU LIMITS: CONDITIONS FOR INVESTOR-STATE ADJUDICATION UNDER EU AGREEMENTS

While the EU has acquired a new power and it is finally “catching up” with the regime of bilateral investment Treaties (BITs), the Commission is also negotiating and concluding new mega-regional free trade agreements (FTAs).³⁵⁹ Considering the ongoing fundamental FTAs of the European Union, it is important to previously refer to the FTA with the Republic of Korea and the FTA with the Andean Community.

On 6 October 2010 the European Union and the Republic of Korea signed an FTA, the successor of the previous Framework Agreement on Trade and Cooperation. The two countries have been significant trading partners in goods and services for a long time.³⁶⁰

³⁵⁹ See BILATERAL INVESTMENT TREATIES 1959-1999
<http://unctad.org/en/pages/PublicationArchive.aspx?publicationid=195>

³⁶⁰ South Korea, April 29,2016 available at <http://ec.europa.eu/trade/policy/countries-and-regions/countries/south-korea/>.

In June 2012 the European Union signed a comprehensive Trade Agreement with Colombia and Peru and it has been provisionally applied with Peru as of 1 March 2013, and with Colombia as of 1 August 2013.³⁶¹

In July 2014 negotiations were concluded for the accession of Ecuador to the Trade Agreement with Colombia and Peru. In order to apply the Agreement with Ecuador, the Parties will now engage in the relevant internal procedures for its approval.³⁶²

It is important to specify that the agreements do not cover provisions on investment protection, such as provisions specifically relating to expropriation, fair and equitable treatment, Investor-State dispute settlement procedures.³⁶³ However, they contain dispute solutions mechanism in order to settle any dispute between the Parties concerning the interpretation and application of these Agreements.³⁶⁴

In both the agreements the dispute solution clause refers to a third party mechanism. Prior to the exercise of the right to dispute the parties have a duty of consultation in order to reach a mutual agreed solution.³⁶⁵

The mechanism is strongly modelled after the WTO mechanism with some differences. A panel is usually constituted of three arbitrators that will decide the dispute within 120 days from the establishment of the controversy.³⁶⁶

³⁶¹ ANDEAN COMMUNITY, April 29, 2016 available at <http://ec.europa.eu/trade/policy/countries-and-regions/regions/andean-community/>.

³⁶² *Id.* (describing the process of the treaty).

³⁶³ *Id.* (clarifying that there is not an investment chapter).

³⁶⁴ The EU-South Korea Free Trade Agreement and Its Implications for the United States available at <https://www.fas.org/sgp/crs/row/R41534.pdf>.

³⁶⁵ EU-South Korea Free Trade Agreement, art. 14.3; Trade Agreement between the European Union and Colombia and Peru art. 301.

³⁶⁶ The WTO dispute solutions usually take 9 months to be decided; Article 14.7 of the EU-South Korea Free Trade Agreement; Article 307 of the Trade Agreement between the European Union and Colombia and Peru.

Moreover, under the FTA the complaining party is free to recur to retaliation or not, while under the WTO Dispute Settlement Understanding, the member must suspend concessions in the same sector as the sector in which the violation takes place. Finally, differently from the WTO mechanism there is no right to appeal and the award will be immediately binding for the parties.³⁶⁷

Nowadays the European Union is negotiating FTAs that contain an investment chapter and an investor-state arbitration mechanism, such as the Transatlantic Trade and Investment Partnership (TTIP), the EU-Vietnam bilateral trade agreements and the newly released Comprehensive Economic and Trade Agreement with Canada (CETA 2016).³⁶⁸ This Chapter will analyze what these agreements are and the investor-state mechanism that they establish.

Before analyzing the actual negotiations of the European Union, it is appropriate to consider a possible issue on the dispute solution mechanism, in the case in which the European Union will successfully conclude investment agreements.

The EU cannot be part of an arbitration before the ICSID, the principal investor-state arbitration mechanism, because, as stated in Chapter 1.2.4., the ICSID Convention can only be signed by States that are members of the World Bank or party to the Statute of the International Court of Justice. The EU is neither of these (COM(2010)343) and being a state is an evident requirement for adherence to the ICSID Convention.³⁶⁹

³⁶⁷ EU-South Korea Free Trade Agreement, art. 14.7; Trade Agreement between the European Union and Colombia and Peru art. 308.

³⁶⁸ D. GALLO, F. G. NICOLA, *op.cit.*

³⁶⁹ EUROPEAN COMMISSION, *Towards a comprehensive European international investment policy*, 2010, available at http://trade.ec.europa.eu/doclib/docs/2010/july/tradoc_146307.pdf. ; A. REINISCH, *op.cit.* 193.

When, on May 23, 2014 the European Commission tried to intervene as a third-party in the ICSID proceeding between Spain and Guatemala, on the basis of its new competence for extra-EU investment obligations, it was rejected because the application came too late.³⁷⁰

Even to be part of an ICSID procedure the State of the investor and the State to the dispute both have to be members of the World Bank or party to the ICJ Statute, there is another tool, the ICSID additional-facility rules.³⁷¹ However, also in this case the European Union cannot benefit from them because, like the Convention, the additional-facility rules only apply to States and not to international organizations such as the EU.³⁷²

Excluding ICSID, the EU can be part of an international investment arbitration before the Stockholm Chamber of Commerce (SCC), before an *ad hoc* tribunal conducted under the rules of UNCITRAL and also before *ad hoc* tribunals conducted in accordance with both the international agreements that establish them and international law.³⁷³

With regard to the three FTAs concluded by the EU and its Member States, including ISDS clauses, on one hand the FTAs with South Africa and South Korea contain a very limited *ad hoc* arbitration, with tribunals having jurisdiction over certain issues only, on the other hand the ECT countenances a wide range of institutionalized arbitration tribunals featuring extended jurisdiction, such as ICSID tribunals, ICSID additional-facility tribunals, *ad hoc* arbitrations conducted

³⁷⁰ Article 37 of Arbitration Rules of ICSID; Investment Arbitration Reporter (IAreporter.com), *European Commission's DG Trade tries to intervene for first time in an extra-EU BIT case to offer "systemic" views, but ill-timed application is rejected*, July 9, 2014.

³⁷¹ R. CAFANI PANICO, *op.cit.* (introducing additional rules on investor-state arbitration).

³⁷² *Id.* (explaining why the European Union cannot recur to the Additional Facilities rules).

³⁷³ *Id.* (stating under which rules European Union can be part of an arbitration proceeding).

under UNCITRAL rules and the arbitration tribunals of the SCC.³⁷⁴ Of course, recourse to ICSID means that the ICSID Convention should be modified so that it also applies to the EU.³⁷⁵

In conclusion, until now, the EU could only conduct *ad hoc* arbitrations proceedings and disputes before the SCC, while EU Member States have the opportunity to conduct any kind of investor-state arbitration proceeding, including ICSID proceedings.

As it will be explained in Chapter 3.4.2., concerning the CETA, the TTIP and the Agreement with Vietnam, it is noteworthy that the European Commission has declared that it intends to create an appellate body for investor-state disputes, a *quasi*-permanent tribunal which can review arbitral awards at first instance, that could solve the issue.³⁷⁶

3.1. THE COMPREHENSIVE ECONOMIC TRADE AGREEMENT (CETA)

EU-Canada Comprehensive Economic and Trade Agreement (CETA) negotiations were launched at a transatlantic summit in Prague in May 2009. There, the leaders of European Union and Canada affirmed that they wish to strengthen and deepen their strategic partnership that builds on their shared values. They remarked that their priority areas remain as follows: a comprehensive economic

³⁷⁴ *Id.* (referring to the rules to which the FTAs concluded by the EU and its Member States refer).

³⁷⁵ *Id.* (proposing to modify the ICSID Convention).

³⁷⁶ EUROPEAN COMMISSION, *Fact sheet. Investment Protection and Investor-to-State Dispute Settlement in EU agreements*, November 2013, pages 8-9; European Commission, *Investment Provisions in the EU-Canada free trade agreement (CETA)*, December 2013, page 3; European Commission, *Investment Protection and Investor-to-State Dispute Settlement (ISDS) in EU agreements*, March 2014, p. 2.

partnership agreement, climate change and the environment, energy security and sustainability, as well as international peace and security. They also reiterated their objective to enhance the free and secure movement of people between the EU and Canada, with a view to extending the visa-free travel to Canada for all EU citizens as soon as possible.³⁷⁷

CETA includes chapters on regulatory cooperation, food and consumer product standards, technical barriers to trade, public procurement, domestic regulation, trade in services, and other areas. At the request of the Canadian government, CETA includes an extensive investment protection chapter and investor-to-state dispute settlement (ISDS) process, though it is clear that the Commission is anxious to use the Canadian and Singapore negotiations to develop an EU-wide investment policy.³⁷⁸

This paragraph will give a general overview on the CETA and, then, it will focus on the investor-state mechanism that the agreement contains.

3.1.1. OVERVIEW ON THE CETA

President Barroso, President Van Rompuy and Prime Minister Harper announced the end of the CETA negotiations at the EU-Canada Summit on 26 September 2014.³⁷⁹

The European Commission and Canada conducted a legal review of the original version of this text, which was then translated into the other official

³⁷⁷ Press Release, European Commission, EU-CANADA SUMMIT DECLARATION (May 6, 2009) http://europa.eu/rapid/press-release_PRES-09-120_en.html.

³⁷⁸ *Id.* (introducing the investment chapter in the CETA).

³⁷⁹ CETA – Summary of the final negotiating results http://trade.ec.europa.eu/doclib/docs/2014/december/tradoc_152982.pdf (referring to when the negotiation has been terminated).

languages of the EU and Canada, and will now be submitted to the Council and the European Parliament for approval.³⁸⁰

The objective of CETA is to increase bilateral trade and investment flows and contribute to growth in times of economic uncertainty through different instruments.³⁸¹

Firstly, the EU and Canada have agreed to eliminate customs duties for imports of goods originating in the EU and Canada either when CETA comes into force or gradually within 3, 5 or 7 years for almost all goods.³⁸² Moreover, export duties and other export restrictions will be generally prohibited.³⁸³

Secondly, in order to avoid products of a third country indirectly benefitting from the Agreement, the EU and Canada found compromise on rules of origin.³⁸⁴

Thirdly, a chapter is dedicated to technical barriers to trade (TBT) and one to the rights and the obligations of the EU and Canada under the Sanitary and Phytosanitary rules. Both are chapters built on the key of the provisions of the WTO.³⁸⁵

Moreover, the chapter on Customs and Trade Facilitation will simplify and render more transparent the customs clearance of goods in order to facilitate bilateral trade and reduce transaction costs for importers and exporters.³⁸⁶

³⁸⁰ Comprehensive Economic and Trade Agreement (CETA), http://ec.europa.eu/trade/policy/in-focus/ceta/index_en.htm (clarifying which the next steps will be).

