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The Dawn of a New BIT Generation? – The New European Investment Policy

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In July this year, the European Commission published its communication "Towards a comprehensive European international investment policy" (COM(2010) 343 final) and a draft Regulation "establishing transitional arrangements for bilateral investment agreements between Member States and third countries" (2010/0197 (COD)). This initiative is based on the still controversial change brought about by the Lisbon Treaty, by which the Member States included "foreign direct investments" in the Common Commercial Policy (Article 207 TFEU) and thus made it an exclusive competence of the European Union. The Commission is now claiming this new exclusive competence for the Union and seeks to develop a new European policy on foreign investments. There is still some discussion about the exact scope of this new Union competence (i.e. around the definition of "foreign direct investments") but it seems quite clear that this new competence will at least partially cover numerous matters currently treated in the over 1,200 BITs in force between EU member states and third countries. And it is clear that the European Parliament will have – and already has – an increased say in the development of this new European investment policy, which will inevitably lead to an increased politicization of the discussion regarding investment treaty arbitration.

The new exclusive EU competence means that in the medium and long run the existing member state BITs will be successively replaced by European BITs or investment chapters in FTAs concluded by the EU with third countries (on the latter see Roger Alford's entry). The EU Commission's communication provides a vague sketch of what the EU's policy in this respect may look like. What is more acute is the transitional period: what happens with the existing BITs and investment arbitrations in the meanwhile? These questions are addressed in the Commission's draft Regulation. (For a more in-depth analysis of the Commission's proposals see the LSE lead study commissioned by the European Parliament available here).

In a nutshell, the Commission proposes a "grandfathering rule" that would bring the existing BITs in conformity with the exclusivity of the new EU competence (Article 2(1) TFEU) by providing for an automatic authorisation for member states to maintain in force their BITs with third countries (NB: not intra-EU BITs which the Commission considers to be superseded by EU law, see Christophe von Krause's entry) under the condition of notifying them to the Commission. While the authorisation would stem from Parliament and the Council, the powers to withdraw the authorisation for a BIT would be with the Commission on the basis of the following grounds:
• incompatibility with EU Law (on this see the recent ECJ decision on the problematic capital

transfer provisions in Austrian, Swedish and Finnish BITs C-205/06, 249/06 and C-118/07)
• overlap with provisions of a EU negotiated instrument with the third country (such as the FTAs with Chile or Corea);
• incompatibility with the new EU policy on investment that is to be developed and implemented by the Union's institutions;
• if the Council does not act for a year on the Commission's request for a mandate for negotiating an EU instrument that would substitute member state BITs.

While the first two grounds are unproblematic (and the second rather redundant because of the first), the third and fourth ground have been subject to criticism and objections. How is an EU policy actually determined so as to serve as a benchmark for allowing legal action against a member state BIT? And why should the Commission be able to punish the member states for not playing ball by sacking their BITs? As suggested in the report – and now picked up by the *Rapporteur* in the Parliamentary Committee – the former can be addressed rather by providing a narrow interpretative guideline (see below). And as regards the latter, and as highlighted in detail in the LSE report, there are probably good and legitimate reasons for giving the Commission some leverage against the member states to overcome their reluctance to sacrifice their BITs. Otherwise, the Union's exclusive competence would risk *de facto* to degenerate to a merely concurrent competence and thus to dead letter. The Commission, who is the guardian of the Treaties and of the Union's interests (Article 17(1) TEU), is obliged to propose a procedural framework that will guarantee the efficient development of the Union's policies and safeguard its exclusive competence against erosion.

Following the hearing in the European Parliament's International Trade Commission (INTA) on 9 November, the INTA *Rapporteur*, the Swedish Green MEP Carl Schlyter, has presented his draft Report which contains a number of important amendments to the Commission's draft regulation on the transitional arrangements for the member state BITs, see here (click on PE452.807, then on pdf). This draft report introduces yet another major challenge to the Member States. It proposes to include a "sunset" clause that would limit the Union's provisional authorisation for the existing BITs of EU member states with third countries (NB: not intra-EU) to a maximum of 13 years (8 years, extendable by another 5 years). Such a sunset provision would mean that all member states would be required to terminate their BITs, which would mean the end of more or less half of the world's BITs by the end of that period. This suggestion is likely to cause much uproar in the practitioner community and in the member state governments, who will probably try to get this proposal struck down already in the INTA itself.

