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The External Dimension of EU Investment Law: Jurisdictional Clashes and Transformative Adjudication

Daniele Gallo* Fernanda G. Nicola†

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Abstract

EU trade and investment policy is in flux. The rate at which the global trade and investment architecture is evolving through the mega-regional Free Trade Agreements ("FTAs") is unprecedented. In this context, we explain how European lawyers and trade negotiators are addressing the newly acquired investment competence, while at the same time reforming investment arbitration and proposing new systems of dispute resolution at the international level. EU trade negotiators have put forward transformative proposals for investment chapters in their FTAs to safeguard, above all, the autonomy of the EU legal order in its relationship with international arbitration law. By mapping the clash between the investor-State adjudication regime and the EU legal order, we identify the possible legal tools needed to overcome them. Moreover, while supporting the new EU judicial architecture and its procedural rules through an Investment Court System ("ICS"), rather than traditional Investor-State Dispute Settlement ("ISDS") clauses, we propose greater engagement with State-to-State arbitration and further substantive reforms for a truly transformative adjudication system addressing global inequalities created by the current investment regime.

KEYWORDS: EU, Trade, Investment, Free Trade Agreements, Investment Arbitration, Investor-State Dispute Settlement

ARTICLE

THE EXTERNAL DIMENSION OF EU INVESTMENT LAW: JURISDICTIONAL CLASHES AND TRANSFORMATIVE ADJUDICATION

Daniele Gallo[1] *and Fernanda G. Nicola*[2]

ABSTRACT

EU trade and investment policy is in flux. The rate at which the global trade and investment architecture is evolving through the mega-regional Free Trade Agreements ("FTAs") is unprecedented. In this context, we explain how European lawyers and trade negotiators are addressing the newly acquired investment competence, while at the same time reforming investment arbitration and proposing new systems of dispute resolution at the international level. EU trade negotiators have put forward transformative proposals for investment chapters in their FTAs to safeguard, above all, the autonomy of the EU legal order in its relationship with international arbitration law. By mapping the clash between the investor-State adjudication regime and the EU legal order, we identify the possible legal tools needed to overcome them. Moreover, while supporting the new EU judicial architecture and its procedural rules through an Investment Court System ("ICS"), rather than traditional Investor-State Dispute

1. Author of Sections I.A-B, II.B and III.A. Senior Lecturer/Associate Professor of International and EU Law, Law Department, Luiss University, Rome, Italy. The author is grateful to Prof. Andrea Giardina for his critical suggestions. Acknowledgments go to Dr. Filippo Fontanelli, Ms. Maria Laura Marceddu, and Dr. Michele Potestà for their valuable comments on an earlier draft. Prof. Gallo served as legal advisor on the ISDS clause in the TTIP for the Italian Ministry for Economic Development and the Italian Trade Agency. The views and opinions expressed in this article are those of the author and do not purport to reflect the official policy or position of the Italian Government.

2. Author of Introduction, Sections II.A and III.B, and Conclusion. Professor of Law at Washington College of Law, American University; Director of the Program on International Organizations Law and Diplomacy. I have presented this paper at American Association of Law Schools, EU law section meeting in New York City in January 2015, at Boston University in 2016 and at Carlos III in Madrid in 2016, where I have received precious comments. I am indebted for their insights to Duncan Kennedy, Daniela Caruso, Padideh Ala'i, Aluisio De Lima-Campos, Lance Compa, Brishen Rogers and to Megan Glaub for her research assistance. All errors are mine only.

Settlement ("ISDS") clauses, we propose greater engagement with State-to-State arbitration and further substantive reforms for a truly transformative adjudication system addressing global inequalities created by the current investment regime.

INTRODUCTION

In delimiting the EU's new competence in the field of direct investments under Article 207(1) of the Treaty on the Functioning of the European Union ("TFEU"), this provision, read together with Article 3(1)(e) TFEU, has left some important gaps in demarcating the scope of investment protection rules as part of the EU's common commercial policy. While the EU has acquired a new power and is finally "catching up" with the regime of bilateral investment treaties ("BITs"), the Commission is negotiating and concluding new mega-regional Free Trade Agreements ("FTAs"), such as the Transatlantic Trade and Investment Partnership ("TTIP"), the EU-Singapore and EU-Vietnam bilateral agreements and the newly released Comprehensive Economic and Trade Agreement with Canada ("CETA 2016").[3] Because of the political relevance of TTIP and the public consultation launched by the Commission on Investor State

3. Pending the publishing of this article, the European Commission and the Canadian government have agreed to include a new approach on investment protection and investment dispute settlement in the CETA, which almost entirely implements the one put forward by the Commission in its Proposal of 21 November 2015 for Investment Protection and Resolution of Investment Disputes Proposal in the TTIP. *See* Chapter II, Transatlantic Trade and Investment Partnership, E.U.-U.S. (unratified as of Aug. 2016), available at http://trade.ec.europa.eu/doclib/docs/2015/november/tradoc_153955.pdf [hereinafter 2015 TTIP Proposal]. Following the legal revision of the text by the Commission, the CETA was made public on February 29, 2016. *See* Comprehensive Economic and Trade Agreement, E.U.-Can. (unratified as of Aug. 2016), available at http://ec.europa.eu/trade/policy/in-focus/ceta/index_it.htm [hereinafter CETA]. A few weeks before, on February 1st, the text of the FTA with Vietnam, as it had been negotiated by the Parties – which content may change following the legal revision by the Commission – was finalized. *See* EU-Vietnam Trade Agreement, E.U.-Viet. (unratified as of Aug. 2016), available at http://ec.europa.eu/trade/policy/countries-and-regions/countries/vietnam/ [hereinafter EU-Viet. FTA]. This agreement, like the CETA, has been shaped on the 2015 TTIP Proposal. The authors took this evolution into account, as far as possible, which touches upon several issues at the core of this article, including: the establishment of a permanent investment tribunal and of an appeal system; the future institution of a permanent multilateral investment court; and the exclusion of EU law from the jurisdiction of the tribunals.

Dispute Settlement ("ISDS") on March 27 2014 – which results have been published on January 13 2015[4] – the regime of investment arbitration has sparked public interest questions of judicial accountability, transparency and democracy.

As Sophie Meunier has shown, the long-awaited transfer of competence over investment law, brought by the Lisbon Treaty, from the Member States to the EU – which enables the Union to negotiate on their behalf in FTAs containing investment chapters –, has happened by "stealth," meaning that the tense political debate prior to the shift of competence left open important questions on implementation.[5] For example, the German Constitutional Court expressed caution on including such a broad investment protection in competence, arguing instead that it should be confined to investment as a controlling power over an enterprise.[6] The EU has not yet overcome the resistance of its Member States committed to maintaining their BITs and to the protection of property according to their different constitutional traditions.[7]

Moreover, it remains to be seen what the CJEU will state in its Opinion 2/15 on the FTA with Singapore, as it was requested by the Commission, in accordance with Article 218(11) TFEU, to rule on the delimitation of competences between the EU and Member States in the field of external investment law. In particular, the Commission asked the Court whether the Union has the requisite competence to

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4. COMMISSION STAFF WORKING DOCUMENT, REPORT, ONLINE PUBLIC CONSULTATION ON INVESTMENT PROTECTION AND INVESTOR-TO-STATE DISPUTE SETTLEMENT (ISDS) IN THE TRANSATLANTIC TRADE AND INVESTMENT PARTNERSHIP AGREEMENT (Jan. 13, 2015), http://trade.ec.europa.eu/doclib/docs/2015/january/tradoc_153044.pdf [hereinafter TTIP Consultation].

5. *See* Sophie Meunier, Integration By Stealth: How The European Union Gained Competence Over Foreign Direct Investment (Dec. 23, 2013) (paper for the 7th Annual Conference of the Political Economy of International Organizations, January 16-18, 2014, Princeton University), http://www.uni-heidelberg.de/md/awi/peio/meunier_05.09.2013.pdf, at 2.

6. *See* Meunier, *supra* note 5, at 12. *See* August Reinisch, *The EU on the Investment Path*, (unpublished draft paper), available at http://law.scu.edu/wp-content/uploads/investment/Reinisch-EU-Investment-Law-Quo-Vadis-26-01-2013.pdf at n.7 (citing the German Constitutional Court, 2 BvE 2/08, 30 June 2009, ¶ 379).

7. *See* Presentation by Joakim Reiter, Deputy Secretary General UNCTAD at the XXIV Meeting of the Trade Policy Experts Group (Mar. 15, 2016) (explaining that the difference between Sweden and Germany vis-a-vis to BITs lies also in the different protection of property that can be found in the Swedish constitution but not in the German one) (notes from the presentation on file with author).

sign and conclude the agreement without the involvement of the Member States.[8]

The political tensions and ambiguities left in the Treaty of Lisbon over the external EU investment competence have created new challenges but also opened new avenues to reform international investment regimes and their dispute mechanism. Initially, to avoid the clashes between intra-EU BITs, the Commission launched a series of infringement proceedings against Sweden, Austria, and Finland, obliging the Member States to eliminate incompatibilities between their international and EU law obligations in favor of the latter.[9] Throughout the TTIP negotiations that began in 2013, and the most recent CETA 2016 and the EU-Vietnam FTA, the EU has demonstrated great transformative potential in setting aside old ISDS clauses enforced by private arbitrators while establishing permanent tribunals of first instance and appeal and aiming to consolidate a multilateral investment Court system.

This transformative process began when the Commission realized that, at least in the EU, the inclusion of ISDS clauses remained one of the main "nails in the coffin" the TTIP negotiations brought up, not only in international legal circles but also amongst the EU and its Member States, across academia, and in civil society. Of particular importance in the EU context are the aforementioned results of the Commission's public consultation launched on March 2014, followed by the Commission's Concept Paper published in May 2015,[10] the European Parliament's resolution of July 8, 2015[11] and the

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8. More specifically the Commission asked the CJEU the following questions: which provisions of the agreement fall within the Union's exclusive competence?; Which provisions of the agreement fall within the Union's shared competence?; Is there any provision of the agreement that falls within the exclusive competence of the Member States? *See* Request for an Opinion Submitted by the European Commission Pursuant to Article 218(11) TFEU, (Opinion 2/5), available at http://curia.europa.eu/juris/document/document.jsf?text=&docid=170868&pageIndex=0&doclang=EN&mode=lst&dir=&occ=first&part=1&cid=224938.

9. *See* Nikos Lavranos, *Member States' Bilateral Investment Treaties (BITs): Lost in Transition?*, *in* HAGUE YEARBOOK OF INTERNATIONAL LAW, 281-82 (Nikos Lavranos et al. eds., 2011).

10. *See* Commission Concept Paper: *Investment in TTIP and beyond – the path to reform* (May 15, 2015) available at http://trade.ec.europa.eu/doclib/docs/2015/may/tradoc_153408.PDF last visited August 10, 2016 (hereinafter Commission Concept Paper).

11. The European Parliament, in its Resolution of July 8, 2015, has not rejected the inclusion *ex se* of the ISDS clause in the TTIP. *See* Julie Levy-Abegnoli, *TTIP: EU Commission Unveils Replacement for Controversial ISDS*, PARLIAMENT MAGAZINE (Sept. 16, 2015), https://www.theparliamentmagazine.eu/articles/news/ttip-eu-commission-unveils-

Commission's 2015 TTIP Proposal.[12] ISDS clauses were indeed an incredibly controversial topic in the media and feared by civil society in Europe, causing the Commission a huge setback in negotiations. After a large stakeholder consultation encountered over 150,000 responses, the Commission elaborated a preliminary response attempting to highlight the two major sites of the controversies around investor-State arbitration and the right to regulate.[13] While the negotiators have argued that these responses would be used sparingly, an UNCTAD report has shown that ISDS clauses do not necessarily positively impact investment flows[14] and lawyers have argued over the limits of domestic courts and long awaited an international investment court.[15] Many host governments see these clauses as an obstacle to environmental and social policies that will be challenged in front of arbitrators rather than courts. On the other hand, investors favor ISDS clauses for fear that host governments will adopt legislation in conflict with investment or trade treaty obligations.

The position of the Commission resulted in a compromise between these two polar positions in its Report on the consultation on ISDS in TTIP. Here the Commission began signaling its initial criticism to the traditional ISDS model. For instance, the Commission explained how for small and medium-size enterprises the costs of ISDS mechanisms remain too high, especially with the application of the "loser pay" principle.[16] Commissioner Malmström has explained that there are already some 1,400 EU agreements (another 3,000 globally) in existence since the 1950s and that BITs are overall a German invention.[17] However, in response to the criticisms on ISDS, in December 2015 David O'Sullivan, EU Ambassador to the United States, addressed the ISDS challenge: "TTIP will allow us to improve

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replacement-controversial-isds?utm_medium=email&utm_campaign=Daily+Parliament+Magazine+Round-Up&utm_content=Daily+Parliament+Magazine+Round-Up+CID_7aaab1fa16cc22afa94c82df5cfb75e5&utm_source=Email+newsletters&utm_term=TTIP+EU+Commission+unveils+replacement+for+controversial+ISDS.

12. *See* Chapter II, Transatlantic Trade and Investment Partnership, *supra* note 3.

13. *See* TTIP Consultation, *supra* note 4, at 3.

14. *See* TRADE AND INVESTMENT REPORT 2014, UNCTAD (2014), http://unctad.org/en/PublicationsLibrary/tdr2014_en.pdf.