³⁸¹ *Id.* (stating the main objective of the CETA).

³⁸² *Id.* (referring to imports between EU and Canada).

³⁸³ *Id.* (considering exports between EU and Canada).

³⁸⁴ *Id.* Rules of origin allow European and Canadian products to be moved between the applicable countries free of duties. (addressing the rules of origin chapters).

³⁸⁵ *Id.* (analyzing two chapters inspired by WTO).

³⁸⁶ *Id.* (discussing how trades will be easier).

Furthermore, other areas are analyzed in the CETA, with chapters dedicated to services and investment, government procurement, intellectual Property Rights (IPR), Geographical Indications and trade and sustainable development.³⁸⁷

Considering the investment provisions in the CETA, it represents the first agreement that puts all EU investors on the same, equal footing. It introduces important innovations to investment protection and it establishes the most progressive system to date for Investor-to-State Dispute Settlement.

3.1.2. INVESTOR-STATE ADJUDICATION IN THE CETA

In Chapter 8, CETA sets precise and new standards on investment. The CETA has been described by the European Commission as providing “clearer and more precise investment protection standards, i.e. the rules, as set out in CETA, removing ambiguities that made these standards open to abuses or excessive interpretations”.³⁸⁸

In the Preamble and in the article 9, CETA expressly establishes regulatory measures. It recognizes that the provisions of this Agreement preserve the right to regulate within their territories, resolving to preserve their flexibility to achieve legitimate policy objectives, such as public health, safety, environment, public morals and the promotion and protection of cultural diversity.³⁸⁹ This means that the host state of the investment can avoid compensation for the measures taken, if they are considered by the tribunals necessary in order to safeguard some primary goals of the state.

³⁸⁷ *Id.* (listing the other chapters considered in CETA).

³⁸⁸ EUROPEAN COMMISSION, *Investment Provisions in the EU-Canada Free Trade Agreement (CETA)*, 2016.

³⁸⁹ CETA, Preamble.

Article 10 introduces a closed text which precisely defines the fair and equitable standard of treatment and the full protection and security without leaving discretion to arbitrators. Usually investment treaties do not specifically describe when a breach of fair and equitable treatment occurs. CETA, making a list of all the factors, avoids uncertainty. A breach of this standard can only arise when there is: a denial of justice in criminal, civil or administrative proceedings, fundamental breach of due process, including a fundamental breach of transparency, in judicial and administrative proceedings, manifest arbitrariness, targeted discrimination on manifestly wrongful grounds, such as gender, race or religious belief, abusive treatment of investors, such as coercion, duress and harassment.³⁹⁰

Concerning the full protection and security clause, the agreement specifies that protection does not extend beyond physical security. Consequently, the host state cannot be liable where security is not given to the investment environment.³⁹¹

In article 12, CETA defines expropriation and it uses the classical definition according to the well-established customary international law.³⁹² Annex A makes clear what constitutes indirect expropriation: “*indirect expropriation occurs where a measure or series of measures of a Party has an effect equivalent to direct expropriation, in that it substantially deprives the investor of the fundamental attributes of property in its investment, including the right to use, enjoy and dispose of its investment, without formal transfer of title or outright seizure*”.³⁹³ For the first time in an EU agreement, parties agreed on such definition especially in order to avoid claims against legitimate regulatory measures taken to protect health, safety

³⁹⁰ CETA, art. X.9.

³⁹¹ CETA, art. 8.10.

³⁹² CETA, art. 12.

³⁹³ CETA, Annex 11.

or the environment.³⁹⁴ Since the differentiation between an indirect expropriation and a regulatory measure has always represented an issue, the CETA gives criteria that the tribunal must take into consideration in order to distinguish between a non-compensable and a compensable action of the state. The tribunal shall consider a number of criteria: the economic impact of the measure or series of measures, the duration of the measure or series of measures of a Party, the extent to which the measure or series of measures interferes with distinct, reasonable investment-backed expectations, and finally, the object, context and intent of the measures.

In Article 8.7, CETA refers to the most favored nation (MFN) clause and it explicitly affirms that the MFN clause cannot be applied to the dispute settlement procedures.³⁹⁵ This means that neither Canada or EU may invoke more favorable dispute solution clause contained in an investment agreement with a third country, since the most favorable mechanism will not be extended to the investors of the country with the less favorable clause.

CETA represents the first agreement that has a binding code of conduct for arbitrators acting in an ISDS dispute.³⁹⁶ The “Code of Conduct for arbitrators and mediators” is contained in the Annex 29-B and it is realized in order to prevent conflicts of interest, for example when an arbitrator in one dispute subsequently becomes a legal representative in another similar dispute, or vice-versa.³⁹⁷

In Article 8.36, CETA introduces full transparency in ISDS disputes: all documents, hearings will be open to the public and interested parties will be able

³⁹⁴ INVESTMENT PROVISIONS IN THE EU-CANADA FREE TRADE AGREEMENT (CETA) http://trade.ec.europa.eu/doclib/docs/2013/november/tradoc_151918.pdf.

³⁹⁵ CETA, art. 8. 7.

³⁹⁶ CETA, art. 8. 25.

³⁹⁷ Annex 29-B, CETA.

to make submissions.³⁹⁸ Moreover, UNCITRAL Transparency Rules must be applied in connection with proceedings.

Article 8.33 establishes a fast track system for rejecting unfounded or frivolous claims.³⁹⁹ Article 8.19 and 8.20 contain specific provisions on mediation and consultation to encourage an amicable solution.⁴⁰⁰

On February 2016, the Contracting Parties agreed to remove the ISDS clause and introduce the Investment Court System. This change will be further discussed in Chapter 3.4.2.

In conclusion, CETA is considered a landmark agreement and what was learnt during the CETA talks will most likely inspire the EU negotiators working with the US to achieve similar success.⁴⁰¹ It is obvious that both agreements have a similar goal: creating a comprehensive agreement that helps companies prosper in the transatlantic market place.⁴⁰² Nevertheless, EU stresses that CETA and TTIP are two separate negotiations with two different partners and it does not prejudge the outcome of the EU-US negotiations.⁴⁰³

3.2. FTA WITH VIETNAM

On 2 December 2015, the conclusion of the negotiations for an EU-Vietnam Free Trade Agreement (FTA) was announced by EU and Vietnam. The negotiations started in June 2012 with a view to ensure an agreement, both on trade

³⁹⁸ CETA, art. 8. 33

³⁹⁹ CETA, art. 8. 20, art. 8.30

⁴⁰⁰ CETA, art. 8.18

⁴⁰¹ Questions and answers <http://ec.europa.eu/trade/policy/in-focus/ceta/questions-and-answers/>.

⁴⁰² *Id.* (referring to the similarities between CETA and TTIP).

⁴⁰³ *Id.* (specifying that CETA and TTIP represent two separates negotiations).

and investment. After the conclusion of negotiations, the legal review and translation into the EU's official languages and Vietnamese began. Then, the Commission will issue a proposal to the Council of Ministers for approval of the agreement. The final agreement will have a legally binding link to the Partnership and Cooperation Agreement (PCA) that deals with the overall relationship between the EU and Vietnam.⁴⁰⁴

The aim of the agreement is to unlock a market with huge potential for EU firms, supporting Vietnam's transition towards a more competitive and smarter economy. Moreover, it will trigger high quality investment in both directions, supported by a new investment dispute resolution system.⁴⁰⁵

EU Trade Commissioner, Cecilia Malmström, said: "*Today's completion of the negotiations is good news for both the EU and Vietnam. Vietnam is a vibrant economy of more than 90 million consumers with a growing middle class and a young and dynamic workforce. Its market has great potential and offers numerous opportunities for the EU's agricultural, industrial and services exports. This FTA is also significant because of its strong focus on sustainable development. It will support Vietnam's efforts to further enhance economic growth and development for its people in the years to come. This agreement provides a new model for trade policy with developing countries*". Commissioner Malmström added: "*The EU and Vietnam have also committed to ensure the respect of workers' rights and to support a sustainable management of natural resources*".⁴⁰⁶

⁴⁰⁴ *The EU and Vietnam finalise landmark trade deal*, Brussels, 2015 available at <http://trade.ec.europa.eu/doclib/press/index.cfm?id=1409>.

⁴⁰⁵ *Id.* (stating the aim of the FTA with Vietnam).

⁴⁰⁶ *Id.* (reporting the words of the EU Trade Commissioner).

The Agreement will reduce tariff and non-tariff restrictions, facilitate licenses, establish rules of origin, and liberalize temporary work permissions for foreign employees.⁴⁰⁷

Considering the investment chapter, the EU-Vietnam FTA incorporates the traditional protections for qualifying foreign investors and their investments explained in Paragraph 1.1.1. It obviously considers the obligation to provide ‘fair and equitable treatment’, ‘full protection and security’, ‘national treatment’ and ‘most favored nation treatment’. However, in relation to the two last clauses, the agreement is subject to important exceptions for certain industries including communication services, cultural services, fishery, forestry, mining and oil and gas. The treaty also guarantees that any expropriation of a qualifying investment will be accompanied by ‘prompt, adequate and effective’ compensation.⁴⁰⁸

Vietnam has agreed to accept the EU's novel approach on investment protection, a permanent investment dispute resolution system with an appeal mechanism.⁴⁰⁹

3.3. TRANSATLANTIC TRADE AND INVESTMENT PARTNERSHIP BETWEEN UNITED STATES AND EUROPEAN UNION (TTIP)

On June 17th 2013, representatives from the European Union and the United States gathered at the G8 Summit in Northern Ireland and announced their commitment to the Transatlantic Trade and Investment Partnership (the “TTIP”),

⁴⁰⁷ H. PAST, *Eu- Vietnam Trade: Commerce for Free Trade Agreement* available at http://www.eurocommerce.eu/media/11171/eu_vietnam_150414.pdf.