What may appear as a radical attempt to liquidate the existing BIT generation quicker than proposed by the Commission is, however, not all that irrational in terms of legal certainty. After all, virtually all the BITs in question contain termination clauses that provide for continuing protection for an additional 20 years after the termination. There is no doubt that this extended protection will remain in force under international law irrespective of any withdrawal of authorisation by the EU. This means that the current system of investment protection for investments already made and those made within the next 13 years will continue to be effective at least until the year 2043 (in the most unlikely event that the draft Regulation was adopted this year). This sunset horizon of over 30 year should exceed the projections and the respective need for legal certainty of most (prudent) investors even in large infrastructure or oil & gas projects.

A totally different question is whether, in practical terms, the Commission will be capable not only to review the existing 1,200 BITs in the next (after the suggested amendment now only) four years but, moreover, substitute them by negotiating some 180 new treaties within the next 13 years. This would certainly be quite a herculean effort. But the *Rapporteur*'s understanding is apparently that things will only move if there is sufficient pressure to press forward. In any case, the operation of the termination clauses in the BITs would again allow for a much larger time frame. One would not need to worry too much about investors finding them standing in the rain without any umbrella (that is, even ignoring the debate about whether prudent investors actually require such an umbrella in the first place for their adventures).

As regards more detail, the *Rapporteur* followed the LSE study on the need to have some specifications for defining the EU's policies the incompatibility with which would allow the Commission to withdraw the authorisation for a BIT. Following the lines of the ECJ's PFOS decision (C-246/07 ¶¶ 76 et seq.), the Report refers to policies "as specified in individual or general mandates to open or to conclude negotiations with third countries or other acts or concerted practices of the Union's institutions in the field of the common commercial policy". Furthermore, the amendment would contain a reference to the general principles of the Treaties, which refer, inter alia, to human rights, equality, sustainable development, free and fair trade and the eradication of poverty. Again, this reference will, no doubt, be coined as a dangerous heavy politicization of investment treaty law and an inacceptable reflection of the Rapporteurs political colours. It has to be born in mind, however, that the European Union's explicit commitment to these values is found in the Treaties themselves and goes hand in hand with its institutions' obligation to promote them also in their dealings with third countries (Article 3.5 TEU). This politicization is thus not much more than the inevitable consequence of the transfer of powers to the EU for foreign investments and will be much more accentuated by the necessary involvement of the European Parliament in the definition of the European commercial common policy.

For the rest, the Report's amendments attempt to streamline the language of the Commission draft and to emphasize the need for the Commission to be able to make the Union's interest heard before investment arbitrations. Worth noting in this respect is that the report suggests introducing a new ground for the withdrawal of authorisation for a BIT if its dispute resolution provision prove to be an obstacle to the EU Commission's participation, at least as *amicus curiae*, in arbitrations brought against a member state. Again, this is an amendment which is likely to cause protest since it will put much pressure on arbitral tribunals to think twice whether they want to deny the Commission *amicus curiae* status. However, the experience with the Commission's intervention seems to have been a rather constructive one, so there does not seem to be much need to worry on this front.

What does this development mean for the future of investment arbitration? First of all, we are so far only talking about proposals – which can only come into force if accepted by the majority of member states in the Council. Given many member states' stern opposition in this matter, the next months will be dominated by their attempts to persuade MEP's of other colours that the *Rapporteur* to obtain changes that would shield their BITs against EU interference and extend their life line of their BITs. Their fundamental position is that BITs must remain in force until effectively substituted by EU instruments. This position, however, is difficult to sustain. On one hand, as put radically by one national policy advisor in a discussion at the London School of Economics on 10 November 2010 (see here), the member states are conscious that most ("99%") of their BITs are to some degree incompatible with EU law. On the other hand, the member states themselves agreed with the Lisbon Treaty that the matter of regulating and thus also protecting foreign direct investments is of the exclusive competence of the Union. This means that the Commission needs to have a reasonable margin of manoeuvre to develop and implement the Union's policies, let alone the (already existing) power to force member states to bring their legislations and treaties in line with EU law (as shown by the ECJ's decisions against Austria, Sweden and Finland).

It therefore seems rather likely that the way forward will be tough negotiations on the basis of the text that is presently on the table. As in any difficult negotiation, all sides will have – and can be expected to have anticipated – to make some concessions. In the alternative, i.e. if the Council were to refuse any procedural framework more or less along the lines proposed by the Commission, the latter will be forced to take a much more aggressive approach, which would be the use of the infringement procedure and litigation over the member state's obligation to cooperate. This will not help the general objective of preserving legal certainty – a goal that all stakeholders claim to be committed to. What is certain is that the Commission will press forward in this matter; that Parliament will demand more participation in the process; and that the member states will have to accept that the days of their BITs are numbered, however generously… Irrespective of what the sunset will eventually look like, we can probably expect the dawn of a new generation of BITs under European lead rather sooner than later.

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