15. *See* GUS VAN HARTEN, INVESTMENT TREATY ARBITRATION AND PUBLIC LAW 180 (2007).

16. *See* TTIP Consultation, *supra* note 4, at 16, 22 (discussing various business NGOs opposed to the principle).

17. Cecilia Malmström, EU Trade Comm'r, Eur. Comm'n, Speech at the Open Europe & Friedrich Naumann Stiftung: Debating TTIP, (Dec. 11, 2014).

them. We must acknowledge both their weaknesses (cases against tobacco plain packaging legislation being an example of 'ISDS gone wrong') and their benefits (preventing expropriation, for example, with its consequent job losses)."[18] The changing attitude of the Commission towards the traditional ISDS model was fueled by Phillip Morris' challenge against Australian packaging regulations, and the subsequent tobacco carve-out in order to avoid potential investors' claims of action in this sector for the Trans-Pacific Partnership Agreement (TPP) between the US and 11 other Asia-Pacific nations.

In 2015, however, the Commission went further than just introducing carve-out clauses with the TTIP's transformative investment proposal, moving away from the traditional ISDS model of private arbitrators to create instead an Investment Court System, constituted ("ICS") by permanent tribunals. This was in response to the criticisms expressed by the European Parliament, civil society, some Member States and their national parliaments alike distrusting the current international arbitration regimes for lack of democratic accountability, consistency, openness and independence. Throughout its TTIP negotiation position, the Commission progressively sought to address both procedural and substantive criticism: starting from the fact that international arbitrators ought to be more independent and the system more open, it launched the proposal of permanent tribunals with nominated permanent judges bound to ethical rules to prevent conflicts of interest. In response to the lack of consistency and the broad discretion of arbitrators in the application of general principles (such as the right to regulate and the fair and equitable treatment ("FET") standard) the Commission drafted comprehensive tests departing from notions of equity in customary international law ("CIL").

The establishment of permanent investment tribunals, of first and second instance, is a prominent innovation of the latest reiteration of the FTA with Vietnam as well as of the CETA 2016, which both further engage in the creation of a multilateral court system replacing

18. Letter by David O'Sullivan, Ambassador of the European Union to the United States, Responding to TTIP Criticisms (Dec. 9, 2015), http://www.euintheus.org/press-media/letter-by-david-osullivan-responding-to-ttip-criticisms/.

the investment tribunals.[19] As to the CETA 2016, a permanent Tribunal, with fifteen appointed members in equal numbers by the EU, Canada, and third parties for terms of five years, will also have high ethical standards about their independence and possible conflicts of interest.[20] In following the approach of TTIP, CETA 2016 ensures consistency in adjudication with the creation of a permanent "Appellate Tribunal" that will uphold, modify or reverse the Tribunal's awards and will be constituted by a decision of the CETA Joint Committee.[21] The EU-Vietnam FTA establishes as well a Tribunal of first instance of nine members[22] and an "Appeal Tribunal," constituted by six judges once again appointed in equal number by the EU, Vietnam and third countries.[23] While CETA leaves it to the Joint Committee to decide the procedures of the Appellate Tribunal, the EU-Vietnam FTA, like the TTIP 2015 Proposal, specifies judges' salaries, appellate procedures and goes as far as stating that the Appeal Tribunal should decide by consensus or anonymous majority voting.[24] However, the long-term goal of both CETA 2016 and EU-Vietnam Tribunals is to transform this bilateral system into a multilateral one that could eventually also incorporate the TTIP tribunals.[25]

This transformative proposal has met lots of resistance, especially amongst US trade circles, in which lawyers have warned against overstating the benefits of a permanent system of investment disputes between States and investors, the unintended consequences of a more "consistent" investment regime with less flexibility, and the costly procedures coinciding with greater accountability in decision-

19. *See* Commission Press Release, CETA: EU and Canada Agree on New Approach on Investment in Trade Agreement, IP/16/399 (Feb. 29, 2016), http://europa.eu/rapid/press-release_IP-16-399_en.htm.

20. *See* CETA, *supra* note 3, arts. 8.27 and 8.30.

21. CETA, *supra* note 3, art. 8.28. For an explanation, see Press Release, CETA: EU and Canada Agree on New Approach on Investment in Trade Agreement (Feb. 29, 2016), http://europa.eu/rapid/press-release_IP-16-399_en.htm.

22. *See* EU-Viet. Free Trade Agreement, Ch. II of Ch. 8, Sect. 3, *supra* note 3, art. 12, ¶ 2; 2015 TTIP Proposal, *supra* note 3, Ch. II, art. 9.

23. *See* EU-Viet. Free Trade Agreement, Ch. II of Ch. 8, Sect. 3, *supra* note 3, art. 13, ¶ 2; 2015 TTIP Proposal, *supra note 3*, Ch. II, art. 10.

24. *See* EU-Viet. Free Trade Agreement, Ch. II. of Ch. 8, Sect. 3, *supra* note 3, art. 13, ¶ 12.

25. *See* CETA, *supra* note 3, art. 8.29; EU-Viet. Free Trade Agreement, Ch. II of Ch. 8, Sect. 3, *supra* note 3, art. 15.

making.[26] When compared to the US and the recent TPP agreement, the EU appears in CETA 2016 and the EU-Vietnam FTA as an equally influential global actor, yet more committed to transformative reforms and greater engagement and responsiveness to its civil society.[27]

However, we argue that the transformative EU proposal stems, above all, from internal constraints such as the need to safeguard the EU legal order and to avoid jurisdictional clashes, as well as the need to reconcile the opposing notions of the right to regulate for public interest, and the fair and equitable treatment of foreign investments.[28] In Section I, we show the rationale for why the EU should remain committed to the inclusion of investor-State adjudication in its FTAs, such as the new ICS – in contrast with old fashioned ISDS clauses. This includes the risk of politicization arising from systems of dispute resolution governed only by diplomatic protection and State-to-State arbitration, as well as from the lack of direct effect of international trade agreements. Section II shows that the Commission has introduced important provisions in its EU-Vietnam FTA and CETA 2016, which aim at preserving the right to regulate for public policies and create a clear and objective test to interpret the FET standard beyond the vague equity principles derived from CIL. Regarding extra-EU agreements, we identify the main challenges for the EU in concluding those agreements while simultaneously respecting the principle of autonomy of the EU legal order above all in order to safeguard the interpretive monopoly of the CJEU. In Section III, we seek to focus on the relation between State-to-State arbitration and investor-State adjudication in order to envisage an effective system of coordination between these two mechanisms. As far as investor-State arbitration is concerned, our reasoning counts for FTAs, such as Singapore, which does not (at least so far) include an ICS, as well as for other agreements, such as the TTIP, should the ICS not be included in the final text (due to the Third Country partner's opposition or, less likely, to a changeover on the part of EU institutions). As it will be shown, most of the analysis may apply also

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26. *See* Caroline Simson, *TTIP's Investment Court System Likely to be Problematic,* LAW360, (Feb. 2016), http://www.law360.com/articles/763889/ttip-s-investment-court-system-likely-to-be-problematic.

27. *See* Fernanda G. Nicola, *The Politicization of Legal Expertise in the TTIP Negotiation*, 78 L. & CONTEMP. PROBS. 175 (2015).

28. *See* George A. Bermann, *Navigating EU Law and the Law of International Arbitration*, 28 ARB. INT'L 397, 443-44 (2012).

to agreements containing ICS provisions. Finally, we address the transformative potential of the permanent investment tribunals in CETA 2016 and the EU-Vietnam FTA from both a procedural and substantive perspective. The ICS demonstrates that the Commission has challenged the *status quo* of the traditional ISDS regime to institutionalize a permanent tribunal. From a procedural perspective we welcome this new investment regime embodying the main criteria of public law adjudication. Yet we question whether in substance the ICS is equipped with necessary tools to engage with global inequalities, sustainable devolvement and human rights violations arising in the current international investment regime in a transformative way.[29]

I. THE RATIONALE FOR KEEPING INVESTOR-STATE ADJUDICATION IN EU FREE TRADE AGREEMENTS

A. Risks of Politicization Arising from State-to-State Arbitration and National Jurisdictions

The rationale for the inclusion of investor-State arbitration in the form of ISDS[30] in the free trade and investment agreements under negotiation or conclusion by the EU[31] lies in the need to ensure impartiality and the de-politicization of disputes.[32] The same holds

29. *See* UNCTAD INVESTMENT REPORT 2015, UNCTAD xi-xii (2015), http://unctad.org/en/PublicationChapters/wir2015ch0_KeyMessage_en.pdf (committing to sustainable development and corporate social responsibility as a tradeoff to property protection).

30. *See generally* UNCTAD WORLD INVESTMENT REPORT 2015, UNCTAD (2015), http://unctad.org/en/PublicationsLibrary/wir2015_en.pdf; ICSID 2015 ANNUAL REPORT, ICSID (2015), https://icsid.worldbank.org/apps/ICSIDWEB/resources/Documents/ICSID_AR15_ENG_CRA-highres.pdf (providing data and statistics on the proliferation of investment dispute settlement systems). *See, e.g.*, ANDREAS LOWENFELD, INTERNATIONAL ECONOMIC LAW 554-57 (2008); August Reinisch, *The Proliferation of International Dispute Settlement Mechanisms, The Threat of Fragmentation vs. the Promise of a More Effective System? Some Reflections From the Perspective of Investment Arbitration*, *in* INTERNATIONAL LAW BETWEEN UNIVERSALISM AND FRAGMENTATION: FESTSCHRIFT IN HONOUR OF GERHARD HAFNER 107-25 (Isabelle Buffard, James Crawford, Alain Pellet, & Stephan Wittich, eds., 2008) (identifying some of the main features of current investment dispute settlement systems).

31. *See* Consolidated Version of the Treaty on the Functioning of the European Union arts. 216-19, 2012 O.J. C 326/47, at 144-47 [hereinafter TFEU].

32. *See* Aron Broches, *The Convention on the Settlement of Investment Disputes between States and Nationals of Other States*, *in* SELECTED ESSAYS: WORLD BANK, ICSID, AND OTHER SUBJECTS OF PUBLIC AND PRIVATE INTERNATIONAL LAW 194-96, 188-239 (1995) (stressing that ICSID itself was conceived as a means of de-politicization). *See also* Ibrahim

true, *mutatis mutandis*, for other systems of investor-State adjudication, such as the ICS included in the 2015 TTIP Proposal, the EU-Vietnam FTA and the CETA 2016. Indeed, if no provision is made for this type of dispute-settlement mechanism,[33] the only avenues available to foreign investors wishing to sue the EU and/or its Member States (and directly enforce their rights), as well as to European investors wishing to sue the host partner State, will be State-to-State arbitration[34] and domestic judicial proceedings.[35] "Domestic" means, as far as the EU is concerned, procedures both before Member States' national courts and the CJEU.[36] In this respect, it is too soon to assess with certainty what the new evolution on the institution of an ICS, currently applied to two EU trade partners (Canada and Vietnam, one developed country, one developing country) may represent for agreements still under negotiation or conclusion. Definitely, if confirmed in the future, it will represent a radical twist that may be effective for the whole EU trade and

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F.I. Shihata, *Towards a Greater Depoliticization of Investment Disputes: The Role of ICSID and MIGA*, 1 ICSID R.—FOREIGN INV. L.J. 1 (1986); Sergio Puig, *Emergence and Dynamism in International Organizations: ICSID, Investor-State Arbitration and International Investment Law*, 44 GEO. J. INT'L L. 531 (2013). *See* Catharine Titi, *Are Investment Tribunals Adjudicating Political Disputes? Some Reflections on the Repoliticization of Investment Disputes and (New) Forms of Diplomatic Protection*, 32 J. INT'L ARB. 261, 262-67 (2015) (giving an historical overview on the Convention, from the standpoint of de-politicization of disputes). *See generally* Kaj Hober, *Does Investment Arbitration Have a Future?*, *in* INTERNATIONAL INVESTMENT LAW: A HANDBOOK 1873-79 (Marc Bungenberg, Jörn Griebel, Stephan Hobe, & August Reinisch eds., 2015) (writing on the future of investor-state arbitration). On the limits of de-politicization see Martins Paparinskis, *The Limits of De-politicization in Contemporary Investor-State Arbitration*, *in* SELECT PROCEEDINGS OF THE EUROPEAN SOCIETY OF INTERNATIONAL LAW 271-84 (James Crawford & Sarah Nouwen eds., 2010).

33. Moreover, while it is true that the rationale for investor-State arbitration lies in the de-politicization of disputes, it is also true that all remedies have some contraindications; for example, the danger of politicization may arise regardless of the system of conflict resolution concerned, including investor-State arbitration.

34. *See Free-trade agreements: A Better Way to Arbitrate*, ECONOMIST (Oct. 11, 2014), http://www.economist.com/news/leaders/21623674-protections-foreign-investors-are-not-horror-critics-claim-they-could-be-improved

(writing as one of the most influential supporters of State-to-State remedies in the context of investment agreements).

35. *See generally* EUROPEAN PARLIAMENT, DRAFT REPORT CONTAINING THE EUROPEAN PARLIAMENT'S RECOMMENDATIONS TO THE COMMISSION ON THE NEGOTIATIONS FOR THE TRANSATLANTIC TRADE AND INVESTMENT PARTNERSHIP (TTIP) (2014) http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//NONSGML+COMPARL+PE-549.135+01+DOC+PDF+V0//EN (reporting in favor of this twofold solution (State-to-State arbitration *and* domestic remedies)).