⁴⁰⁸ *See generally*, Agreement with Vietnam, Chapter II, section II.

⁴⁰⁹ *The EU and Vietnam finalise landmark trade deal*, Brussels, 2 December 2015 available at <http://trade.ec.europa.eu/doclib/press/index.cfm?id=1409>.

for the first time.⁴¹⁰ That day represented a special day for relations between European Union and the United States.⁴¹¹ The TTIP, if ever realized, will integrate two of the most developed, most sophisticated, and certainly the largest economies in the world.⁴¹² Since its onset, both parties recognized that it did not represent an easy task, but they promised to find convincing answers to legitimate concerns, and solutions to thorny issues.⁴¹³ The purpose of this agreement is to reaffirm the strong partnership and the shared values of democracy and individual freedom in a common commitment to create jobs and sustainable growth.⁴¹⁴ These parties aim to build their common wealth and a safer, more prosperous world for future generations.⁴¹⁵

If ratified, the TTIP will feature a chapter on investments and an investor-state arbitration clause.⁴¹⁶

This Part explores the current status of the TTIP, defines the main aspects of this agreement and describes the rationale behind the investment chapter. Paragraph 3.3.1 provides an overview of the TTIP, by laying out what this free

⁴¹⁰Remarks by President Obama, European Commission President Barroso, and European Council President Van Rompuy on the Transatlantic Trade and Investment Partnership (June 17 2013) <https://www.whitehouse.gov/the-press-office/2013/06/17/remarks-president-obama-uk-prime-minister-cameron-european-commission-pr> ; PRESIDENTS BARROSO AND OBAMA ANNOUNCE LAUNCH OF TTIP NEGOTIATIONS <http://www.euintheus.org/press-media/ttip-launch-with-president-obama-at-g8-a-powerful-demonstration-of-our-determination-to-shape-an-open-and-rules-based-world-says-president-barroso/> (discussing how politicians have stressed the importance of TTIP).

⁴¹¹ *Id.* (addressing the relevance of the episode).

⁴¹² *Id.* (stating the importance of the TTIP).

⁴¹³ *Id.* (referring to the undertaking of the states).

⁴¹⁴ EU-US, Joint statement (Mar. 26 2014) http://www.eeas.europa.eu/statements/docs/2014/140326_02_en.pdf.

⁴¹⁵ *See supra* note 406 (describing the final aim of the parties).

⁴¹⁶ EUROPEAN COMMISSION, *Investment Protection and Investor-to-State Dispute Settlement (ISDS) in European Union agreements* http://trade.ec.europa.eu/doclib/docs/2014/march/tradoc_152273.pdf ; M. WEAVER, *op.cit.*, 235 ff. (specifying the contents of the TTIP).

trade agreement entails. Paragraph 3.3.2. will consider the United States and the European Union background in the negotiation. Paragraph 3.3.3. will consider the United States and European Union positions, discussing how the negotiations will likely be executed.

3.3.1. OVERVIEW ON THE TTIP

The TTIP is a proposed FTA currently under negotiation between the United States and European Union.⁴¹⁷ The TTIP deals with three different areas: market access, regulatory components and rules.⁴¹⁸ Concerning the area of market access, the TTIP's goal is to increase market access through the elimination of barriers to trade and investment in goods, services, and agriculture and the further opening of government procurement markets; the average tariffs between the United States and the European Union are already relatively low, at an average rate of about 3.5% ad valorem for the United States and about 5.5% for the European Union.⁴¹⁹ However, there are higher tariffs on certain import-sensitive product categories such as dairy, sugar and confectionery, beverages and tobacco, fish and fish merchandises, and textiles and apparel.⁴²⁰ Given the magnitude of the transatlantic

⁴¹⁷ S. I. AKHTAR, V. C. JONES, *Cong. Research Serv., R43158, Proposed Transatlantic Trade And Investment Partnership (Ttip): In Brief*, 2013, 1; EUROPEAN COMMISSION, *The Transatlantic Trade and Investment Partnership (TTIP), TTIP explained*, 2015 available at http://trade.ec.europa.eu/doclib/docs/2014/may/tradoc_152462.pdf.

⁴¹⁸ S. I. AKHTAR, V. C. JONES, *op.cit.* 1; EUROPEAN COMMISSION, *The Transatlantic Trade and Investment Partnership (TTIP)*, p.1 (analyzing the main parts of the TTIP).

⁴¹⁹ S. I. AKHTAR, V. C. JONES, *op.cit.* 6; EUROPEAN COMMISSION, *The Transatlantic Trade and Investment Partnership (TTIP)*, p.1 (outlining how US-European Union market works and how tariffs currently stand).

⁴²⁰ S. I. AKHTAR, V. C. JONES, *op.cit.* 6; EUROPEAN COMMISSION, *The Transatlantic Trade and Investment Partnership (TTIP)*, p.1 (discussing which products feature higher tariffs between United States and European Union).

relationship, further elimination and reduction of tariffs could yield significant economic gains.⁴²¹

In relation to the regulatory issues the TTIP will enhance regulatory coherence and cooperation.⁴²² The crux of the TTIP, as regarded by many commentators, hinges on regulatory issues.⁴²³ Fundamental sectors of interest include automobiles, chemicals, cosmetics, information communication technologies, medical devices, pesticides, and pharmaceuticals.⁴²⁴ However, there is disagreement on whether a comprehensive agreement on regulatory issues will actually be reached, as stark differences between the United States and European Union respective positions still exist.⁴²⁵

Firstly, the United States and European Union have been discussing various regulatory disparities, and although many have been resolved, a number of issues still remain.⁴²⁶

Second, some of the regulatory differences depend on divergent public preferences and values.⁴²⁷ For example, European consumers usually prefer “naturally produced” foods, while American consumers are inclined to accept

⁴²¹ S. I. AKHTAR, V. C. JONES, *op.cit.* 6; EUROPEAN COMMISSION, *The Transatlantic Trade and Investment Partnership (TTIP)*, p.1 (addressing that a change of the tariffs could have a strong economic impact).

⁴²² S. I. AKHTAR, V. C. JONES, *op.cit.* 7; EUROPEAN COMMISSION, *The Transatlantic Trade and Investment Partnership (TTIP)*, p.1 (affirming what the regulatory chapter will realize).

⁴²³ S. I. AKHTAR, V. C. JONES, *op.cit.* 7; See generally *Usitc, Trade Barriers That Us Small And Medium-Sized Enterprises Perceive As Affecting Exports To The European Union, Investigation NO. 332-541, PUB. 4455, MARCH 2014*, <http://www.usitc.gov/publications/332/pub4455.pdf> (elucidating that the regulatory chapter is often considered the most important part of the TTIP).

⁴²⁴ S. I. AKHTAR, V. C. JONES, *op.cit.*, 7 (listing the main areas of the regulatory chapter).

⁴²⁵ S. I. AKHTAR, V. C. JONES, *op.cit.*, 7 (noting that there will be difficulties in finalizing the agreement).

⁴²⁶ S. I. AKHTAR, V. C. JONES, *op.cit.*, 7 (addressing problems related to the regulatory chapter).

⁴²⁷ S. I. AKHTAR, V. C. JONES, *op.cit.*, 7 (stating that some of the differences between United States and European Union relate to preferences and values).

products developed by alternative forms of agricultural production, like genetically modified food (GMO).⁴²⁸

Third, while European Union has a preventative decision-taking approach in the case of risk (precautionary principle), some United States enterprises think that this approach can impact businesses since it would lead stringent limits on regulation.⁴²⁹ The European Union is discussing these regulatory standards with the United States on the rigorous condition that no concessions are made regarding the levels of protection currently in Europe, such as health shields, environmental safeguards and consumer protections.⁴³⁰ Regulatory calibration and mutual recognition will only be possible if confluence on the safety and environmental standards is assured.⁴³¹

Finally, the TTIP will develop new rules in areas such as foreign direct investment, intellectual property rights, labor, the environment, and emerging areas of trade.⁴³² Many trade rules are already regulated in the World Trade Organization (WTO) of which both the United States and European Union are members, and this means that they will probably refer to them.⁴³³ Other trade-related rules, while not addressed in the WTO, have become a standard part of United States and European Union FTAs with other countries.⁴³⁴ The negotiations

⁴²⁸ S. I. AKHTAR, V. C. JONES, *op.cit.*, 7 (illustrating an example of different preferences between United States and European Union consumers).

⁴²⁹ S. I. AKHTAR, V. C. JONES, *op.cit.*, 7 (clarifying that while European Union prefers a precautionary approach, United States disagrees, considering the impact on small-business activities). Concerning the precautionary principle look at article 191 TFEU.

⁴³⁰ EUROPEAN COMMISSION, *The Transatlantic Trade and Investment Partnership (TTIP)* (describing the conditions imposed by European Union for the negotiation of regulatory measures).

⁴³¹ *Id.* (noting which guarantee will probably be necessary for reaching the agreement).

⁴³² S. I. AKHTAR, V. C. JONES, *op.cit.*, 8 (demonstrating the scope of the TTIP).

⁴³³ *Id.* (commenting that TTIP rules may be similar to some already established practices).

⁴³⁴ *Id.* (asserting that some rules, not contained in the WTO are considered standards).

could also break new ground on other issues that are not heavily featured, or even present, in prior FTAs and multilateral agreements, such as on state-owned enterprises.⁴³⁵

An agreement on market access, regulations and rules is fundamental because it represents an opportunity to boost transatlantic economic growth.⁴³⁶ Not only the limitation on market access but also the differences on rules and regulation often cost time and money.⁴³⁷ This is the reason why if the TTIP will be realized, the United States and European Union could make real savings for their businesses, create jobs and bring better value for consumers.⁴³⁸

3.3.2. EUROPEAN UNION AND UNITED STATES APPROACHES DURING THE NEGOTIATIONS OF THE TTIP

This Section will focus on the Contracting Parties to the TTIP, that is, the United States and the European Union. Firstly, it will describe the European Union background, the European Union competence, available drafts released to the public, and the main provisions of the proposed agreement. Secondly it will consider the United States Model BIT, the principal source on the United States' point of view.