36. On this point *see infra* Section I.A.2.

investment policy, including the TTIP. The following analysis had been conceived, on the basis of the most relevant literature on investment arbitration, and then carried out, in its core elements, before the finalization of both the CETA 2016 and the EU-Vietnam FTA; yet most of it, although being devoted originally to ISDS mechanisms, applies also to the new ICS and thus includes several references to such evolution throughout this article.

1. State-to-State Arbitration

Regarding State-to-State arbitration, the investor's home State has a discretionary right to protect its nationals by diplomatic means. The State's full discretion concerns the commencement, prosecution and settlement of the claim, as well as the payment of damages,[37] if awarded by the arbitrators.[38] A risk of politicization may thus arise insofar as the State decides whether to initiate a dispute based on the investor's economic and political power (and his ability to persuade and lobby the government in a more or less transparent manner) rather than on the legal soundness of his claim.[39] Diplomatic protection, especially in the case of investment disputes, is apt to create political and legal uncertainty and can be used in an arbitrary fashion; therefore, it may impair the fairness and effectiveness of the

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37. *See* Mavrommatis Palestine Concessions (Greece v. U.K.), Judgment, P.C.I.J. A-2, ICGJ 236 [1924], ¶ 12, (". . . it is an elementary principle of international law that a State. . . [b]y taking up the case of one of its subjects and by resorting to diplomatic action or international judicial proceedings on his behalf . . . is in reality asserting its own rights – its right to ensure, in the person of its subjects, respect for the rules of international law.").

38. *See* Anthea Roberts, *State-to-State Investment Treaty Arbitration: A Hybrid Theory of Interdependent Rights and Shared Interpretive Authority*, 55 HARV. INT'L L. J. 1, 2 (2015). *See generally* Kate Parlett, *Diplomatic Protection and Investment Arbitration*, *in* INTERNATIONAL INVESTMENT LAW AND GENERAL INTERNATIONAL LAW: FROM CLINICAL ISOLATION TO SYSTEMIC INTEGRATION? 211-30 (Rainer Hofmann, & Christian J. Tams eds., 2011); Peter Muchlinski, *The Diplomatic Protection of Foreign Investors: a Tale of Judicial Caution*, *in* INTERNATIONAL INVESTMENT LAW FOR THE 21ST CENTURY: ESSAYS IN HONOUR OF CHRISTOPH SCHREUER, 341-62 (Christina Binder et al. eds., 2009) (writing on diplomatic protection and investment adjudication); Gary Born, *A New Generation of International Adjudication*, 61 DUKE L.J. 775 (2012); Susan D. Franck, *The ICSID Effect? Considering Potential Variations in Arbitration Awards*, 51 VA. J. INT'L L. 825 (2011); Ben Juratowitch, *The Relationship Between Diplomatic Protection and Investment Treaties*, 23 ICSID REV.—FOREIGN INV. L.J. 10 (2008).

39. *See, e.g.,* Christoph Schreuer, *Investment Protection and International Relations*, *in* THE LAW OF INTERNATIONAL RELATIONS—LIBER AMICORUM HANSPETER NEUHOLD 345 (August Reinisch, & Ursula Kriebaum eds., 2007); Christoph Schreuer, *Do We Need Investment Arbitration?*, TRANSNAT'L DISP. MGMT 1 (2014), https://www.transnational-dispute-management.com/article.asp?key=2026.

system concerned. As emphasized by Joseph Weiler, "the bigger the economic stake, the more powerful the multinational," the more likely investors "are to get the ear of a government which will espouse their case."[40]

If State-to-State arbitration is the only dispute resolution system available, the risk of politicization can still also arise because a government may be inclined (or disinclined) to take up the cause of an investor due to the political and economic advantages (or disadvantages) of bringing an international action against another State – that is, due to the nature and importance of the political interests that underpin its relationship with the State hosting the investment. The espousal of a claim often depends on the interests of the State rather than those of the investor, as observed by Michael Reisman when he speaks of "the caprice of sovereign-to-sovereign politics."[41] Moreover, national authorities may put pressure on international arbitrators in order to avoid a "debacle," which could seriously damage the State's international reputation.[42] An additional risk is that once a State-to-State dispute has been initiated, investors will have no control over the proceedings started by their home State, with the ultimate consequence of being left out of the process altogether.[43] Having said this, however, Section III will show that State-to-State arbitration should not be abandoned as such, but rather included in the EU's international agreements along with investor-State adjudication.[44]

2. National Jurisdictions

If domestic judicial proceedings are the only other course of action available besides State-to-State arbitration, investors are forced

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40. Joseph H. H. Weiler, *European Hypocrisy: TTIP and ISDS*, EJILTALK.ORG (Jan. 21, 2015), http://www.ejiltalk.org/european-hypocrisy-ttip-and-isds. *See also* Freya Baetens, *Transatlantic Investment Treaty Protection – A Response to Poulsen, Bonnitcha and Yackee* 9 (Mar. 12, 2015), https://www.ceps.eu/publications/transatlantic-investment-treaty-protection-%E2%80%93-response-poulsen-bonnitcha-and-yackee.

41. *See* Ecuador v. United States, Expert Opinion with Respect to Jurisdiction in the Interstate Arbitration Initiated by Ecuador Against the United States, 20-21, ¶ 37 (Perm. Ct. Arb., 2012).

42. *See* Weiler, *supra* note 40.

43. *See* Armand de Mestral, *Investor-State Arbitration between Developed Democratic Countries*, CIGI 32 (Sept. 2015), https://www.cigionline.org/sites/default/files/isa_paper_series_no.1.pdf.

44. On this point, see *infra* Section III.A.

to bring their claims solely before the courts of the host State.[45] Thus, there is a risk of politicization and partiality because domestic jurisdictions may be induced to rule in favor of the host State in response to national authorities wishing to avoid paying compensation – and transferring State money – to foreign investors. Therefore, a distinction could be made based on the reliability of a national court depending on the country concerned. Indeed, the rationale for investor-State adjudication seems less obvious in the case of agreements between the EU and developed capital-exporting countries than in that of EU agreements with developing countries – which are generally also capital-importing countries.[46] As noted in a statement on investor-State arbitration in the TTIP submitted to the European Commission by a group of academics (in the framework of the public consultation launched on March 27, 2014 and concluded on July 13, 2014, discussed above), it is difficult to argue investors in the US-EU context have reason to worry in either region. Indeed, investor-State arbitration, inserted in international agreements, was traditionally aimed at attracting investments made in developing countries with weak legal and judicial systems. In the case of bilateral agreements between developed and developing countries, there has always been a concern that the courts of a developing country may fail to ensure the same degree of impartiality and fairness as is expected of the judiciary in a developed democracy, thus making it necessary to resort to an arbitral tribunal chosen by the parties and called upon to apply procedural and substantive rules known in advance to both parties.

As to the more problematic question of whether domestic courts alone or with investor-State tribunals should settle disputes arising out of trade and investment agreements between the EU and non-EU developed countries, there seem to be at least three reasons for keeping international adjudication (rather than traditional arbitration) in this case. First, domestic proceedings can be lengthy, taking more time than proceedings before investment tribunals, which contradicts the aim of ensuring the speedy resolution of disputes.[47]

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45. Yet, it might be that a clause on commercial arbitration is included in the contracts negotiated by the investor.

46. However, countries such as China, albeit their status as a capital-exporting country, are still considered developing States.

47. *See* European Federation for Investment Law and Arbitration (EFILA), *A Response to the Criticism against ISDS*, 33 J. INT'L ARB. 1, 28 (2016) (noting that, although the average

Secondly, from the point of view of foreign investors, it is not certain that all of the EU's Member States provide for internal remedies allowing investors to challenge decisions by public authorities. Moreover, as confirmed by a number of reports by international organizations such as the World Economic Forum and documents by EU institutions, not all judiciaries in the EU have been exempt from strong criticism in relation to their quality, independence, and efficiency.[48] As a result, it is not surprising that countries such as the United States greatly support the insertion of investor-State arbitration in their agreements with the EU.[49] As noted in the literature, one may wonder why EU Member States have been reluctant to abandon their BITs with new Member States formerly part of the Communist Bloc if they esteem that their nationals will be granted equal protection under EU law or under the laws of the new Member States.[50] Conversely, from the standpoint of the EU, the omission of an investor-State adjudication system from the agreements with third countries may entail serious consequences as far as countries with weak judicial systems are concerned. For instance, with respect to the TTIP, the UK House of Lords' European Union Committee, in its 14th Report of Session 2013–14, recognized that their inclusion could add vital precedential value in advance of similar agreements with nations like China.[51] An alternative could be to avoid inserting the system only in the agreements with developed, Western democracies. Yet, this approach would be difficult to justify vis-à-vis the developing countries with which the EU has already negotiated agreements containing a provision on investor-State adjudication. In any event, such an asymmetry could lead to dangerous disparities since the judicial organs of the EU and Member States would have jurisdiction over certain foreign investors but not

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BIT arbitration takes three years, this is still faster than what it is needed to exhaust available remedies in many developed national judicial systems).

48. *See* GLOBAL COMPETITIVENESS REPORT 2015-2016, WORLD ECONOMIC FORUM, http://reports.weforum.org/global-competitiveness-report-2015-2016/ (providing data, statistics and rankings on global investment disputes); *see also* EUROPEAN COMMISSION, THE 2015 EU JUSTICE SCOREBOARD (2015), http://ec.europa.eu/justice/effective-justice/files/justice_scoreboard_2015_en.pdf.

49. *See* de Mestral, *supra* note 43, at 7-8 (giving insight on the NAFTA case law).

50. *See id.* at 7.

51. EU Committee Fourteenth Report: The Transatlantic Trade and Investment Partnership, Content of the TTIP, Ch. 3, ¶ 169 (2014), http://www.publications.parliament.uk/pa/ld201314/ldselect/ldeucom/179/17906.htm#a42.

others, with different treatment accorded to private parties on the basis of their country of nationality.

Thirdly, rulings by different Member States' national courts may cause inconsistencies and result in a lack of legal certainty, putting foreign investors at a disadvantage. In this regard, the problem with a system based solely on domestic jurisdictions is that national courts may have different approaches to a number of matters, such as the recognition of the immunity of the host State, the interpretation of the notion of property, the definition of "indirect expropriation" and the scope and extent of compensation, in spite of the obligations arising from customary law and Article 1 of Protocol 1 ECHR.[52] In this perspective, and with respect to the TTIP, the claim that the United States would be willing to rely specifically on internal remedies and conclude an agreement with the EU even without an investor-State adjudication system (as was the case with their agreement with Australia[53]) cannot be accepted *per se* precisely because of the fundamental difference between a bilateral agreement with a third State and an agreement with an international organization (and its members), especially in the light of the problems arising from the existence of a supranational court and the risks connected to the diversity of court decisions among the 28 EU Member States.[54]

B. Lack of Direct Effect of EU Free Trade Agreements

Another important reason why a system of investor-State adjudication seems to be of great importance for EU agreements is that it offers investors remedies that may not otherwise be available, at least under current EU law relating to the status of international agreements in domestic legal systems. This issue can be better understood by looking at the debate on the TTIP that took place amongst the EU Member States, from which emerged that some governments, including that of France, stressed the need to assign domestic (i.e., national and EU) courts a stronger role than the one

52. *See* CHRISTOPH GRABENWARTER, EUROPEAN CONVENTION ON HUMAN RIGHTS: COMMENTARY 359-71 (2014) (analyzing the ECtHR's relevant case law on the provision).

53. *See generally* Austl.–U.S. Free Trade Agreement, May 18, 2004, A.T.S. 1 (AUSFTA).

54. This applies especially with regard to the different level of protection granted to investors.

envisaged in the text of CETA 2014[55] as reported by the Commission in its Concept Paper of May 2015.[56]

1. Role of the CJEU

Typically, domestic courts could enforce jurisdiction mainly through inclusion of either an explicit incentive for investors to bring the matter before national courts or a mandatory rule of prior exhaustion of local remedies in the agreement, according to which individuals can bring a claim before international tribunals upon the condition that they exhausted all domestic avenues of redress. An alternative could be to give investors the right to choose between bringing an action before a domestic court or, by virtue of an investor-State dispute settlement clause, before an international tribunal (the so-called "fork in the road"). A drastic solution would be to exclude investor-State adjudication altogether, where consequently only domestic judges would be competent to settle disputes between the parties to the agreement.[57]

However, such a revaluation of the role of domestic jurisdictions, no matter the intensity, would raise issues with regard to the level of judicial effectiveness ensured by local remedies. Specifically for the EU, the question is whether foreign investors affected by Member States and/or EU measures could *effectively* invoke the provisions of a free trade agreement (1) before the CJEU, in order to challenge the legality of EU acts pursuant to Article 263(4) TFEU,[58] and/or (2) before national jurisdictions, in order to challenge the validity of national law, to obtain an interpretation of EU law under Article 267 TFEU or challenge its validity under the same provision.[59] While there is nothing preventing investors from having

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55. CETA 2014 is the predecessor of CETA 2016, i.e. the agreement finalized by the EU with Canada before the legal revision conducted by the Commission. The 2014 version of CETA is available at http://trade.ec.europa.eu/doclib/docs/2014/september/tradoc_152806.pdf.

56. *See* Commission's Concept Paper, *supra* note 10, para. IV.

57. As opposed to the mere possibility to do so, which is implicitly or explicitly recognized by most BITs and FTAs, including the latest generation of agreements concluded by the EU.

58. *See* TFEU, *supra* note 31, art. 263(4) ("Any natural or legal person may. . . institute proceedings against an act addressed to that person or which is of direct and individual concern to them, and against a regulatory act which is of direct concern to them and does not entail implementing measures.").

59. *See* TFEU, *supra* note 31, art. 267 (". . . the Court of Justice of the European Union shall have jurisdiction to give preliminary rulings concerning: (a) the interpretation of the

recourse to domestic courts *per se*, reflecting on "effectiveness" means assessing whether the internal avenues offered by the MS as well as by the EU would allow non-EU investors to *effectively* enforce their rights. This implies determining whether an investor may exercise his/her rights by relying directly on international law provisions having a direct effect. If so, the individual would be granted (in principle) access to a self-standing judicial remedy. Consequently, the inclusion of an ISDS or ICS clause would not be indispensable for an investor whose home State was a party to the agreement concluded with the EU. If, on the contrary, no such exercise was possible, the investor would have no access to direct effective judicial remedies, with the result that it would be inconvenient for him – in terms of duration and cost of litigation – to bring the treaty-based claim first before a domestic court and then before an international tribunal.

In the absence of a provision of primary or secondary law establishing the types of effects of treaty obligations, it is up for the CJEU to decide on the matter. In its earlier case law, the CJEU, opting for a monist interpretation of the relationship between international law and the EU legal order, allowed private parties to invoke international law provisions that were sufficiently precise and unconditional.[60] However, a brief analysis of the CJEU recent case law on the status of international agreements in the EU legal order is sufficient to show that the Court tends to deny, in concrete terms, the direct effect of the provisions contained in such agreements, thus excluding the possibility for natural and legal persons to invoke them before the CJEU.[61] The Court[62] has confirmed this approach in its

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Treaties; (b) the validity and interpretation of acts of the institutions, bodies, offices or agencies of the Union.").

60. *See* Haegeman v. Belgium, 181/73, [1974] E.C.R 449, ¶ 2–6; Hauptzollamt Mainz v. C.A. Kupferberg & Cie KG a.A, 104/81, [1982] E.C.R ¶ 20 (identifying what are the conditions that international law provisions must fulfill for being invoked by individuals).

61. *See*, *e.g.*, Portugal v. Council, Case C-149/96, Portuguese Republic v. Council, [1999] E.C.R. I-08395; Van Parys NV v. Belgisch Interventie- en Restitutiebureau (BIRB), Case C-377/02, [2005] E.C.R. I-1465; Fabbrica Italiana Accumulatori Motocarri Montecchio SpA v. Council, FIAMM Joined Cases C-120/06P & C-121/06P, [2008] E.C.R. I-6513; Monsanto Technology LLC Judgment of the Court (Grand Chamber) of 6 July 2010, Case C-428/0, 2010 I-06765 (involving WTO law). *See generally* Yassin Abdullah Kadi and Al Barakaat International Foundation v. Council of the European Union and Commission of the European Communities, Joined Cases C-402/05 P and C-415/05 P, [2008] I-06351 [2008] E.C.L.I. 461; Commission of the European Communities v. Ireland, Case C-459/03, [2006] I-04635; The Queen, on the application of International Association of Independent Tanker Owners (Intertanko) and Others v. Secretary of State for Transport, Case C-308/06, [2008] I-

Stichting Natuur en Milieu judgment,[63] concerning the 1998 Aarhus Convention,[64] where a Commission Decision authorizing The Netherlands to postpone the introduction of certain EU clean air requirements was challenged by an NGO. The application, considered well founded by the General Court (GC), was finally dismissed by the European Court of Justice (ECJ). The EU judges remarked that, according to settled case law, the provisions of an international agreement to which the EU is a party can be relied on in support of an action for annulment of an act of secondary EU legislation only where the nature and broad logic of that agreement do not preclude it, and those provisions appear to be unconditional and sufficiently precise.[65]

04057; Commune de Mesquer v. Total France SA and Total International Ltd., Case C-188/07, [2008] I-04501 (involving international law outside the WTO).

62. *See generally* Jacques Bourgeois, *The European Court of Justice and the WTO*, *in* THE EU, THE WTO, AND THE NAFTA 71-124 (Joseph H. H. ed., 2000); Christina Eckes, *The European Court of Justice and (quasi)judicial bodies of international law*, *in* BETWEEN AUTONOMY AND DEPENDENCE: THE EU LEGAL ORDER UNDER THE INFLUENCE OF INTERNATIONAL ORGANISATIONS 85–109 (Ramses A. Wessel, & Steven Blockmans eds., 2013); Piet Eeckhout, EU EXTERNAL RELATIONS LAW 323-436 (2011); INTERNATIONAL LAW AS LAW OF THE EUROPEAN UNION (Enzo Cannizzaro, Paolo Palchetti, & Ramses A. Wessel eds., 2011); Pieter Jan Kuijper, *'It Shall Contribute to . . . the Strict Observance and Development of International Law'*, *in* THE COURT OF JUSTICE AND THE CONSTRUCTION OF EUROPE: ANALYSES AND PERSPECTIVES ON SIXTY YEARS OF CASE LAW 589–612, 597–601 (2013); Mario Mendez, THE LEGAL EFFECTS OF EU AGREEMENTS (2013); Allan Rosas, *The European Court of Justice and Public International Law*, *in* THE EUROPEANISATION OF INTERNATIONAL LAW – THE STATUS OF INTERNATIONAL LAW IN THE EU AND ITS MEMBER STATES 71-85 (Jan Wouters, André Nollkaemper, & Erika de Wet eds., 2008); Marco Bronckers, *From "Direct Effect" to "Muted Dialogue": Recent Developments in the European Courts' Case-law on the WTO and Beyond*, J. INT'L ECON. L. 885 (2008); Marco Bronckers, *The Effect of the WTO in European Court Litigation*, 40 TEX. INT'L L.J. 443 (2005); John Errico, *The WTO in the EU: Unwinding the Knot*, CORNELL INT'L L.J. 179 (2011); Nikolaos Lavranos, *Protecting European law from international law*, EUR. FOREIGN AFF. REV. 265 (2010); Anna Peters, *The Position of International Law Within the European Community Legal Order*, GR. Y.B INT'L L. 9 (1997); Gráinne de Búrca, *The European Court of Justice and the International Legal Order After Kadi*, (The Jean Monnet Ctr. Working Paper No. 01/09, 2009), http://jeanmonnetprogram.org/paper/the-european-court-of-justice-and-the-international-legal-order-after-kadi/; Christina Eckes, *International Law as Law of the EU: The Role of the ECJ*, (Cleer Working Paper, June 2010), http://www.asser.nl/media/1622/clee10-6web.pdf; Gráinne de Búrca, *International Law Before the Courts: The European Union and the United States Compared*, (NYU Sch. L., Pub. L. & Legal Theory, Working Paper No. 14-61, 2014), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2487361 (discussing the legal effects of international law in the EU legal order).

63. *See* Council and Commission v. Stichting Natuur en Milieu and Pesticide Action Network Europe, Joined Cases C-404/12 P and C-405/12 P, [2015] E.C.L.I. 5.

64. *See generally* UNECE Convention on Access to Information, *Public Participation in Decision-making and Access to Justice in Environmental Matters*, UN Doc. ECE/CEP/43 (Oct. 30, 2001).

65. *See Stichting Natuur en Milieu*, *supra* note 63, at ¶ 53.

Most importantly, the Court observed that Article 9(3) of the Aarhus Convention does not contain any unconditional and sufficiently precise obligations capable of directly regulating the legal position of individuals.[66] The Court, in relation to bilateral trade treaties, instead, recognized, at least in theory, to private parties the right to directly invoke those agreements;[67] however, this recognition has been contradicted by the normative choices made by EU negotiators with their third countries' counterparts in the CETA 2016, the EU-Vietnam FTA, as well as in the 2015 TTIP Proposal. The same holds true for those FTAs that have been already concluded, are now in force and do not include investment chapters. All these agreements have a clause which leaves no room for doubt.[68]

For instance, Article 8 of the Council decision on the FTA with Korea reads: "[T]he agreement shall not be construed as conferring rights or imposing obligations which can be directly invoked before Union or Member State courts and tribunal."[69] The draft FTA with Vietnam provisional Article X.19, entitled "No Direct Effect", Chapter XX, provides that "nothing in this Agreement shall be construed as conferring rights or imposing obligations on persons, other than those created between the Parties under public international law." Furthermore, Article 30(6) of CETA 2016, which mirrors Article 14(16) of CETA 2014, states that "nothing in this Agreement shall be construed…as permitting this Agreement to be directly invoked in the domestic legal systems of the Parties," where the expression "domestic legal systems" is to be understood as

66. *See Stichting Natuur en Milieu*, *supra* note 63, at ¶¶ 46-47.

67. *See e.g.*, Igor Simutenkov v. Ministerio de Educación y Cultura and Real Federación Española de Fútbol, Case C-265/03, [2005] E.C.R. I-02579, ¶¶ 20-29.

68. *See generally* EU-Korea Free Trade Agreement; EU-Colombia Free Trade Agreement; EU-Peru Free Trade Agreement, EU-Singapore Free Trade Agreement; EU-Viet. Free Trade Agreement, *supra* note 3; CETA, *supra* note 3. *See* Aliki Semertzi, *The preclusion of direct effect in the recently concluded EU free trade agreements*, COMMON MKT. L. REV. 1125 (2014) (providing an interesting survey of agreements).

69. Council Decision, 2011/265/EU (on the signing, on behalf of the European Union, and provisional application of the Free Trade Agreement between the European Union and its Member States, of the one part, and the Republic of Korea, of the other part), art. 8, 2011 O.J. 2011, L 127/1. The FTA with Singapore reads: "For greater certainty, nothing in this Agreement shall be construed as conferring rights or imposing obligations on persons, other than those created between the Parties under public international law". *See* Free Trade Agreement, EU-Sing., art. 17.15, *authentic text as of* May 2015 (pending formal approval by the European Commission, Council of Ministers, and ratification by the European Parliament).

comprising both national and EU legal orders.[70] Moreover, on one hand, the CJEU affirmed that if the Parties decided to define in the agreement the scope of the rights and obligations arising from the treaty, the Court itself will abide by that choice.[71] On the other hand, it made clear that international agreements are self-executing "only where the nature and the broad logic of the latter do not preclude this."[72] The above-mentioned clause prevents investors from directly invoking the treaties, not only before Member States' courts but also before the CJEU. From this, it follows that FTAs will get the same treatment, *mutatis mutandis*, as that accorded by the CJEU to WTO law.[73]

2. Effective Judicial Protection

The lack of direct effect of FTAs clearly represents an obstacle to ensure an effective system of judicial protection of individual rights.[74] In fact, denying access to domestic courts blunts the impact of such agreements on daily life, reducing the courts' efficacy and leaving their potential unrealized. The effectiveness of EU law itself has been ensured over the years only through the CJEU's recognition of direct effect – combined with the application of the principle of supremacy – and its qualification as a matter of both human rights and

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70. Even though Article 30(6) does not expressly identify the judicial bodies concerned, in contrast with the text contained in other FTAs. *See* Comprehensive Economic and Trade Agreement (CETA), Can.-E.U., art. 30.6, *draft finalized* Sept. 2014 (Pending internal approval process in Canada and the European Union), http://trade.ec.europa.eu/doclib/docs/2014/september/tradoc_152806.pdf.

71. *See* Air Transport Association of America & Others v. Secretary of State for Energy and Climate Change, Case C-366/10, [2011] E.C.R. I-13755, ¶ 49 (noting that "European Union institutions which have power to negotiate and conclude an international agreement are free to agree with the third States concerned what effect the provisions of the agreement are to have in the internal legal order of the contracting parties").

72. *See* Intertanko and Others, Case C-308/06, [2008] E.C.R. I-4057, ¶ 45.

73. *See* Antonello Tancredi, *On the Absence of Direct Effect of the WTO Dispute Settlement Body's Decisions in the EU Legal Order*, *in* INTERNATIONAL LAW AS LAW OF THE EU, *supra* note 62, at 249-68.

74. *See* Marise Cremona, Guest Editorial, *Negotiating the Transatlantic Trade and Investment Partnership (TTIP)*, 31 COMMON MKT. L. REV. 354-62 (2015); Marco Bronckers, *Is Investor–State Dispute Settlement (ISDS) Superior to Litigation Before Domestic Courts? An EU View on Bilateral Trade Agreements*, 18 J. INT'L ECON. L. 655, 662-64, 674-76 (2015) [hereinafter *Is Investor-State Dispute Settlement*]; Daniel Thym, *The Missing Link: Direct Effect, CETA/TTIP and Investor-State Dispute Settlement*, EU L. ANALYSIS (Jan. 7, 2015) (observing that the denial of direct effect of a free trade and investment agreement constitutes a "stumbling block" for its long-term success), http://eulawanalysis.blogspot.it/2015/01/the-missing-link-direct-effect-cetattip.html; *see also* TTIP Consultation, *supra* note 4.

market integration.[75] Therefore, an investor-State adjudication mechanism seems to be necessary, at least as long as the approach of the EU to the incorporation of international law in the EU system remains unchanged (i.e., as long as this mechanism is the only one currently capable of providing a direct procedural remedy to foreign investors).