As stated in Chapter II, Paragraph A, Part 1, with Article 207 of the Lisbon Treaty the European Union has acquired the right to regulate foreign direct

⁴³⁵ *Id.* (arguing that the TTIP could potentially create new standards).

⁴³⁶ *Id.* (outlining what the TTIP can represent).

⁴³⁷ WHAT'S TTIP?, in *The Colorado European Union Center of Excellence*, 2014, <http://www.du.edu/korbel/ceuce/publications/blog/2014/lambert-what-is-ttip.html> (addressing the problems of barriers in trade).

⁴³⁸ *Id.* (stating what the TTIP can bring in the world economy).

investment.⁴³⁹ Consequently, the European Union can exercise an exclusive competence provided by the Lisbon Treaty and reform the regime of the existing treaties of Member States.⁴⁴⁰ In June 2012 a first draft (“the European Union Draft”) text was released.⁴⁴¹ The European Commission’s Trade Policy Committee released initial negotiating objectives for the TTIP (“European Union Directive”) in June 2013 in a private correspondence with Member States.⁴⁴²

The ISDS clause initiated debate in the European Union Commission and, therefore, the Commission organized a public consultation on twelve issues between March 27 and July 13, 2014.⁴⁴³ The consultation outlined a possible European Union approach in order to achieve a balance between the protection to investors and the European Union’s and Member States’ right to regulate.⁴⁴⁴ Obviously, all the documents related to TTIP, according to the European Court of Justice, will be subject to the European Union transparency procedure.⁴⁴⁵

In November 2015, the European Commission completed its new approach on investment protection and investment dispute resolution for the TTIP, proposing

⁴³⁹ TFEU, art. 207; EUROPEAN COMMISSION, *Commission Proposal for a Regulation of the European Parliament and of the Council Establishing a Framework for Managing Financial Responsibility Linked to Investor-State Dispute Settlement Tribunals Established by International Agreements to which the European Union is Party*, COM (2012) 335 p. [hereinafter European Union Draft].

⁴⁴⁰ TFEU art. 207; European Union Draft.

⁴⁴¹ European Union Draft.

⁴⁴² EUROPEAN COMMISSION, Initial Position Paper of the Trade Policy Committee on Transatlantic Trade and Investment Partnership (TTIP), COM (2013) 238/13.

⁴⁴³ EUROPEAN COMMISSION, European Commission launches public online consultation on investor protection in TTIP, 2014 (introducing the role of public opinion in Europe).

⁴⁴⁴ *Id.* (stating the value of the public consultation).

⁴⁴⁵ Case C-350/12 P, Council v. Int’l Veld, 2014 EUR-Lex Celex Lexis 2039 (Jul 3, 2014). (clarifying the role of transparency in EU).

an Investment Court System.⁴⁴⁶ The Investment Court System could replace all the ISDS mechanisms in European union agreements, aiming to create a permanent mechanism in investment dispute solution.⁴⁴⁷

While the European Union has publicly stated its desire to release an official public text of the European Union position on the ISDS provision in the TTIP, the United States does not want to publicly release any information regarding the closed-door negotiations.⁴⁴⁸ To understand the United States approach, it is necessary to refer to the Model US BIT adopted in 2004 and revised by the Obama administration in 2012.⁴⁴⁹ Like its predecessor 2004 model BIT, the 2012 model BIT provides strong investor protections and preserves the government's ability to regulate in favor of the public interest.⁴⁵⁰ The Obama administration made several important changes to the BIT text to enhance transparency and public participation;

⁴⁴⁶ EUROPEAN COMMISSION, *EU finalises proposal for investment protection and Court System for TTIP* (Nov. 2015) <http://trade.ec.europa.eu/doclib/press/index.cfm?id=1396>; EUROPEAN COMMISSION, *Transatlantic Trade And Investment Partnership: Trade In Services, Investment And E-Commerce* (Nov. 12, 2015) [hereinafter the Proposal] http://trade.ec.europa.eu/doclib/docs/2015/november/tradoc_153955.pdf (introducing the investment permanent court)

⁴⁴⁷ The Proposal (analyzing the effects of the introduction of an investment permanent court).

⁴⁴⁸ M. WEAVER, *op.cit.*, 258 ff.; J. CRISP, *US to open TTIP reading rooms across EU*, (Apr. 29 2015, 8:40) available at <http://www.euractiv.com/sections/trade-society/us-open-ttip-reading-rooms-across-eu-314175> (the approach of the United States regarding the transparency of the negotiation).

⁴⁴⁹ U.S. Model BIT; EUROPEAN COMMISSION, *Transatlantic Trade and Investment Partnership Trade In Services, Investment And E-Commerce Chapter Ii – Investment*, 2015, available at http://trade.ec.europa.eu/doclib/docs/2015/september/tradoc_153807.pdf (introducing the main source in order to identify the United States view on investor-state arbitration).

⁴⁵⁰ OFFICE OF THE U. S. TRADE REPRESENTATIVE, *United States Concludes Review of Model Bilateral Investment Treaty*, 2002, available at <https://ustr.gov/about-us/policy-offices/press-office/press-releases/2012/april/united-states-concludes-review-model-bilateral-inves> . (describing characteristics of the US MODEL BIT).

sharpen the disciplines that address preferential treatment to State-owned enterprises; and strengthen protections relating to labor and the environment.⁴⁵¹

3.3.3. UNITED STATES AND EUROPEAN UNION PERSPECTIVES ON A TTIP

The previous sections discussed the negotiations for CETA and the Agreements with Vietnam that have been already finalized. Since the TTIP is still ongoing it is interesting to analyze the United States' and the European Union's approach in investor-state arbitration. The main questions that have been subject of public consultation in Europe as regards the main classical provisions in a BIT can be a starting point for comparison between the United States and European Union perspectives on a TTIP. Consequently, this section will analyze differences and similarities and consider the US Model BIT, the European Union drafts and the relevant public documents.

Considering the scope of the substantive investment protection provisions, both sides have a very broad definition of investment. The definition included contributions to the economic development of the host State, monetary contributions, certain duration of performance for a contract and a participation in the risks of the transaction. The US Model and European Union Proposal on the Investment Permanent Court also provide similar lists of examples of investment, which include enterprise; shares, stocks and other forms of equity participation in an enterprise; bonds, debentures and other debt instruments of an enterprise; loans to an enterprise, etc.⁴⁵²

⁴⁵¹ *Id.* (stating the differences between the US MODEL BIT of 2004 and the US MODEL BIT of 2012).

⁴⁵² U.S. Model BIT art. 1; the Proposal (considering the differing approaches in defining investment between the United States and European Union).

Referring to the non-discriminatory treatment for investors, both the European Union Proposal on the Investment Permanent Court and US Model BIT consider that foreign investors should not be discriminated against.⁴⁵³ At the same time the aforementioned materials recognize that in certain rare cases, discrimination against investors may need to be envisaged.⁴⁵⁴ The European Union also includes exceptions for differences in treatment between investors and investments where necessary to achieve public policy objectives (the protection of health, the environment, consumers, etc.).⁴⁵⁵

Considering the fair and equitable treatment, the main objective of the European Union is to clarify the standard in a way that a State could be held responsible only for breaches of a limited set of basic rights.⁴⁵⁶ These are: the denial of justice, the disregard of the fundamental principles of due process; manifest arbitrariness; targeted discrimination based on gender; race or religious belief; and abusive treatment, such as coercion, duress or harassment.⁴⁵⁷ The US Model BIT describes this provision only referring to the concept of the denial of justices and due process.⁴⁵⁸

About expropriation, the two provisions are very similar, as they refer to the typical definition of expropriation.⁴⁵⁹ One difference between the two documents

⁴⁵³ The Proposal, art. 3; U.S. Model, ANNEX B (considering the non-discrimination clause).

⁴⁵⁴ The Proposal, art.2; U.S. Model, ANNEX B (analyzing the exception to the non-discrimination clause).

⁴⁵⁵ The Proposal, art.2; U.S. Model, ANNEX B (explaining the specificity of the European Union provision).

⁴⁵⁶ The Proposal, art. 3 (addressing the objective of European Union regarding the fair and equitable treatment).

⁴⁵⁷ The Proposal, art. 3 (mentioning the main rights linked to the fair and equitable treatment).

⁴⁵⁸ U.S. Model, art. 5 (considering the United States point of view in the fair and equitable treatment).

⁴⁵⁹ U.S. Model, art.6; the Proposal, art. 5 (considering in general the position of the Contracting Parties on the expropriation clause).

is that the European Union Draft is more detailed on public welfare objectives.⁴⁶⁰ The US considers public welfare objectives to be public health, safety, and the environment.⁴⁶¹ Meanwhile, the European Union considers non-discriminatory measures taken for legitimate public purposes to be the protection of public health, safety, environment or public morals, social or consumer protection or promotion and protection of cultural diversity.⁴⁶²

Article 2 of the European Union Proposal on the Investment Permanent Court contains a specific article describing regulatory measures.⁴⁶³ The European Union objective is to achieve a balance between the protection of investors and the Member States' right to regulate.⁴⁶⁴ The European Union plans to safeguard the Member States' right to regulate as a basic underlying principle, that investment protection standards cannot be interpreted by arbitral tribunals in a manner that would detrimentally affect the right to regulate, and that the European Union will ensure that all the necessary safeguards and exceptions are in place.⁴⁶⁵ There is no United States specific provision on the issue.⁴⁶⁶

Both the United States Model and the European Union Proposal on the Investment Permanent Court aim to ensure transparency and openness in the ISDS system under TTIP, making hearings open and all documents available to the

⁴⁶⁰ The Proposal, Annex 1 (explaining how the European Union provision is more detailed).

⁴⁶¹ U.S. Model, Annex B (discussing the United States provision on expropriation).

⁴⁶² The Proposal, Annex 1 (considering the European Union provision on expropriation).

⁴⁶³ The Proposal, art.2 (introducing the concept of regulatory measure).

⁴⁶⁴ EUROPEAN COMMISSION, European Commission launches public online consultation on investor protection in TTIP, 2014 (discussing the aim of the EU).

⁴⁶⁵ *Id.* (analyzing the objective of the EU).