The other possible option is to recognize the indirect effect of international agreements, but it does not seem to be the best alternative. In other words, the issue is whether that recognition, through the principle of consistent interpretation, could adequately protect the interests and rights of investors claiming to be the victim of a violation by EU or national authorities.[76] According to said principle, both national courts and the CJEU must interpret the law in a manner consistent with the agreement itself, which operates as a parameter of legitimacy in the EU legal order, within the limits of the established case law.[77] The problem with consistent interpretation is that it confers so much discretion on domestic courts that uniformity and legal certainty may be endangered at the expense of foreign investors, especially given the existence of 28 different jurisdictions. Furthermore, it does not seem a satisfactory path as the requirements

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75. *See* Ernst-Ulrich Petersmann, *Transformative Transatlantic Free Trade Agreements without Rights and Remedies of Citizens?*, 18 J. INT'L ECON. L., 579, 583-84, 594 (2015) (remarking on the human rights dimension implied in the legal discourse on direct effect of free trade and investment agreements); *see Is Investor-State Dispute Settlement*, *supra* note 74, at 675 (commenting on the market integration dimension of direct effect recognition).

76. *See generally* Federico Casolari, *International Law within the EU Legal Order: The Doctrine of Consistent Interpretation*, *in* INTERNATIONAL LAW AS LAW OF THE EU, *supra* note 62, at 395-415; Gaetano Iorio Fiorelli, *WTO as a parameter for the EC legislation through the "consistent interpretation" doctrine*, *in* THE ABSENCE OF DIRECT EFFECT OF WTO IN THE EC AND IN OTHER COUNTRIES 121-33 (Claudio Dordi, ed., 2010); Giacomo Gattinara, *Consistent Interpretation of WTO Rulings in the EU Legal Order?*, *in* INTERNATIONAL LAW AS LAW OF THE EU, *supra* note 62, at 269-87; Gerrit Betlem & André Nollkaemper, *Giving Effect to Public International Law and European Community Law before Domestic Courts. A Comparative Analysis of the Practice of Consistent Interpretation*, 14 EUR. J. INT'L L., 569 (2003); Jan-Peter Hix, *Indirect Effect of International Agreement: Consistent Interpretation and Other Forms of Judicial Accommodation of WTO Law by the EU Courts and US Courts*, (Jean Monnet Working Paper No. 03/13, 2013), http://jeanmonnetprogram.org/paper/indirect-effect-of-international-agreements-consistent-interpretation-and-other-forms-of-judicial-accommodation-of-wto-law-by-the-eu-courts-and-the-us-courts-2/ (giving general considerations concerning the doctrine of consistent interpretation, as applied by the CJEU to international law).

77. *See*, *e.g.*, Interfood GmbH v. Hauptzollamt Hamburg-Ericus, Case C-92/71, [1972] E.C.R. 231; Hauptzollamt Mainz v. CA Kupferberg & Cie KG, Case C-104/81, [1982] E.C.R. 3644; Fediol v. Commission, Case C-70/87, [1989] E.C.R. 1825; Nakajima v Council, Case C-69/89, [1991] E.C.R. I-2169.

for indirect effect are only slightly more relaxed than those for direct effect. In any event, it is beyond doubt that by relying on the indirect effect of international agreements' provisions, such as a reading of EU legislation that cannot be *per se contra legem*, an individual does not seek to challenge the legality of a domestic measure but merely wants to have that provision interpreted in a favorable way.[78] This means that, while not unimportant, the impact of such an action is limited[79] in scope.[80]

In light of the foregoing, one may conclude that FTAs that contain a clause on the preclusion of direct effect, but no provision on investor-State adjudication, are a step back in terms of protection of individual rights. At present, a system of investor-State dispute settlement – even though "external" to the EU legal order as well as to national ones – appears to be the only solution to ensure an advanced form of judicial protection to investors. Having said this, the situation would certainly be different where the agreement contains no clause precluding direct effect, and consequentially private enforcement before domestic courts is possible. In this respect, what the EU should do is depart from its current approach and give domestic courts (the CJEU and national judges) the power to adjudicate claims submitted by private parties. On one hand, FTAs should not preclude the direct effect of the provisions they contain. On the other hand, the CJEU should take action since it is responsible for deciding whether to recognize direct effect and, as stated in the *Kupferberg* case, the existence of an institutional framework for settling disputes between the parties to an agreement "is not in itself sufficient to exclude all judicial application of that agreement."[81]

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78. *See*, *e.g.,* Federico Casolari, L'INCORPORAZIONE DEL DIRITTO INTERNAZIONALE NELL'ORDINAMENTO DELL'UNIONE EUROPEA, 336-350, 345-346 (2008) (It.).

79. *See Is Investor–State Dispute Settlement*, *supra* note 74, at 665.

80. It is limited in scope – with different conditions and objectives – also Article 340 TFEU, in that it confers upon investors the right to right to rely on such provision to ask for compensation damages for wrongful behaviour on the part of EU institutions; see on this point Francesco Munari, Chiara Cellerino, *General Principles of EU law and international investment arbitration*, in *DIRITTO DEL COMMERCIO INTERNAZIONALE*, 2015, 115, at 136 (examining the potential of Article 340 TFEU).

81. *See* Hauptzollamt Mainz v. CA Kapferberg and Cie KG, C-104/81, [1982] E.C.R. 3664, ¶ 20; *see also* Beatrice Bonafé, *Direct Effect of International Agreements in the EU Legal Order: Does it Depend on the Existence of an International Dispute Settlement Mechanism?*, *in* INTERNATIONAL LAW AS LAW OF THE EU, *supra* note 62, 229-48 (explaining the interplay between direct effect and the existence of a court in international agreements).

Regarding the case of agreements concluded with partners of the EU, whose legal systems do not provide for self-executing rights deriving from international law provisions, the recognition of direct effect by the EU and Member States would arguably create an asymmetry between the parties to the agreement and might be unprofitable for both European and national institutions. This argument first does not fully take into account the case law of the CJEU, in which the Court observes that such divergence "is not in itself such as to constitute a lack of reciprocity in the implementation of the agreement."[82] Secondly, it does not address the key role of the protection of justiciable fundamental rights, to which the principle of reciprocity does not apply.[83]

In any event, should FTAs be granted direct effect in the future, the rule of prior exhaustion of local remedies may apply in principle. While this rule, as previously noted, cannot produce any *effet utile* if and when direct effect is excluded, its recognition would allow private parties to effectively bring their claims first before domestic courts, so that if unsuccessful, they may later have recourse to investor-State tribunals. However, this cannot obscure the fact that additional problems attached to the involvement of national courts still remain. As underlined above, they concern the fragmentation of rulings caused by the 28 jurisdictions, as well as the different level of investment protection (at both procedural and substantive levels) ensured by national courts. It is beyond doubt that in order to secure an effective system of investment disputes settlement, Member States and the EU should find a way to reduce the obstacles implied in many national judicial systems as much as possible. A substantial homogeneity and adequate protection of investor's rights might be guaranteed by the involvement of the CJEU should the investor be dissatisfied with rulings delivered by a court of a Member State and the national court be inclined (or obliged) to request the Court to give a ruling, in accordance with Article 267 TFEU.

82. *See CA Kapferberg and Cie KG*, [1982] E.C.R. 3664, ¶ 18.

83. *See Is Investor-State Dispute Settlement*, *supra* note 74, at 672, 675.

II. DANGEROUS LIAISONS BETWEEN INVESTOR-STATE ADJUDICATION AND THE CJEU: THE PRINCIPLE OF AUTONOMY OF EU LAW UNDER ATTACK

A. Inevitable Clashes for Intra-EU BITs

Conflict of laws has been a challenging subject for the EU and its Member States starting with the drafting of the 1968 Brussels Convention on Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters.[84] With the entry into force of the Treaty of Amsterdam in 1999, the EU has attempted to resolve the controversies in private international law conventions by undertaking the "communitarization" of private international law.[85] In addition, the Amsterdam Treaty gave the European Parliament powers to veto and regulate other commercial treaties, and adjust them toward applicable EU law. Despite these efforts, it has turned into complex jurisdictional clashes between two different international legal regimes in what George Bermann called the "distant worlds of EU and international arbitration law."[86]

If international commercial treaties have been reconciled with EU law norms, in contrast the clash between Bilateral Investment Treaties (BITs) and EU law has been dramatic. The Treaty of Lisbon aimed to reconcile some of these differences through article 351(2) TFEU requiring Member States to take any "appropriate steps to eliminate the incompatibilities established" in international treaties incompatible with EU law. This provision, however, has been of limited usefulness in the clashes between BITs signed either among Member States of the EU (Intra-EU BITs) [87] or between a Member

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84. *See* Vera Fritz, *Tessili vs. Dunlop 1976: The Political Background of Judicial Restraint* (in BILL DAVIES AND FERNANDA NICOLA EDS., EU LAW STORIES: CONTEXTUAL AND CRITICAL HISTORIES OF EUROPEAN JURISPRUDENCE (2016 forthcoming) (on file with author).

85. *See* Fausto Pocar, *The "Communitarization" of Private International Law and its Impact on the External Relations of the European Union*, in THE EXTERNAL DIMENSION OF EC PRIVATE INTERNATIONAL LAW IN FAMILY AND SUCCESSION MATERS 3-15 (Alberto Malatesta, Stafania Bariatti & Fausto Pocar eds., 2008).

86. *See* George Bermann, *supra* note 28, at 400.

87. *See* Konstanze von Papp, *Solving Conflicts with International Investment Treaty Law from an EU Law Perspective: Article 351 TFEU Revisited*, 42 LEGAL ISSUES OF ECON. INTEGRATION 325 (2015), available at SSRN: http://ssrn.com/abstract=2726550 ("It will be argued that the current reading of Article 351 TFEU is of limited usefulness, since it is overly restrictive and ultimately concerned with fostering EU supremacy in external relations.").

State and a non-EU State (Extra EU-BITs).[88] This part focuses on the intra-BITs that create an obvious challenge to the EU legal order especially due to the fact that a number of them were agreed around the 1990s, well before the EU enlargement of 2004. Therefore, many BITs were concluded between the wealthy existing EU Member States whose investors wanted to be reassured before investing in the former Eastern European States eventually known as the "EU 13" block. By 2014, when the EU 13 countries had all become EU members, the Intra-EU BITs were not eliminated but rather kept as guarantees of protection from expropriation without compensation and arbitration procedures.

As a result, the Commission has through infringement proceedings asked Member States to terminate existing Intra-EU BITs that are contrary to EU law.[89] Paradoxically, today European investors might want to maintain their benefits under BITs because the independence of the judiciary in both Hungary and Poland is at risk in these Member States.[90] However, the fact that BITs confer rights only to investors from some Member states and not others creates a discrimination based on nationality that is incompatible with EU law and reinstated by CJEU case law. Yet it is hard to adapt ISDS clauses because international investment arbitration includes other organizations such as the International Centre for Settlement of Investment Disputes ("ICSID"). The ICSID convention plays an important role in the inflexibility of the BITs to adapt to EU law. For example, in terms of jurisdiction, the ICSID convention allows the arbitral tribunal to assert final jurisdiction over a dispute, which creates a major irritant for EU law and the potential conflict with CJEU jurisprudence.[91] Even though there may be some conflicts in the interpretation of BITs and EU law by arbitrators in an investor-

88. *See* Bermann, *supra* note 28, at 440.

89. *See* Commission Press Release, IP/15/5198 (Jun. 18, 2015), http://europa.eu/rapid/press-release_IP-15-5198_en.htm.

90. *See* Commission, Fact Sheet, *College Orientation Debate on recent developments in Poland and the Rule of Law Framework: Questions & Answers*, (Jan. 13, 2016), http://europa.eu/rapid/press-release_MEMO-16-62_it.htm; Kim Scheppele, *EU Commission v. Hungary: The Case for the Systemic Infringement Action*, VERFASSUNGSBLOG (Nov. 22, 2013), http://verfassungsblog.de/eu-commission-v-hungary-the-case-for-the-systemic-infringement-action/; Wojciech Sadurski, *What Makes Kaczynski Tick?*, I-CONNECT (Jan. 14, 2016), http://www.iconnectblog.com/2016/01/what-makes-kaczynski-tick/?utm_source=feedburner&utm_medium=email&utm_campaign=Feed%3A+I-CONnectBlog+%28I-CONnect+Blog%29.

91. *See* Bermann, *supra* note 28, at 439.

State dispute, under the Amsterdam Treaty of 1999 the Commission has the power to halt the enforcement of the final award.

According to George Bermann, another major reason often invoked by the Commission for non-enforcement of arbitral awards is public policy. This argument gained momentum in the case *Eco Swiss China Time Ltd v. Benetton International NV*.[92] In *Eco Swiss*, Benetton licensed a Hong Kong company (Eco Swiss) to manufacture watches using the slogan "Benetton by Bulova."[93] The agreement contained a limitation that "Eco Swiss could not sell the products in Italy."[94] The European Commission was not given notification of the agreement nor its special marketing scheme, and therefore the agreement was in violation of EU competition law.[95] Eco Swiss sued Benetton for damages. In application of the arbitration clause, an arbitral tribunal was formed under the laws of the Netherlands Institute of Arbitration and the substantive matter was judged in application of Dutch Law.[96] The tribunal held Benetton liable for the breach of the licensing agreement and ordered the payment of damages. The European Court of Justice ("ECJ"), however, voided the enforcement of the award stating that the award was issued in violation of EU anti-competition laws and that the enforcement of the award would be against public policy.[97]

While the Commission has used Eco Swiss to assert that "EU competition policy does indeed constitute EU public policy," the EU prohibition of State aids has become another major claim of non-enforcement of arbitral awards with mixed outcomes.[98] As a result EU law has determined that a Member State cannot provide State aid to an investor unless the Commission has previously approved the aid under its guidelines. This is a key issue when it comes to the clash between EU law and BITs; the *Micula Brothers* case has become the

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92. The EU Commission, based on public policy, set aside the award stating that the enforcement of the award would be considered a blunt violation of EU Law and ant competition laws. *See* Eco Swiss China Time Ltd. v. Benetton International NV, Case C-126/97, [1999] E.C.R. 3055.