⁴⁶⁶ U.S. Model, (underlying that there is not a provision on the right to regulate in the US Model BIT).

public.⁴⁶⁷ The European Commission also proposed to include the 2013 UNCITRAL Rules on Transparency in Treaty-based Investor-State-Arbitration as mandatory in the TTIP.⁴⁶⁸ These rules would “contribute significantly to the establishment of a harmonized legal framework for a fair and efficient settlement of international investment disputes, increase transparency and accountability and promote good governance.”⁴⁶⁹

Both the United States and the European Union address the problem of multiple claims, since investors are able to either seek to obtain redress in domestic courts or to submit a claim to the Investment Tribunal.⁴⁷⁰ They also require a cooling-off period, for the parties before seeking arbitration, that means to engage in consultation or mediation, in order to support domestic rule.⁴⁷¹ Nevertheless, no mandatory exhaustion of local remedies is required.⁴⁷²

The European Union proposes the introduction of instruments to easily dismiss frivolous claims.⁴⁷³ For instance, the European Union is proposing that the losing party to any arbitration case should bear all reasonable costs of the proceedings if a disputing party has acted improperly by raising manifestly frivolous objections or improper preliminary objections or unfounded claims.⁴⁷⁴

⁴⁶⁷ EUROPEAN COMMISSION, European Commission launches public online consultation on investor protection in TTIP, 2014; U.S. Model, art. 29 (describing the purpose of the European Union and US).

⁴⁶⁸ The Proposal, art. 18 (analyzing the European Union proposal).

⁴⁶⁹ UNCITRAL, Rules on Transparency in Treaty-based Investor-State-Arbitration, preamble (clarifying the object of the rule).

⁴⁷⁰ The Proposal, art.14; U.S. Model, art. 23 (introducing the multiple claim issue).

⁴⁷¹ The Proposal, art. 2,3,4,5; U.S. Model, art. 23 (addressing the cooling-off period clause).

⁴⁷² The Proposal; U.S. Model, art. 24(discussing the absence of the exhaustion of local remedies provision).

⁴⁷³ EUROPEAN COMMISSION, European Commission launches public online consultation on investor protection in TTIP, 2014 (stating the European Union proposal on frivolous claim).

⁴⁷⁴ The Proposal, art. 28.2 (explaining the European Union proposal).

The US Model BIT refers only to the possibility that the tribunal could consider the claimant's claim or the respondent's objection in order to verify whether or not it was frivolous.⁴⁷⁵

The European Union intends to introduce a specific mechanism called a filter.⁴⁷⁶ A filter grants a Party to the agreement the opportunity to intervene and dismiss claims in particular cases that involve measures taken for prudential reasons in order to protect the overall stability and integrity of the financial system.⁴⁷⁷ The protection of the financial system is also considered in the US Model BIT, establishing a sovereign right to regulate for the United States in certain areas.⁴⁷⁸

The United States and the European Union have an identical approach on interpretation.⁴⁷⁹ They agree on the binding interpretation that ISDS tribunals must respect to limit undesirable interpretations by ISDS tribunals.⁴⁸⁰ Moreover, the parties agree to establish that the non-disputing party can present written or oral submissions on issues relating to the interpretation of the Agreement.⁴⁸¹

In conclusion, it is dubious whether the TTIP will come to fruition, but in the event that it does, it holds the potential to revolutionize the global economy.⁴⁸²

⁴⁷⁵ U.S. Model, art. 28 (describing the United States provision).

⁴⁷⁶ EUROPEAN COMMISSION, European Commission launches public online consultation on investor protection in TTIP, 2014 (introducing the European Union proposal on claims).

⁴⁷⁷ *Id.* (discussing the European Union proposal).

⁴⁷⁸ U.S. Model (noting the lack of any filter in the US model Bit on the same topic).

⁴⁷⁹ U.S. Model, art. 30. 3; the Proposal, art. 13 (analyzing similarities between United States and European Union).

⁴⁸⁰ U.S. Model, art. 30. 3; the Proposal, art. 13 (describing the approach of United States and European Union on interpretation).

⁴⁸¹ U.S. Model, art.28; the Proposal, art. 22.3 (observing that the parties can submit questions related to the interpretation of the Agreement).

⁴⁸² *See generally* Paragraph 3.3.; MICHAEL BECKERMAN, *The Future of the Global Economy Depends on the U.S.-EU Trade Deal*, 2013 (analyzing the consequences of the TTIP).

The United States and the European Union, two huge modern economies, have the chance to create a completely new system that will simplify trade and investment between both Contracting Parties.⁴⁸³ However, numerous concerns exist in relation to all the chapters within the TTIP.⁴⁸⁴ In particular referring to the chapter pertaining to investment a number of obstacles must first be overcome.⁴⁸⁵ As explained earlier, the European Union has proposed a public consultation on twelve main issues, the resolution of which deals with most of these concerns.⁴⁸⁶

The aim of this work is neither to realize a political analysis, nor a social one. This work analyzes the main issues about the investor-state arbitration dispute solution, looking exclusively at the United States and European Union texts. The resulting discovery is that upon dissection, the United States and European Union positions on law are not as far apart as they initially seem — moreover, they seem reconcilable.⁴⁸⁷

The United States and European Union have similar points of view on scope of the substantive investment protection provisions, non-discriminatory treatment for investors, fair and equitable treatment, expropriation, multiple claims and relationship to domestic courts, reducing the risk of frivolous and unfounded cases, and guidance by the parties (the European Union and the US) on the interpretation of the agreement.⁴⁸⁸

⁴⁸³ *See generally* Paragraph 3.3. (addressing which area the TTIP focus on).

⁴⁸⁴ *See supra* note 406 (affirming that the realization of the TTIP represents a difficult task).

⁴⁸⁵ *See generally* Paragraph 3.3. (considering the general issues of the investment chapter).

⁴⁸⁶ EUROPEAN COMMISSION, European Commission launches public online consultation on investor protection in TTIP, 2014 (taking into account the role of the public opinion).

⁴⁸⁷ *See generally* Paragraph 3.3.2. (affirming that the position between the United States and European Union are not different).

⁴⁸⁸ *See generally* Paragraph 3.3.2. (clarifying which points the United States and European Union have in common).

While the United States and European Union agree on many issues, it remains unclear how the parties could agree on the proposed Investment Permanent Court and on an appellate mechanism. These two problems will be now analyzed.

3.4. THE INVESTMENT COURT SYSTEM

In response to the criticism on the investor-state arbitration mechanism, the Commission has changed its initial approach in relation to the investment clause in the TTIP, specifically, to the composition, competences, and powers of the arbitrators. This change may be found in the proposal of the Commission made on the 21st of November, 2015.⁴⁸⁹ This is in part based on the concept paper on *Investment in TTIP and Beyond – the Path for Reform. Enhancing the Right to Regulate and Moving from the Current ad hoc Arbitration towards an Investment Court*, May 2015.⁴⁹⁰ Both the Concept Paper and the Proposal modify the ISDS, with the result in the creation of an advanced system for the solution of controversies, called Investment Court System (ICS).⁴⁹¹

This approach is based on the innovations of the ISDS clause introduced in the Agreement with Singapore and the previous text of the CETA before its revision. Paragraph 3.4.1. will deal with the Investment Court System contained in the Proposal of the Commission. Paragraph 3.4.2. will analyze the dispute solution mechanism in the agreements with CETA and Vietnam trying to making

⁴⁸⁹ The Proposal.

⁴⁹⁰ EUROPEAN COMMISSION, *Investment in TTIP and beyond – the path for reform Enhancing the right to regulate and moving from current ad hoc arbitration towards an Investment Court*, available at http://trade.ec.europa.eu/doclib/docs/2015/may/tradoc_153408.PDF.

⁴⁹¹ D. GALLO, *La Proposta della Commissione europea in merito al sistema di risoluzione delle controversie tra Stato e investitore previsto nel Transatlantic Trade and Investment Partnership (TTIP) e la recente prassi dell'Unione europea: una rivoluzione è in atto?* in Severino, Del Vecchio, Bari 2016.

a comparison with the Proposal made by the Commission for the TTIP with the United States. Finally, Paragraph 3.4.3. will introduce some issues concerning the relationship between the Investment Court System and the EU law, in particular the role of the European Court of Justice.

3.4.1. THE INVESTMENT COURT SYSTEM IN THE PROPOSAL OF THE COMMISSION

The Proposal, to which the US has not given an answer, is focused on the second chapter of the TTIP that is in the title related to services, investments and e-commerce. The last section is titled “*Resolution of Investment Disputes and Investment Court System*” and it is composed of thirty articles, and two addenda. The first of these focuses on mediation, and the other on the Code of Conduct of Arbitrators. The thirty articles are divided into different subsections. The fourth subsection is titled Investment Court System, which is composed of articles nine through 12, and it represents the changes that will affect the nature and the functioning of the arbitrators.⁴⁹²

Article 9 is the most important modification, because it supersedes the traditional model of the ISDS, characterized by an arbitral tribunal, and generally composed of three arbitrators, two of whom are nominated by the Parties, and the final chosen in common.⁴⁹³

This provision introduces a new tribunal that must solve controversies which arise on the basis of Article 6, which identifies four kinds of applicable norms: the *ICSID* Convention, the *Additional Facilities Rules*, the UNCITRAL

⁴⁹² *Id.*

⁴⁹³ The Proposal, art.9.

rules, and the other rules chosen by the parties on the request of the investor.⁴⁹⁴ The tribunal is of first grade and it is composed of fifteen members, in charge for 6 years (renewable), denominated “*judges*” and not arbitrators.⁴⁹⁵

The nomination is realized by an organ named *Committee* in the Proposal, the composition of which is not completely clear. There are three possible hypotheses: a Committee with a general competence, a Committee with a specific competence in services and investments, and a Committee with a competence on trade, including investments.⁴⁹⁶

Of the fifteen judges, five are citizens of a Member State of the European Union, five come from the United States and five come from third States.⁴⁹⁷ It is not clear whether or not the five judges coming from European Union and third states must be of different nationalities.⁴⁹⁸

Paragraph 6 provides that the tribunals decide in divisions of three judges, one judge coming from the United States, one from European Union and one of a third country, that will be the president of the division.⁴⁹⁹ It has not been established whether the judge of the Member State must have the nationality of the investor, if European, or of the State, if the investor will be American.⁵⁰⁰

The presidency is assigned in rotation for two years to one of the five judges coming from a third country and the president has to ensure that the composition of the divisions will be random and unpredictable.⁵⁰¹

⁴⁹⁴ The Proposal, art. 6.