93. *See* Bermann, *supra* note 28, at 411.

94. *Id.* at 411.

95. Contrary to Article 101 TFEU prohibits agreements between undertakings and concerted practices that might prevent or distort competition in the Member States.

96. *See* Bermann, *supra* note 28, at 412.

97. *See id.* at 413.

98. *Id.*

paradigmatic example of a clash between two distinct bodies of law resulting in a complex litigation before ICSID.

1. The Micula Brothers Case

The *Micula Brothers* case has become a landmark ICSID decision that shows the clashes of two worlds due to an intra-EU BIT agreement and the prohibition of state aids in EU law. In 1988, the Romanian government enacted the "Emergency Government Ordinance" ("EGO 24"). This statute allowed some tax exemptions to investors, such as custom duty exemptions and other tax incentives ("incentives").[99]

Capitalizing on the incentives, the Micula brothers commenced various investments in Romania.[100] In April 2003, Sweden and Romania signed a BIT.[101] Under the BIT, the signatory States would (1) require each contracting party to ensure fair and equitable treatment of the investments by investors of the other contracting party ("FET clause"),[102] and (2) observe any other obligation entered into by the State with an investor of the other contracting party with regard to their investment ("umbrella clause").[103] In 2007, Romania discontinued these incentives as part of a condition to join the European Union. The termination of the incentives by the Romanian government was the cause of action to file BIT arbitration by the investors. Meanwhile the brothers, Ioan and Viorel Micula, acquired Swedish citizenship, which allowed them to file a complaint under the BIT claiming unfair treatment to a foreign investor.[104]

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99. *See* Nikos Lavranos, *Interference of the European Commission in the Enforcement of Arbitration Awards: The Micula Case*, GLOBAL INVESTMENT PROTECTION (May 5, 2014), http://www.globalinvestmentprotection.com/index.php/interference-of-the-european-commission-in-the-enforcement-of-arbitration-awards-the-micula-case/ (". . . the incentives included subsides, tax breaks and custom duty exceptions for investors on machinery and raw materials").

100. They opened the following companies: European Food SA, Starmill SRL, and Multipack SRL. *Micula v. Romania*, ICSID Case No. ARB/05/20, Final Award, ¶ 4 (Dec. 11 2013).

101. Bilateral Investment Treat between the Government of Romania and the Government of the Kingdom of Sweden. Date of BIT signature 05/29/2002; Date of entry into force 04/01/2003.

102. Sveriges Internationaella Overenskommelser, art. 3(2), [SO 2003:2], at 4-5.

103. *See Micula*, ICSID Case No. ARB/05/20, Final Award at ¶ 342.

104. *See id.* at 3. The Swedish citizenship allowed the Micula brothers to file a complaint against Romania under the FET clause (Article 3.2) because the clause protects foreign investors in the host country. Had they not acquired Swedish citizenship, the Micula Brothers could not have sued Romania under the BIT.

Once litigation started, Romania challenged the jurisdiction of ICSID. However, on September 24, 2008 the arbitral panel ("Tribunal") rejected this contention and ratified its jurisdiction to solve the dispute.[105] On the merits, the Micula brothers alleged that they made investments "in one of the poorest and least developed regions of Romania" with the expectation that the incentives would remain in place for ten years, and the legal change harmed their investment-backed expectation.[106] Further, claimants argued that Romania failed to inform the investors that the incentives, particularly the raw materials incentive, would have to be reversed.[107] This harm to the expectations, as claimed by the Micula brothers, amounted to an expropriation without compensation.[108] Also, they argued that Romania breached the BIT when it failed to provide FET when it ceased the incentives.[109] Finally, they alleged the BIT was not contrary to EU law because under article 9(2) of the BIT, the Investment Treaty would prevail in case of a conflict of laws.[110] Romania, on the other hand, argued that the claimants did not rely on the incentives to make their investments, or if they did, that reliance was unreasonable.[111] Romania also contended that the changes in the incentive regime did not violate the BIT as its actions were reasonably related to a rational policy, namely EU accession.[112] If the BIT were found to be incompatible with EU law, the latter would prevail on the basis of the principle *lex specialis derogat legi*

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105. *See Micula*, ICSID Case No. ARB/05/20, Final Award at ¶¶ 284-85.

106. *See id.* at ¶¶ 1, 252 ("The Claimants claim that, in reliance on those incentives, and in reliance on the expectation that these incentives would be maintained during a 10-year period, they made substantial investments in the Ştei-Nucet-Drăgăneşti disfavored region located in Bihor County in northwestern Romania.").

107. *See* Nikos Lavranos, *Interference of the European Commission in the Enforcement of Arbitration Awards: The Micula v. Romania Case*, GLOBAL INVESTMENT PROTECTION (Nov. 5, 2014), http://www.globalinvestmentprotection.com/index.php/interference-of-the-european-commission-in-the-enforcement-of-arbitration-awards-the-micula-case/
(acknowledging that "some Romanian regional authorities continued to reassure the investors that these Incentives would be safeguarded, while other parts of the government, who were negotiating with the European Commission (EC) on the accession, became convinced that it would have to be dropped.").

108. *Micula*, ICSID Case No. ARB/05/20, Final Award at ¶¶ 256, 270.

109. *Id.* at ¶ 257.

110. *Id*. at ¶ 294. In relying on the preservation of rights provision the claimants added that, even if under EU law Romania was obliged to phase out the Incentives, this would not excuse Romania's alleged breaches of the BIT and international law.

111. *Micula*, ICSID Case No. ARB/05/20, Final Award at ¶ 132.

112. *Id.*

generali.[113] Romania also asserted that Article 31(3)(c) of the Vienna Convention would require that the BIT be interpreted in light of EU Law, eliminating conflicting obligations.[114] Further, Romania prompted the tribunal to take into account the wider juridical context in which the BIT between Romania and Sweden was negotiated and concluded.[115] The conclusion of the BIT was a direct consequence of the European Union Association Agreement in the context of Romania's accession to the EU.[116]

The Tribunal rejected the contention made by Romania and considered that the BIT and the EU law are not in conflict and therefore the BIT should be applied as an independent body of law.[117] The Tribunal asserted that EU law seemed to be part of the general scheme of applicable laws to this dispute.[118] The Tribunal held that Romania had breached its obligation of providing a FET to the Micula Brothers under the BIT.[119] They set forth a test to consider if Romania failed to provide FET, analyzing if (a) the State had made a promise or assurance, (b) the claimants relied on that promise or assurance as a matter of fact, and (c) such reliance was reasonable.[120] The Tribunal found that: (a) Romania made specific promises to the claimants in regards to the incentives and their duration; (b) Romania's conduct had induced the claimants to believe that the incentives would not be taken; and (c) it was reasonable for the Micula Brothers to believe that the incentives were legal under Romanian law.[121]

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113. "Special law repeals general laws." *Id.* at ¶ 310.

114. *Id.* at ¶ 305.

115. *Micula*, ICSID Case No. ARB/05/20, Final Award at ¶ 304.

116. *See id.* at ¶ 308 ("In view of the above, the Respondent contends that all substantive obligations contained in the BIT must be interpreted in a manner consistent with EU law. This includes in particular Article 64 of the Europe Agreement and Article 87 of the EC Treaty.").

117. *See id.* at ¶ 319 ("As a first step, the Tribunal notes that there is no real conflict of treaties. In the time period relevant to this dispute, the relevant rules of international law applicable to Romania and Sweden were the Europe Agreement (which entered into force on 1 February 1995) and the BIT (which entered into force on 1 April 2003). The Accession Treaty was not signed until 25 April 2005, and entered into force on 1 January 2007, date on which the EC Treaty also entered into force with respect to Romania.").

118. *Id.* at ¶ 317.

119. This was held by the majority of the arbitrators: Laurent Lévy and Stanimir Alexandrov. However, the Tribunal did not find a regulatory taking in this case. *See Micula v. Romania*, ICSID Case No. ARB/05/20, Separate Opinion of Georges Abi-Saab, ¶ 13 (disagreeing that Romania's lack of transparency amounted to a breach of FET).

120. *Micula*, ICSID Case No. ARB/05/20, Final Award at ¶¶ 608, 668.

121. *Id.* at ¶¶ 677, 703, 721.

The Tribunal held that the BIT and the applicable EU laws were not in conflict since there was not reasonable foreseeability that Romania's accession to the EU would change any provision to the already-negotiated BIT.[122] In cases of doubt of the application and finality of the BIT, the tribunal stated that it must consider the application of the BIT in the light most favorable to the investors.[123] The main reason it held that Romania's accession to the EU did not change the BIT was that Romania maintained certain provisions of EGO 24 that were not under EU pressure to change.[124] Also, the majority of the arbitrators (Laurent Lévy and Stanimir Alexandrov) held that EGO 24 was still applicable since the BIT did not provide a definition of FET of investors.[125] The Tribunal held that even though legislation is constantly evolving, the nation has to strive to protect the legitimate interest of its investors by acting in a procedurally proper manner.[126] Failure to comply with these guidelines would result in the nation's international liability. The monetary award amounted to $250 million.[127]

In 2015, via a decision addressed to Romania, the Commission ordered a halt on payment to the investors since the award was

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122. *See id. at* ¶ 321 (stating that "the Tribunal notes that the BIT does not contain any reference to EU accession or to the EU. Further, the Accession Treaty did not contain any references to the BIT, let alone seek to modify any of the BIT's provisions").

123. The Tribunal took this approach based on Saluka Investments BV (Netherlands) v. Czech Republic. *See Micula v. Romania*, ICSID Case No. ARB/05/20, at ¶ 504; *see generally* Saluka Investments BV (Netherlands) v. Czech Republic, IIC 210, Partial Award (Mar. 17, 2006), http://www.italaw.com/sites/default/files/case-documents/ita0740.pdf.

124. *See* Christian Leathely and Alejandro Garcia*, Breach of fair and equitable treatment standard (ICSID)*, ARBITRATION NOTES (Jan. 16, 2014, 4:41 PM), http://hsfnotes.com/arbitration/2014/01/16/breach-of-fair-and-equitable-treatment-standard-icsid/ ("The tribunal reasoned that the existence of an 'obligation' should be determined according to 'governing law', in this case, Romanian law.").

125. *See id.* at ¶ 446.

126. *See Micula v. Romania*, ICSID Case No. ARB/05/20, at ¶ 529 ("In the Tribunal's view, the correct position is that the state may always change its legislation, being aware and thus taking into consideration that: (i) an investor's legitimate expectations must be protected; (ii) the state's conduct must be substantively proper (e.g., not arbitrary or discriminatory); and (iii) the state's conduct must be procedurally proper (e.g., in compliance with due process and fair administration). If a change in legislation fails to meet these requirements, while the legislation may be validly amended as a matter of domestic law, the state may incur international liability.").

127. *See Micula v. Romania*, 2015 O.J. (L 232) 69, ¶ 27 ("The Tribunal further decided that Romania has to pay damages to the claimants. In total, the Tribunal awarded the claimants RON 376,433,229 plus interest.").

incompatible with EU State aid rules.[128] The principal reason for ordering the payment stop was that such payment would be considered illegal State aid since the Micula brothers would receive compensation in the same amount of the benefits.[129] Therefore these benefits are in direct violation of the EU State aid rules. The role of EU law with respect to intra-EU BITs remains, however, a disputed issue as to which arbitral tribunals held certain views; if the *Micula Brothers* tribunal suggested that EU law would be part of the factual background to the case, by contrast, in *Electrabel SA v. Hungary*, the arbitral tribunal considered EU law to be applicable law.[130] There are a number of pending cases in which this is an issue in dispute. A few years before, in *Eureko v. Slovak Republic*, the Tribunal decided that the BIT was not in violation of EU law because unlike in *Micula Brothers*, the BIT was still fully enforceable. [131]

If interpreted through the lens of the US regulatory takings jurisprudence, the *Micula Brothers* case might reach a different outcome. In *Penn Central Transportation Co. v. New York,*[132] the US Supreme Court formulated a comprehensive test to assess regulatory taking based on three elements: (1) the economic impact of the regulation on the particular owner;[133] (2) the protection of reasonable

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128. *See id.* art. 2(1) ("Romania shall not pay out any incompatible aid referred to in Article 1 and shall recover any incompatible aid referred to in Article 1 which has already been paid out to any one of the entities constituting the single economic unit benefiting from that aid in partial implementation or execution of the arbitral award of 11 December 2013, as well as any aid paid out to any one of the entities constituting the single economic unit benefiting from that aid in further implementation of the arbitral award of 11 December 2013 that the Commission has not been made aware of or that is paid out after the date of this Decision. 2. Viorel Micula, Ioan Micula, S.C. European Food SA, S.C. Starmill S.R.L., S.C. Multipack, European Drinks SA, Rieni Drinks SA, Scandic Distilleries SA, Transilvania General Import-Export S.R.L., and West Leasing S.R.L shall be jointly liable to repay the State aid received by any one of them.").

129. *See id.* at ¶ 48.