⁴⁹⁵ The Proposal, art.9.

⁴⁹⁶ D. GALLO, *op.cit.*

⁴⁹⁷ The Proposal, art. 9.

⁴⁹⁸ D. GALLO, *op.cit.*

⁴⁹⁹ The Proposal, art.9. para. 6.

⁵⁰⁰ D. GALLO, *op.cit.*

⁵⁰¹ The Proposal, art.9. para. 7.

Paragraph 4 refers to the professional qualification of the judges and it establishes that the judges shall possess the qualifications required in their respective countries for appointment to judicial office, or be jurists of recognized competence. Moreover, they must have demonstrated expertise in public international law, in particular in international investment law, international trade law and the resolution of disputes arising under international investment or international trade agreements.⁵⁰²

This is extremely important because it means that it is necessary that judges have to be expert not only on the trade and investment but that they have a broad knowledge in law in a way that they will take into consideration international law, including norms on interpretation, and human rights protection.⁵⁰³

Paragraph 15 relates to the retribution of the Tribunal and surprisingly affirms that the fees may be permanently transformed into a regular salary. In this way the Judges shall serve on a full-time basis and they will not be permitted to engage in any occupation.⁵⁰⁴

Finally, paragraph 16 establishes that the Secretariat of ICSID and/or the Permanent Court of Arbitration shall act as Secretariat for the Tribunal.⁵⁰⁵

Article 10 introduces for the first time in an international trade and/or investment agreement an appellate tribunal, competent on the merit of the awards adopted by the tribunal of first grade on the basis of article 9.⁵⁰⁶

The appellate tribunal is composed of six members, in charge for six years. Two of the six judges come from one Member State of the European Union, two

⁵⁰² The Proposal, art.9. para. 4.

⁵⁰³ D. GALLO, *op.cit.*

⁵⁰⁴ The Proposal, art.9. para. 15.

⁵⁰⁵ The Proposal, art.9. para 16.

⁵⁰⁶ The Proposal, art.9. para. 1.

from the United States and two from a third country nominated by the aforementioned Committee on the basis of the candidates proposed by the European Union and the United States.⁵⁰⁷

The presidency is held on the basis of a rotation by one of the judges national of a third country.⁵⁰⁸

Concerning the professional qualifications of the judges of the appellate tribunal, they are the same as the ones indicated for the tribunal of first instance, with the exception that the Members of the Appeal Tribunal shall possess the qualifications required in their respective countries for appointment to the highest judicial offices, not simply for appointment to the judicial offices.⁵⁰⁹

The organizational rules for the division applicable for the tribunal of first instance are applicable to the Appeal Tribunal as well.⁵¹⁰

An appeal can be based on the grounds of Article 52 of the ICSID Convention or if the Tribunal: (i) erred in the interpretation or application of the applicable law; or (ii) manifestly erred in the appreciation of the facts. The introduction of an appeal mechanism in investment arbitration is a current trend.

The ICSID Secretariat has worked on a possible appellate mechanism, and the 2015 UNCTAD Report also advises in favour of an appellate mechanism. The risk that the specific formulation of the EU Proposal entails is that grounds for appeal such as simple error in the interpretation and application of the law, or manifest error in the appreciation of facts are too wide and leave the door open for systematic appeals. Although Article 29 provides that the decision on appeal must

⁵⁰⁷ The Proposal, art.9. para. 5.

⁵⁰⁸ The Proposal, art.9. para. 7.

⁵⁰⁹ The Proposal, art.9. para. 7.

⁵¹⁰ The Proposal, art.9. para. 8.

be issued within six months, this seems rather unrealistic if the Appeal Tribunal has to re-examine the facts of the case.⁵¹¹

The introduction of this body will help ensure consistency in the interpretation of the TTIP and provide both the government and the investor with the opportunity to appeal against awards and to correct arbitrator errors.⁵¹² The European Union proposes that the appellate body will have jurisdiction over the following alleged errors: interpretation or application of applicable law; appreciation of the facts, including the appreciation of relevant domestic law; or, those provided for in Article 52 of the ICSID Convention.⁵¹³ Although there is no appellate mechanism in the United States Model BIT, the United States has acknowledged the possibility to develop one under other institutional arrangements, while guaranteeing transparency.⁵¹⁴

Article 11 establishes the rules that the judges must respect in order to ensure independency and impartiality.⁵¹⁵

Paragraph 1 affirms that they shall not be affiliated with any government, and consequently they shall not take instructions from any government or organization with regard to matters related to the dispute. Moreover, in order to respond to the criticism made by the civil society it has been clarified that the judges shall not participate in the consideration of any disputes that would create a direct or indirect conflict of interest in compliance with the *Code of Conduct*.

⁵¹¹ L. LE BARS, *The EU Proposal Regarding Investment Protection: The End of Investment Arbitration as We Know It?* in Kluwer Blog Arbitration, 2015, available at <http://kluwerarbitrationblog.com/2015/12/29/the-eu-proposal-regarding-investment-protection-the-end-of-investment-arbitration-as-we-know-it/>.

⁵¹² *Id.* (analyzing the advantages in creating the appellate body).

⁵¹³ The Proposal, art. 10 (stating the scope of competence of the tribunal).

⁵¹⁴ U.S. Model, art. 28 (describing the provision related to the appellate body in the US model BIT).

⁵¹⁵ The Proposal art. 11.

Finally, they shall refrain from acting as counsel or as a party-appointed expert or witness in any pending or new investment protection dispute under this or any other agreement or domestic law.⁵¹⁶ The extent of this norm must be clarified in order to understand how much the judges will be limited in giving legal advice.⁵¹⁷

In order to preserve autonomy, any disputing party that believes that a Judge has conflict of interest shall send a notice of challenge to the appointment to the President of the Tribunal or to the President of the Appeal Tribunal.⁵¹⁸

The last provision of the sub-section 4 is article 12, which establishes that in the case in which an international agreement providing for a multilateral investment tribunal will enter into force between the United States and the European Union, the relevant parts of the sub-section 4 will cease to apply.⁵¹⁹ Considering the sub-section 5, article 13 affirms that the Tribunal shall apply the provisions of the TTIP and other rules of international law applicable between the Parties. The Tribunal of first instance, in order to determine if there has been a violation, is required to ascertain the meaning of a provision of the domestic law of one of the Parties as a matter of fact, following the prevailing interpretation of that provision made by the courts or authorities of that Party. This interpretation of domestic law will not be binding for other courts or authorities. Finally, the Committee could have the extremely important role of adopting binding decisions interpreting the provisions of Investment Protection or the Resolution of Investment Disputes and Investment Court System Section of the TTIP.⁵²⁰

⁵¹⁶ The Proposal, art. 11, para. 1.

⁵¹⁷ D. GALLO, *op.cit.*

⁵¹⁸ The Proposal, art. 11, para. 2.

⁵¹⁹ The Proposal art. 12.

⁵²⁰ The Proposal art. 13.

3.4.2. THE INVESTMENT COURT SYSTEM: DIFFERENCES AND SIMILARITIES IN THE PROPOSAL, CETA AND THE AGREEMENT WITH VIETNAM

The proposal of the TTIP has represented a model in the negotiations between the European Commission, the Canadian Government and the Vietnamese Government. Both agreements include the new approach on investment dispute settlement: the investment permanent court. This clear break from the past ISDS approach is a clear signal that the EU's intent is to include this new proposal on investment in its negotiations with all partners.

Considering the Committee, while in the Proposal the composition and nature of the Committee that nominates judges is not clear, for CETA each judge will be chosen by the the '*CETA Joint Committee*', that will be composed by the Minister for Commerce of the Canadian Government and Commissioner for Commerce for the European Union. For the Agreement with Vietnam, the committee is represented by the *Trade Committee*, composed by people with a sectorial competence in commerce, including investments.

Considering the composition of the tribunal, first of all while in the Proposal it is stated that the judges will be in charge for six years, in the CETA the Tribunal members will serve for five years and in the Agreement with Vietnam for four years.

Secondly, while in the Proposal and in the Agreement with Vietnam it is up to the President to select the judge of the third country if the parties agree that the controversy will be decided by only one judge of a third country, the CETA is less specific, simply affirming that it must be nominated at random.

Moreover, only in the CETA is it established that the activity of the ICSID Secretariat is financially sustained by the Parties.

Finally, only in the CETA there is a provision considering the case in which the Committee will not act. In such a case, the ICSID Secretariat will act.⁵²¹

Referring to the Appellate tribunal, the Agreement with Vietnam and the Proposal contain similar provisions with two exceptions: the judges are in charge for five years, not six and the Agreement with Vietnam contains a provision, absent in the Proposal, that establishes that a division of the Appeal Tribunal shall make every effort to make any decision by consensus. Where, nevertheless, a decision cannot be arrived at by consensus, a division of the Appeal Tribunal shall render its decision by a majority of votes of all its Members⁵²².

Concerning the CETA, there are three main differences that distinguish it from the Proposal and the Agreement with Vietnam. In particular, in article 8.28, firstly there is no reference to the composition of the arbitrator but it simply establishes that the arbitrator must be randomly appointed.⁵²³ This absence can be justified on the basis that CETA gives the *CETA Joint Committee* powers that are not conferred to the Committee neither in the Proposal nor in the Agreement with CETA.⁵²⁴

Secondly, the members of the tribunal of first instance shall possess the same qualifications as the Appellate tribunal and so they shall possess the

⁵²¹ M. MANGAN, *A Legal Update from Dechert's International Arbitration Group*, 2016 available at https://www.dechert.com/files/Uploads/Documents/The_EU_succeeds_in_establishing_a_permanent_investment_court_in_its_trade_treaties_with_Canada_and_Vietnam_-_Dechert_-_03242016.pdf.

⁵²² Agreement with Vietnam, art. 13; Agreement with Vietnam, art. 13 para. 12.

⁵²³ CETA, art. 8.28, par. 5.