130. *See* Electrabel SA v Hungary, ICSID Case No. ARB/07/19 (Nov. 25, 2015).

131. *See* Achmea B.V. v. The Slovak Republic, UNCITRAL, PCA Case No. 2008-13, Final Award (Dec. 7, 2012).

132. *See* Penn Cent. Transp. Co. v. New York, 438 U.S. 104 (1978).

133. *Id.* at 124. *See also* JOSEPH WILLIAM SINGER ET. AL, PROPERTY: LAW RULES, POLICIES, AND PRACTICES 1192 (Wolters Kluwer, 6th ed.) (elaborating that the greater the value reduction, the more likely the regulation will qualify as a taking); Lingle v. Chevron U.S.A. Inc., 544 U.S. 528 (2005) (finding that complete deprivation of any "economically viable use" is likely to be a taking unless the regulation denies property rights that never existed in the first place); *accord* Lucas v. South Carolina Coastal Council, 505 U.S. 1003 (1992); Yee v. City of Escondido, 503 U.S. 519 (1992); Pennell v. City of San Jose, 458 U.S. 1 (1988); Kaiser Aetna v. United States., 444 U.S. 164, 175 (1979) (holding that the main characteristic of this ad-hoc test is that it has to be applied to every takings case as separate

or distinct investment-backed expectations;[134] and (3) the character of the governmental action.[135]

The appellant in *Penn Central* was UGP Properties, who owned the land where the Grand Central Station was erected and wanted to construct a 50 story-high office building above the Grand Central Terminal in New York City. The City's Board of Estimates barred that construction based on the Landmarks Preservation Law ("Preservation Law"). The Board also rejected a second proposal to build a building with different characteristics above Grand Central. Due to the denial of both requests to build on the property owned by UGP Properties, the appellant brought suit. The appellant stated that the application of the Preservation Law had taken their property without just compensation in violation of the Fifth and Fourteenth Amendments and arbitrarily deprived them of their property without due process of law.[136]

Justice Brennan reasoned that in deciding whether a particular governmental action has affected a taking, the Court must focus both on the character of the action and on the nature and extent of the interference with rights in the parcel as a whole.[137] Justice Brennan concluded that the ordinance could not be considered a regulatory taking because the economic impact of the Preservation Law did not negate any benefit to the appellant.[138] On the contrary, the impact of takings law has to be analyzed in the property as a whole and not only

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rather than applying a blanket formula to all of them); *see also* Block v. Hirsch, 256 U.S. 135 (1921).

134. *Penn Cent. Transp. Co.*, 438 U.S. at 124; *see also* SINGER, *supra* note 133, at 1194 (explaining if a citizen has already invested substantially, reasonably relying on an existing statutory or regulatory scheme, then the regulation is more likely to be a taking; if the regulation prevents the owner from realizing an expected benefit in the future, imposing merely opportunity cost, it is less likely to be a taking).

135. *Penn Cent. Transp. Co.*, 438 U.S. at 124. This element fluctuates between the governmental prerogative of enacting legislation to limit property rights without just compensation under the basis of "protection of the welfare," and the limit to compensate every time legislation enacted limits every kind of property rights. *See* Pennsylvania Coal v. Mahon, 260 U.S. 393, 413 (1922) ("Government hardly could go on if to some extent values incident to property could not be diminished without paying for every such change in the general law"). ("However, if protecting the welfare is sufficient to characterize a government action as a legitimate regulation rather than an unconstitutional taking, then the government will be able to destroy property interests at will without and the takings clause will be meaningless."); SINGER, *supra* note 133, at 1194.

136. *Penn Cent. Transp. Co.*, 438 U.S. at 122.

137. *Id.* at 133.

138. *Id.* at 138.

on the impact that the law may have on specific parcels of the property.[139] Further, Justice Brennan showed that there was indeed protection of reasonable investment-backed expectations of UGP Properties because the investor had obtained benefits when it leased Grand Central Station and such benefits negated the argument of lack of protection to investors.[140]

Applying Justice Brennan's reasoning to the *Micula Brothers* case, when the investor puts on one side of the scale his proprietary interest, the investor's wealth allegedly taken is in fact the result of prior regulatory interventions that have served his interests.[141] Only if the judge, like Justice Brennan in *Penn Central*, is willing to take apart the entitlement of the investor can he decide whether the investor has lost or deserves protection through compensation.

2. Balancing the Right to Regulate for Public Policy with the Fair and Equitable Treatment (FET) Standard for Investors

The crucial point in the *Micula Brothers* case is whether the State, through statements or conduct, contributed to the creation of a reasonable expectation of regulatory stability under the FET standard. For the tribunal, it is irrelevant whether the State wishes to treat the investors in violation of the FET standard because it is sufficient that it acted in a manner that would reasonably be understood to create such an appearance.[142] The element of reasonableness cannot be separated from the promise, assurance, or representation, particularly if the promise is not contained in a contract or is otherwise not stated explicitly. Whether a State has created a legitimate expectation in an investor is thus a factual assessment that must be undertaken in consideration of all the surrounding circumstances.[143] So, the question is how to assess the circumstances in light of what appears to be an

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139. *Id.* at 130.

140. *See id.* at 136 (noting that UGP maintained the right to use the space as was originally intended, and thus could still gain from the property's value even without building office space).

141. *See generally* Robert Hale, *Coercion and Distribution in a Supposedly Non-coercive State*, 39 POL. SCI. Q. 470 (1923); Duncan Kennedy, *The Stakes of Law, or Hale and Foucault!*, 15 LEGAL STUD. F. 327 (1991).

142. *Micula v. Romania*, ICSID Case No. ARB/05/20, Final Award, ¶ 708 (2013) (repeating the finding that the incentives themselves gave rise to legitimate expectations of their duration).

143. *Id.* at ¶ 669.

implicit promise that affects both the power of the State to regulate for public policy and the FET of investors.

It is possible to trace the *Penn Central* test elaborated by Justice Brennan in the Annex on Expropriation in the Commission position in TTIP, in CETA 2016, and with a minimum change in the EU-Vietnam FTA offering criteria to protect the State's right to regulate.[144] In particular, these agreements provide a multi-factor test for judges to assess the context around potential indirect expropriations:

> 2. (a) the economic impact of the measure or series of measures, although the sole fact that a measure or series of measures of a Party has an adverse effect on the economic value of an investment does not establish that an indirect expropriation has occurred;
>
> (b) the duration of the measure or series of measures of a Party;
>
> (c) the extent to which the measure or series of measures interferes with distinct, reasonable investment-backed expectations; and
>
> (d) the character of the measure or series of measures, notably their object, context and intent.
>
> 3. For greater certainty, except in the rare circumstance when the impact of a measure or series of measures is so severe in light of its purpose that it appears manifestly excessive, non-discriminatory measures of a Party that are designed and applied to protect legitimate public welfare objectives, such as health, safety and the environment, do not constitute indirect expropriations.[145]

The EU-Vietnam FTA lacks only clause 2(c), addressing "reasonable investment expectations," which is included in a similar test in the TPP's Annex 9-B on expropriation.[146] Despite these minimal differences, overall the test of whether there is an indirect expropriation or regulatory taking is nearly similar in all four FTAs,

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144. *See* 2015 TTIP Proposal, *supra* note 3, at Annex I; CETA, *supra* note 3, at Annex 8-A.

145. *See* CETA, *supra* note 3, at Annex 8-A.

146. *See* Trans-Pacific Partnership, Annex 9-B, art. 3a(ii), n.36, Feb. 4, 2016, https://ustr.gov/trade-agreements/free-trade-agreements/trans-pacific-partnership/tpp-full-text [hereinafter TPP] ("For greater certainty, whether an investor's investment-backed expectations are reasonable depends, to the extent relevant, on factors such as whether the government provided the investor with binding written assurances and the nature and extent of governmental regulation or the potential for government regulation in the relevant sector.").

demonstrating that there is no real controversy on this issue thanks to the legacy of *Penn Central*.

Even though there are similarities between EU-Vietnam FTA and CETA on the FET standard, what remains highly controversial between the EU and the US in TTIP is the definition of the FET standard of investment. In the TPP, the FET is part of a minimum standard of treatment that is in accordance with "customary international law principles, including fair and equitable treatment and full protection and security."[147] This means that full protection and security are also part of the minimum standard of treatment under CIL, so that the host State needs to act with due diligence to secure and protect the investment. In contrast, CETA, the EU-Vietnam FTA, and TTIP depart from CIL because there is no broad notion of equity protection for the investors under CIL, though all the protections for the investors are expressly enumerated in the treaties.[148] As Srilal M. Perera explains in two incredibly dense and thoughtful articles, the increasing use of CIL in investment arbitration through notions of equity and fairness filtrated through the FET standard has become a "prolific phenomenon in the past decade."[149] Perera shows that the dangers of "equity-based decision-making," when applied in the context of the FET standard, have resulted in a "subjective, vague and ambiguous characteristic of those undefined terms." As a result, Perera explains, with largely inconsistent awards there was no established criteria or a line of precedent through which to interpret equity-based decisions more objectively.[150] Thus, the major problem of this evolution of interpretation of CIL to assess the FET standard is the subjectivity of judgments due to arbitrators' discretion of interpretation. As a consequence, the degree of liability imposed as reparation has varied without any criteria for the standard of damages.[151]

In light of these critiques, there is a clear divide between the TPP, which includes CIL in the interpretation of the FET standard, and CETA and EU-Vietnam FTA, which have set aside the linkage

147. *See* TPP, *supra* note 146, art. 9.6.

148. *See* CETA, *supra* note 3, art. 8.10 (covering the Treatment of investors and of covered investments).

149. *See* Srilal M. Perera, *Equity-Based Decision-Making and the Fair and Equitable Treatment Standard: Lessons From the Argentine Investment Disputes – Part I*, 13 J. WORLD INV. & TRADE 210, 212 (2012).

150. *Id.* at 213.

151. *Id.* at 215.

between CIL and the FET standard. This remains one of the main causes of the divergence between the US and EU approaches to investment protection. The final legacy of *Micula Brothers* in CETA is the clarification that this agreement cannot be used to prevent the EU to enforce its State aid laws.[152]

B. (Extra-)EU Free Trade Agreements: How to Avoid Jurisdictional Clashes and Safeguard the Interpretive Monopoly of the CJEU

1. Autonomy of the EU Legal Order and the CJEU's Jurisprudence

As recognized by the CJEU in its *Van Gend en Loos* ruling, the EU "constitutes a new legal order of international law,"[153] that is, a legal order distinct from "pure" public international law. The Court went even further in another seminal judgment, *Costa*,[154] where it observed that the law stemming from the Treaty (now Treaties) is to be regarded as "an independent source of law"[155] and, "because of its special and original nature," it cannot be overridden by domestic legal provisions.[156] A corollary attached to the "specialty" and "originality" of EU law is the recognition and protection of its independence or autonomy.[157] The content and extent of this autonomy, as well as the principles of supremacy and direct effect that define it, have been shaped and safeguarded by the CJEU over the years; it is thanks to the Court's jurisprudence that the autonomy of the EU legal order has finally reached the status of an EU constitutional principle.[158]

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152. *See* Press Release, European Commission, CETA: EU and Canada Agree on New Approach on Investment in Trade Agreement (Feb. 29, 2016), http://europa.eu/rapid/press-release_IP-16-399_en.htm.

153. NV Algemene Transport v. Netherlands Inland Revenue Administration, Case 26-62, [1963] E.C.R. 3, 12.

154. Flaminio Costa v. E.N.E.L., Case 6-64, [1964] E.C.R. 1141, 594.

155. *Id.*; *see also* Jan W. van Rossem, *The Autonomy of EU Law: More is less?, in* BETWEEN AUTONOMY AND DEPENDENCE: THE EU LEGAL ORDER UNDER THE INFLUENCE OF INTERNATIONAL ORGANISATIONS, 13 (Ramses A. Wessel & Steven Blockmans eds., 2013) (observing that in the French version of the ruling, the sentence is translated as "une source autonome.").

156. *Flaminio Costa*, [1964] E.C.R. 1141, 594.

157. *See* Bruno de Witte, *Direct Effect, Primacy, and the Nature of the Legal Order*, *in* THE EVOLUTION OF EU LAW, 323-262 (Paul Craig & Gráinne de Búrca eds., 2011); *see also* van Rossem, *supra* note 155, at 41-42 (commenting on the interplay between autonomy and sovereignty.).

158. *See generally* RENÉ BARENTS, THE AUTONOMY OF COMMUNITY LAW (2004); Joseph H. H. Weiler & Ulrich R. Haltern, *The Autonomy of the Community Legal Order: Through the Looking Glass*, 37 HARV. INT'L L.J. 411 (1996); Bruno de Witte, *European Union*

This principle has both an external and internal dimensions. While the latter requires that the powers of the EU institutions not be eroded by national authorities and that EU norms not be outlawed by national legal systems, the former ensures that the functioning of international courts do not put those powers into question and that the norms of international law do not supersede EU law within those courts.[159] In particular, concerns have been raised that the autonomy of the EU legal order may be called into question by the investor-State arbitration mechanisms envisaged in EU agreements with non-EU countries.[160] Similar problems arise also with regard to the relationship between the EU law, on one hand, and, on the other hand, the 2015 TTIP Proposal and the new FTAs containing ICS clauses. As already clarified in Section I, our analysis was conceived before the release of both the CETA 2016 and the EU-Vietnam FTA, thus taking into account especially the ISDS system. However, the risks for possible infringement of the EU autonomy principle concern the ICS as well and will be accordingly considered.