⁵²⁴ D. GALLO, *op.cit.*

qualifications required in their respective countries for appointment to the judicial offices, not the highest judicial offices.⁵²⁵

Finally, while the Proposal and the Agreement with Vietnam extend to the procedure of appeal the application of the provisions on transparency on the Third Party Funding, on the interim decisions, on the discontinuance and the non-disputing party, in CETA the extension is provided only for the non-disputing Party.⁵²⁶

Considering the provision of a multilateral tribunal competent to solve controversies in the area of investments, both the CETA and the Agreement with Vietnam, differently from the Proposal, establish a duty on the Parties to negotiate at an international level, at the institutional tribunal mentioned previously.⁵²⁷ It is written in the CETA and the Agreement with Vietnam, that the Parties shall negotiate, indeed this reference is absent in the Proposal. Moreover, in the CETA, it is expressly affirmed that the Parties shall negotiate an appellate proceeding, while in the Proposal and the Agreement with Vietnam this is a mere eventuality.⁵²⁸ Finally, it will be a CETA joint committee, not the Committee of the Proposal, nor the Trade Committee with the Trade Agreement with Vietnam, that will decide the shrewdness on the institutional level, and if and when the multilateral tribunal will enter into force.⁵²⁹

Concerning the application of the rules on the independence and the impartiality of the judiciary, the CETA, differently from the Proposal and the Agreement with Vietnam, does not refer to the attached code of conduct.⁵³⁰ The

⁵²⁵ CETA, art. 8.28 para. 4.

⁵²⁶ Agreement with Vietnam, art. 28 para. 7; CETA, art. 8.28 para. 4.

⁵²⁷ CETA, art. 8.29; Agreement with Vietnam, art. 15.

⁵²⁸ CETA, art. 8.29; Agreement with Vietnam, art. 15.

⁵²⁹ CETA, art. 8.29; Agreement with Vietnam, art. 15.

⁵³⁰ CETA, art. 8.30; Agreement with Vietnam, art. 8.

attached code of conduct is only valid for the arbitrators of a controversy and mediators but not for the judges of a tribunal.⁵³¹

Another difference is that only the CETA does not impose to abstain as counsel, nominated from one Party or witness, or bi-witness, in pending or future controversies based on the domestic rules of one of the two Parties.⁵³²

A very important difference is that only the CETA establishes that in the case of one Party believing that there is a conflict of interest, it can bring a Notice of Challenge to the appointment to the International Court of Justice. In particular, if, within 15 days from the date of the notice of challenge, the challenged Member of the Tribunal has elected not to resign from the division, the President of the International Court of Justice shall, after hearing the disputing parties and after providing the Member of the Tribunal an opportunity to submit any observations, issue a decision within 45 days of receipt of the notice of challenge and notify the disputing parties and the other Members of the division.⁵³³

On the contrary, in the Proposal and the Agreement with Vietnam, this power is attributed to the Presidents of the tribunals of first instance or the appellate tribunal.⁵³⁴

This provision is unusual because it refers to an institution, or organ, of the United Nations (UN), even if the agreement is signed outside the scope of the UN.⁵³⁵

Considering the issues on the applicable law, both the CETA and the Agreement with Vietnam accept the Proposal's position. The tribunal is not

⁵³¹ CETA, Annex 29.B; CETA, art. 29.7; CETA, art. 29.5.

⁵³² Agreement with Vietnam, art. 14 para. 1; CETA, art. 8.30 para 1.

⁵³³ CETA, art. 8.30 para. 2.

⁵³⁴ The Proposal, art. 11; Agreement with Vietnam, art. 14.

⁵³⁵ D. GALLO, *op.cit.*

required to verify the legitimacy of the measure through the interpretation of the domestic law in question, but its analysis is limited to a check as a matter of fact, and on the basis of the prevalent interpretation of the domestic authorities and courts. Moreover, the tribunals interpretation will not be binding on the domestic authorities and courts.⁵³⁶

While the Proposal only refers to the principles international law, the CETA and the Agreement with Vietnam also refer to the principles of international investment law⁵³⁷.

Moreover, while the Agreement with Vietnam and the Proposal refer only to the domestic law of the investor concerning the interpretation, the CETA does not specify, and consequently, the domestic law of the state may also be relevant.⁵³⁸

In conclusion, the analysis of the Proposal, CETA and the Agreement with Vietnam shows a novel European approach on investments. While there are many similarities between the Proposal, CETA, and the Agreement with Vietnam, however there are also notable differences. The CETA distinguishes itself from the other two on the basis of two aspects. On one side, the Proposal and the Agreement with Vietnam impose more limits on the judges and tribunals, while on the other hand, the CETA has greater openness to public international law, considering the involvement of the Secretary of ICSID and the International Court of Justice.⁵³⁹

3.4.3. EU LIMITS: CONDITIONS FOR INVESTOR-STATE ADJUDICATION UNDER EU AGREEMENTS

⁵³⁶ CETA, art. 8.31 para. 2; Agreement with Vietnam, art. 13 para. 2.

⁵³⁷ CETA, art. 8.31 para. 1; Agreement with Vietnam, art. 13 para. 1.

⁵³⁸ D. GALLO, *op.cit.*

⁵³⁹ *Id.*

After having analyzed the Permanent Investment Court in the CETA, in the Proposal and in the Agreement with Vietnam, it is now important to analyze whether or not this system is consistent with the EU system.

The admissibility of investor-state adjudication is not solely a question of the EU's treaty-making powers under the common commercial policy (article 207 TFEU). Rather, the compatibility of an investor-state dispute settlement in EU international investment agreements raises fundamental questions of EU law since it touches the EU law as “*a new legal order of international law*”, stemmed from an “*independent source of law*” that cannot be overridden by domestic legal provisions.⁵⁴⁰

Consequently, the EU institutions cannot conclude an international agreement that establishes courts that could challenge the effective application of the principles of the EU, among these, also the monopoly of the European Court of Justice.⁵⁴¹

In the first place, it is important to point out that investor-state dispute settlement under future FTAs does not necessarily fall under the Court's reading of Article 344 TFEU as expounded in the *Mox Plant* case. In that case, the Court clarified that an international agreement cannot allow Member States to opt out from the competence of the CJEU.⁵⁴² The reading of the CJEU refers only to EU Member States and it does not seem to come into play in the case of investor-State adjudication as this mechanism does not cover State-to-State disputes.⁵⁴³ However, some authors affirmed that Article 344 TFEU should be applied by analogy to

⁵⁴⁰ *Van Gend & Loos c. Pesi Bassi*, of February 5, 1963, case 26-62, ECLI:EU:C:1963:1, point B, 12; *Flaminio Costa c. E.N.E.L.*, of July 15, 1964, case 6-64, ECLI:EU:C:1964:66, p. 1145; S. W. SHILL, *Luxemburg Limits for Investor-State Dispute Settlement Dispute Under Future Eu Agreements in EU and Investment Agreements*, 2013, p. 39.

⁵⁴¹ TEU, art. 19; D. GALLO, *op.cit.*

⁵⁴² S. W. SHILL, *op.cit.*, 42.

⁵⁴³ *Id.*

investor-state arbitration, even if the article expressly only applies to the relations between Member States.⁵⁴⁴

The autonomy of EU law is not automatically threatened by other international courts and tribunals, and in Opinion 1/91 the court affirmed the general compatibility of EU law with international dispute settlement mechanisms:
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“Where [...] an international agreement provides for its own system of courts, including a court with jurisdiction to settle disputes between the Contracting Parties to the agreement, and, as a result, to interpret its provisions, the decisions of that court will be binding on the Community institutions, including the Court of Justice [...].

An international agreement providing for such a system of courts is in principle compatible with Community law. The Community's competence in the field of international relations and its capacity to conclude international agreements necessarily entails the power to submit to the decisions of a court which is created by such an agreement as regards the interpretation and application of its provisions.”

Assuming that international dispute settlement is compatible with EU law, the Court developed some limits, in light of the autonomy of EU law, in several proceedings under Article 218(11) TFEU.⁵⁴⁶

⁵⁴⁴ In this sense S. HINDELANG, *Circumventing Primacy of EU Law and the CJEU's Judicial Monopoly by Resorting to Dispute Resolution Mechanisms Provided for in Inter-Se Treaties? The Case of Intra-EU Investment Arbitration in Legal Issues of Economic Integration*, 2012, 199 ff.

⁵⁴⁵ S. W. SHILL, *op.cit.*, 44.

⁵⁴⁶ *Id.*

The CJEU has often clarified that courts outside the EU order cannot give binding interpretations on EU law.⁵⁴⁷ In opinion 1/09, on the compatibility with EU law of the European and Community Patents Court, the CJEU stated that if an international agreement concluded with third countries confers new judicial powers on the Court provided, it shall not change the essential character of the function of the Court as conceived in the EU and FEU Treaties.⁵⁴⁸

In the same opinion, the CJEU has also affirmed that an international agreement may affect its own powers providing that the indispensable conditions for safeguarding the autonomy of EU law.⁵⁴⁹

This approach has been further elaborated in Opinion 2/13 on the accession of the EU to the European Convention on Human Rights (ECHR), where the CJEU clarified that it has the monopoly on the interpretation of the European Union law, in the distribution of competences between Member States and European Union and in the allocation of such responsibilities.⁵⁵⁰ This issue is addressed and solved by the Financial Responsibility Regulation.⁵⁵¹

The CJEU also declared the necessity of “*prior involvement procedure*” of the EU for any case pending before the ECHR in a way that the “*EU is fully and systematically informed so that the competent EU institution is able to assess whether the Court of Justice has already given a ruling on the question at issue in*

⁵⁴⁷ Opinion 1/09, Draft agreement – Creation of a unified patent litigation system, [2011] E.C.R. I-1137.

⁵⁴⁸ Opinion 1/09 para. 75.

⁵⁴⁹ Opinion 1/09 para. 76.

⁵⁵⁰ Opinion C-2/13, Draft international agreement – Accession of the European Union to the European Convention for the Protection of Human Rights and Fundamental Freedoms [2013] ¶¶ 179-200, 215-235.

⁵⁵¹ S. SCHILL, *The Proposed TTIP Tribunal and the Court of Justice: What Limits to Investor-State Dispute Settlement under EU Constitutional Law?* in *VerfassungsBlog*, 2015, available at <http://verfassungsblog.de/the-proposed-ttip-tribunal-and-the-court-of-justice-what-limits-to-investor-state-dispute-settlement-under-eu-constitutional-law/>.

that case and, if it has not, to arrange for the prior involvement procedure to be initiated".⁵⁵² In addition, the CJEU should have the power to examine the compatibility of EU rules with the internal obligations before this will be done by an external court.⁵⁵³

In the same opinion, the CJEU affirmed the necessity to include in the international agreement in question, a prior involvement procedure, that will give the CJEU the option to verify any proceeding before the ECtHR, whether or not the CJEU has already decided on the question.⁵⁵⁴ Moreover, the CJEU should be able to examine the compatibility of EU rules with international law before this to be done by another court. The problem is that, according to Article 3 of the accession agreement to the ECHR, it has been established that the CJEU could judge only on the validity of secondary law, and the interpretation of primary law and so, not on the interpretation of the secondary law.⁵⁵⁵ Consequently, according to EU judges, there is a violation of the exclusive competence of the European Union.⁵⁵⁶

These limits may be effective not only in the relationship between the CJEU and the ECHR.⁵⁵⁷ For this reason, scholars have cautioned that the CJEU could prevent investor-state dispute settlement or require specific dispute settlement features under future EU Agreements.⁵⁵⁸

The Commission, deciding to exclude the domestic law from the applicable law in the Proposal on the TTIP, CETA and the Agreement with Vietnam has

⁵⁵² Opinion 2/13 para. 242.

⁵⁵³ Opinion 2/13 para. 242.

⁵⁵⁴ Opinion 2/13 para. 241.

⁵⁵⁵ Opinion 2/13 para. 242-243.

⁵⁵⁶ Opinion 2/13 para. 242-243.

⁵⁵⁷ D. GALLO, F. G. NICOLA *op.cit.*

⁵⁵⁸ S. SCHILL, *The Proposed TTIP Tribunal and the Court of Justice: What Limits to Investor-State Dispute Settlement under EU Constitutional Law?* *op.cit.*

thought to avoid the aforementioned issue of the principle of the autonomy of the EU law and the monopoly of the ECJ.⁵⁵⁹

However, it would be difficult for the tribunals established in the FTAs to not face the EU law and its interpretation.⁵⁶⁰

Moreover, even if the tribunals would have a specific competence, it will be *binding between the disputing parties* and this could affect different areas of the EU internal market, the EU competition law and other sectors of the commerce.⁵⁶¹

Are there any solutions that would ensure the institution of system external to EU order, but consistent with the autonomy of EU principle of EU? Gallo proposes four solutions that deserve to be analyzed.

The first solution can be found in article 267 of the TFEU on preliminary rulings. In this case, where a national court is faced with a question concerning the interpretation of the Treaties or the validity and interpretation of acts, it will request the ECJ to give a ruling. Even considering that the Member States will agree on this solution, the problem could be whether or not an international tribunal can be considered a court of a Member State. The ECJ has excluded that this qualification can be attributed to commercial arbitration, since the relationship concerns two private parties.⁵⁶² However, a tribunal under the ISDS or the ICS cannot be

⁵⁵⁹ D. GALLO, *op.cit.*

⁵⁶⁰ H. LENK, *Investor-state arbitration under TTIP. Resolving investment disputes in an (autonomous) EU legal order*, SIEPS 2015:2, available at http://www.sieps.se/sites/default/files/Sieps%202015_2%20web.pdf.

⁵⁶¹ The Proposal, art. 30; CETA art. 8.41; Agreement with Vietnam art.31.

⁵⁶² Cfr. *Nordsee Deutsche Hochseefischerei GmbH*, del 23 marzo 1982, causa 102/81, ECLI:EU:C:1982:107. See S. Hindelang, *Circumventing Primacy of EU Law and the CJEU's Judicial Monopoly by Resorting to Dispute Resolution Mechanisms Provided for in Inter-se Treaties? The Case of Intra-EU Investment Arbitration*, in *Legal Issues of Economic Integration*, 2012, p. 179 ff.

considered as a judicial organ of a Member State and consequently the article 267 TFEU should be amended.⁵⁶³

The second solution could be to include in the FTAs a *prior involvement procedure*, consistent with Opinion 2/13 of the ECJ and where, not only the primary law, but also secondary law can be interpreted by the judges.

The third solution is represented by the system established by the European Economic Area, containing norms, annexes and protocols finalized to prevent conflicts with EU law. For instance, it provides a mechanism of continuous exchange of information between the organs of the EFTA (*European Free Trade Association*), the institutions of the EEA and the EU.⁵⁶⁴

On the basis of these rules, it could be possible to establish, in the FTAs, an *ex ante* intervention of the Commission before the tribunals competent to solve the controversies on the investments as *amicus curiae*.

The fourth solution comes from a provision contained in the Proposal on the TTIP, in CETA and in the Agreement with Vietnam, where it is written that the *Committee*, the *Committee on Services and Establishment* with *CETA Joint Committee*, and the *Trade Committee*, can issue binding decisions for the tribunals in order to interpret the provisions of the agreement on the protection of investments, on the solution of controversies, and on the Investment Court System, if serious concerns arise.⁵⁶⁵ The provision could be used in the EU by the Commission in order to give an authentic interpretation of the provision that are inconsistent with the EU law. This important system will not solve the issue, since

⁵⁶³ See M. BURGSTALLER, *op. cit.*, p. 217 e pp. 219-220; *contra* JURGEN BASEDOW, *EU Law in International Arbitration: Referrals to the European Court of Justice*, in *Journal of International Arbitration*, 2015, p 378 ff.

⁵⁶⁴ See D. GALLO, *I rapporti tra Corte EFTA e Corte CE nell'ambito del processo di 'cross-fertilization' tra le due giurisprudenze*, in *Il Diritto dell'Unione europea*, 2007, p. 152 ff.

⁵⁶⁵ TTIP, Article 13, par. 5; CETA, Article 8.31, par. 3; Agreement with Vietnam, Article 16, par. 4.

it has a general character and it is pro future, not linked to the specific controversies.

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In any case, it will be important to engage with the CJEU in order to convince the judges that investor-state dispute settlement does not represent a threat to the Court's role as the constitutional court of the UE because of two main reasons: the investment treaty tribunals have a limited role in dealing with individual investor-state relations and because of their interest to solve the arising disputes.⁵⁶⁷

⁵⁶⁶ D. GALLO, *op.cit.*

⁵⁶⁷ S. SCHILL, *Luxemburg Limits for Investor-State Dispute Settlement Dispute Under Future Eu Agreements in EU and Investment Agreements*, Zurich, 2013, p.54.

CONCLUSIONS

Investor-state arbitration in the last 50 years has acquired a fundamental role in the resolution of controversies, especially because of its peculiar features that makes it a singular case in international law: the possibility for a private investor to challenge a sovereign State. For this reason, it very important to define when the State still maintains a right to regulate. Consequently, the investment agreements have to provide a proper basis for protecting the inherent right of states to regulate in the public interest. However, this does not mean that no disciplines would be available to protect against discriminatory or abusive uses of government power.⁵⁶⁸

Investment arbitration has been subject to more debates after the amendment of the Lisbon Treaty that extended the common commercial policy of the EU to foreign investment. Even if the EU's competence in the investment area is still not completely clear, the EU started to negotiate and, in some cases, it has concluded investments agreements under the aforementioned competence.

The relationship between the EU law and investor-state arbitration is one of the main issues to clarify, as the relationship between the investment tribunal, under the ISDS clause or the ICS, and the CJEU.

In particular, the new approach of the EU to create an Permanent Investment Court represents an evolution in investor-state arbitration and a possible passage from an arbitral system to a jurisdictional one. However, a peculiarity of the investment arbitration remains: only the investor can bring the suit, no state can start a case.⁵⁶⁹

The new approach will be considered as a real revolution in investor-state arbitration if some important signals arrive. Firstly, the acceptance of the US

⁵⁶⁸ H. MANN, *The Right of States to Regulate and International Investment Law*, Geneva, 2002, p. 6.

⁵⁶⁹ D. GALLO, *op.cit.*

Government of the Proposal of the TTIP and the entry into force of the CETA and the Agreement with Vietnam, secondly how the CJEU will deal with the arbitration provisions when it will have to judge their legitimacy, and finally if a multilateral system of solution will ever enter into force.⁵⁷⁰

The creation of an Investment Permanent Court could resolve the perceptions of bias from some scholars that believe that private arbitrators cannot resolve public law issues, because they are not independent and impartial. Critics also believe that investment arbitrators are more likely to adopt an expansive approach on issues of jurisdiction because of their financial interests. Another issue is that ad hoc appointment of arbitrators is an incentive for arbitrators to favor the investors, because they are the only able to invoke the use of the investment arbitration system. Other critics believe that such courts would better serve the interests of States because they can in part control the decision-maker panel.⁵⁷¹ Another important benefit deriving from the establishment of a permanent international investment court could be the consistency of rulings. In fact, tenured judges would be more likely to consider themselves bound by precedent.⁵⁷²

With the exclusion of the domestic law of the Contracting Parties in the Proposal on the TTIP, the CETA and the Agreement with Vietnam from the applicable law, the Commission believed to have solved the problem of the autonomy of EU law and the interpretation monopoly of the CJEU. For this reason, in these treaties, there is no prior involvement procedure of the CJEU. However, the introduction of the procedure is preferred because the tribunals will be naturally invested to interpret and apply the EU law, and the introduction of the

⁵⁷⁰ *Id.*

⁵⁷¹ C. A. ROGERS, *The Politics of International Investment Arbitrators* in *Penn State Law Journal* 2013, p. 248 ff.

⁵⁷² *International investment dispute settlement: from ad hoc arbitration to a permanent court*, in *Advisory Council on International Affairs*, 2015 available at <http://aiv-advies.nl/84x>.

aforementioned procedure would represent the best instrument to ensure conformity with EU law.⁵⁷³

In conclusion, the investor-state adjudication in the EU context presents on one hand, broad concerns and doubts, and on the other interesting and revolutionary proposals, all of them still to be clarified. For this reason, the Opinion of the ECJ on the investment chapter of the Agreement with Singapore will be pivotal to understand how the matter will be addressed in the future and whether or not the EU Commission shall change its position.

⁵⁷³ S. SCHILL, *Editorial*, cit., p. 386, “were the CJEU to demand such a prerogative for itself, it would also need to be granted to the constitutional or supreme courts of the EU’s co-contracting parties”; D. GALLO, *op.cit.*

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