The concerns regarding the impact of investor-State adjudication on the autonomy of EU legal order are based on the joint application of Article 19(1) of the TEU and Article 344 of the TFEU, according to which the interpretation and application of EU law falls under the exclusive jurisdiction of the Court, as repeatedly noted by EU judges. Article 19(1) of the TEU demands that the Court (and only the Court) must "ensure that in the interpretation and application of the Treaties

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Law: How Autonomous is its Legal Order? 65 ZEITSCHRIFT FÜR ÖFFENTLICHES RECHT 141 (2010).

159. *See* Bruno de Witte, *A Selfish Court?: The Court of Justice and the Design of International Dispute Settlement Beyond the European Union, in* THE EUROPEAN COURT OF JUSTICE AND EXTERNAL RELATIONS LAW. CONSTITUTIONAL CHALLENGES, 33-46 (Marise Cremona & Anne Thies eds., 2014) (giving an overview of the relationship between the CJEU and other dispute settlement systems, as well as of the external dimension of the Court's action.).

160. *See* EMMANUEL GAILLARD, LEGAL THEORY OF INTERNATIONAL ARBITRATION, 39-66 (2010) (commenting on the autonomy of international arbitration); *see also* George Bermann, *Reconciling European Union Law Demands with the Demands of International Arbitration*, 34 FORDHAM INT'L L.J. 1193 (2011) (providing a broad analysis of the interplay between EU law and arbitration). On the TTIP, see the Commission's Concept Paper, *supra* note 10, ¶ IV.1. Concerns have been expressed with regard to the compatibility of ISDS with the principle of autonomy of the EU legal order. A risk of such incompatibility would exist especially if ISDS tribunals were to interpret EU law in a manner that would be binding on EU institutions. Since ISDS tribunals only interpret the international agreement in question and would examine EU law only as a matter of fact, one may argue that concerns related to the autonomy of EU law are unfounded.

the law is observed," while Article 344 of the TFEU provides that "Member States undertake not to submit a dispute concerning the interpretation or application of the Treaties to any method of settlement other than those provided for therein." In light of these provisions, it becomes clear that any FTA between the EU and third countries must ensure that investor-State tribunals respect EU law, as interpreted and applied by the CJEU (and not by the tribunals on their own.)[161] The Court has confirmed this in a number of judgments and opinions in which, while admitting that the EU's treaty-making power comprises the creation of an international dispute settlement system whose institutions are vested with the authority to adopt rulings that are binding on the EU (including the CJEU), it has held that said institutions cannot render binding interpretations of EU law.[162] In the *Mox-Plant* judgment, for instance, the Court made it clear that an international agreement cannot affect the allocation of responsibilities defined in the Treaties and, consequently, "the autonomy of the Community legal system, compliance with which the Court ensures under Article 220 of the EC (now Art. 19 of the TEU)". That exclusive jurisdiction of the Court is confirmed, in the opinion of the Court, by Article 344 of the TFEU, by which "Member States undertake not to submit a dispute concerning the interpretation or application of the EC Treaty to any method of settlement other than

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161. *See* Angelos Dimopoulos, *The Compatibility of Future EU Investment Agreements with EU Law*, 39 LEGAL ISSUES ECON. INTEGRATION 447, 470 (2012) [hereinafter *Compatibility of Future EU Investment Agreements*]; Julie A. Maupin, *Where Should Europe's Investment Path Lead? Reflections on August Reinisch, "Quo Vadis Europe?"*, 12 SANTA CLARA J. INT'L L. 183, 219 (2014) (noting that it is the Court, and not the arbitrators on their own, that have made this determination).

162. *See* Opinion 1/75, Understanding on a Local Cost Standard, [1975] E.C.R. 1355.; *see generally* 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] (admitting that the EU's treaty-making power comprises the creation of an international dispute settlement system whose institutions are vested with the authority to adopt rulings that are binding on the EU (including the CJEU)); Opinion 1/09, Draft agreement – Creation of a unified patent litigation system, [2011] E.C.R. I-1137; Opinion 1/00, Proposed agreement between the European Community and non-Member States on the establishment of a European Common Aviation Area, [2002] E.C.R. I-3498; Opinion 2/92, Competence of the Community or one of its institutions to participate in the Third Revised Decision of the OECD on national treatment, [1995] E.C.R. 521; Opinion 1/94, Competence of the Community to conclude international agreements concerning services and the protection of intellectual property, [1994] E.C.R. 5267; Opinion 1/91, Draft Agreement Between the Community, on the one hand, and the countries of the European Free Trade Association, on the other, relating to the creation of the European Economic Area, [1991] E.C.R. 6079; Opinion 1/78, International Agreement on Natural Rubber, [1979] E.C.R. 2871.

those provided for therein."[163] In this respect, it is important to point out that, *prima facie*, Article 344 of the TFEU, which refers only to EU Member States, does not seem to come into play in the case of investor-State adjudication as this mechanism does not cover State-to-State disputes.[164] Nevertheless, in the literature it has been claimed that Article 344 of the TFEU could be interpreted, in theory, as covering situations concerning at least one State.[165] This would imply that, if future EU FTAs are concluded as mixed agreements – as they most likely will be –, the outcome may be different, since it could be possible to question the compatibility of the agreements with the EU legal order on the basis of that provision.[166]

As to the various CJEU opinions, the legal framework is the assessment of an international agreement by the CJEU in accordance with Article 218(11) of the TFEU as occurred in the case of the FTA with Singapore, for which an opinion has been requested by the Commission.[167] Article 218(11) of the TFEU provides that "[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 is adverse, the agreement envisaged may not enter into force unless it is amended or the Treaties are revised." The rationale of this provision is to carry out a review of the agreement negotiated by the Commission prior to its conclusion so that, rather than having the Court rule on its validity in the context of a preliminary procedure (Article 267 of the TFEU) or of an annulment action (Article 263 of the TFEU), the EU institutions may amend the text of the treaty in order to ensure its compatibility with the EU treaties (unless the latter are revised.)

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163. *See* TFEU, *supra* note 31, art. 344, at ¶ 123.

164. *See* Stephan W. Schill, *Editorial: Opinion 2/13 – The End for Dispute Settlement in EU Trade and Investment Agreements?*, 16 J. WORLD INV. & TRADE 379, 384 (2015).

165. *See* Konstanze Von Papp, *Clash of "Autonomous Legal Orders": Can EU Member State Courts Bridge the Jurisdictional Divide Between Investment Tribunals and the ECJ? A Plea for Direct Referral from Investment Tribunals to the ECJ*, 50 COMMON MKT. L. REV. 1039, 1052-54 (2013).

166. *See also* Marc Burgstaller, *Investor-State Arbitration in EU International Investment Agreements with Third States*, 39 LEGAL ISSUES OF ECON. INTEGRATION 207, 217 n.45 (2012) (noting, in relation to Article 344 of TFEU, that the argument according to which investor-State arbitration clauses with third states would not be prevented from being included in EU free trade and investment agreements assumes that these agreements will be concluded as 'pure' EU agreements rather than mixed agreements).

167. *See supra* Introduction.

For our purposes, it is sufficient to cite a few passages from Opinion 1/09 on the European and Community Patents Courts, in which the CJEU discussed the creation of a single European judicial institution for intellectual property rights with exclusive jurisdiction.[168]

First of all, the Court stressed that "an international agreement concluded with third countries may confer new judicial powers" on the aforesaid judicial institution, provided that "it does not change the essential character of the function of the Court as conceived in the TEU and the Treaty on the Functioning of the EU (TFEU)."[169] Moreover, it repeated that an international agreement may affect the Court's own powers provided that the indispensable conditions for safeguarding the essential character of those powers are satisfied and, consequently, "there is no adverse effect on the autonomy of the EU legal order."[170]

The approach described above was reiterated with further emphasis in Opinion 2/13 on the accession to the European Court of Human Rights ("ECtHR"),[171] in which the Court made clear, once

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168. *See* Roberto Baratta, *National Courts as 'Guardians' and 'Ordinary Courts' of EU Law: Opinion 1/09 of the ECJ*, 38 LEGAL ISSUES ECON. INTEGRATION 297 (2011) (writing from the standpoint of EU autonomy); Christina Eckes, *The European Court of Justice*, *supra* note 62, at 85; Matthew Parish, *International Courts and the European Legal Order*, 23 EUR. J. INT'L L. 141 (2012). *See also* Opinion 1/91, *supra* note 162 (stating that the jurisdiction conferred on the EEA Court under Article 2(c), Article 96(1)(a), and Article 117(1) of the agreement is likely to adversely affect the allocation of responsibilities defined in the Treaties and, hence, the autonomy of the Community legal order, respect for which must be assured by the Court of Justice pursuant to Article 164 of the EEC Treaty. This exclusive jurisdiction of the Court of Justice is confirmed by Article 219 of the EEC Treaty, under which Member States undertake not to submit a dispute concerning the interpretation or application of that treaty to any method of settlement other than those provided for in the Treaty); Opinion 1/00, *supra* note 162 (holding that preservation of the autonomy of the Community legal order requires therefore, first, that the essential character of the powers of the Community and its institutions as conceived in the Treaty remain unaltered). Second, it requires that the procedures for ensuring uniform interpretation of the rules of the ECAA Agreement and for resolving disputes will not have the effect of binding the Community and its institutions, in the exercise of their internal powers, to a particular interpretation of the rules of Community law referred to in that agreement. Opinion 1/91, *supra* note 162, at ¶ 61-65; Opinion 1/92, Draft Agreement Between the Community on the One Hand, and the Countries of the European Free Trade Association, on the Other, Relating to the Creation of the European Economic Area, [1992] E.C.R. I-2821, at ¶ 32, 34.

169. *See* Opinion 1/09, *supra* note 162.

170. *Id.*

171. Opinion of the Court (Full Court) of 18 December 2014, Accession of the European Union to the European Convention for the Protection of Human Rights and Fundamental; on investor-State arbitration in light of opinion 2/13 see Filippo Fontanelli, *The long shadow of*

and for all, that no body or institution other than the CJEU can interpret EU law in a binding way for Member States and EU institutions,[172] nor determine the distribution of responsibility between a Member State and the EU.[173] Therefore, the CJEU affirmed that it has an exclusive monopoly both in interpreting EU law and in allocating powers to the EU and its Member States by defining the scope of their competences. In Opinion 2/13, it stated that the exclusive interpretive monopoly would be infringed if the EU and its institutions, including the CJEU, were "subject to the control mechanisms provided for by the ECHR and, in particular, to the decisions and judgments of the ECtHR."[174] Indeed, "any action by the bodies given decision-making powers by the ECHR . . . must not have the effect of binding the EU and its institutions, in the exercise of their internal powers, to a particular interpretation of the rules of EU law."[175] As far as the "allocation monopoly" is concerned, the Court observed, *inter alia*, with regard to the "co-respondent mechanism" envisaged in Article 3 of the draft agreement that "if the EU or Member States request leave to intervene as co-respondents in a case before the ECtHR," they must give their reasons and fulfill the conditions for their participation in the procedure. [176] In doing so, the ECtHR would be given the power to decide on that request in the light of the plausibility of those reasons, that is, "to assess the rules of EU law governing the division of powers between the EU and its Member States as well as the criteria for the attribution of their acts or omissions, in order to adopt a final decision in that regard which

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Opinion 2/13 on the Commission's proposal of an investment court system in the TTIP, on file with author; Schill, *supra* note 164 (discussing the implications of the opinion of the Court for investor-State arbitration).

172. *See* Opinion 2/13, *supra* note 171, at ¶¶ 179-200

173. *Id.* at ¶¶ 215-35.

174. *Id*. at ¶ 181.

175. *Id.* at ¶ 184

176. Article 3.1 amends Article 36 of the ECHR (adding a paragraph 4 which reads as follows: "The European Union or a member State of the European Union may become a co-respondent to proceedings by decision of the Court in the circumstances set out in the Agreement on the Accession of the European Union to the Convention for the Protection of Human Rights and Fundamental Freedoms. A co-respondent is a party to the case. The admissibility of an application shall be assessed without regard to the participation of a co-respondent in the proceedings."). *See* COUNCIL OF EUROPE, FIFTH NEGOTIATION MEETING BETWEEN THE CDHH AD HOC NEGOTIATION GROUP AND THE EUROPEAN COMMISSION ON THE ACCESSION OF THE EUROPEAN UNION TO THE EUROPEAN CONVENTION ON HUMAN RIGHTS (June 10, 2013), http://www.coe.int/t/dghl/standardsetting/hrpolicy/Accession/Meeting_reports/47_1(2013)008rev2_EN.pdf.

would be binding both on the Member States and on the EU."[177] It is precisely such review that would "interfere with the division of powers between the EU and its Member States."[178]

Moreover, the Court stressed the need to respect the principle of prior involvement, according to which the CJEU must review the compliance of EU measures with international obligations before an external body from the standpoint of both the validity and interpretation of EU primary and secondary law.[179] As noted by the Court in its 2/13 Opinion, the draft agreement does not contain an explicit prohibition, imposed upon the ECtHR, to interpret the case law of the CJEU where the latter has already given a ruling on the same question of law as that at issue in the proceedings before the ECtHR. In other words, the agreement could be interpreted as giving the ECtHR – rather than the CJEU – the power to rule on such a question.[180] This implies that, in order for the agreement to be in compliance with the prior involvement principle, a provision must be inserted "in such a way as to ensure that, in any case pending before the ECtHR, 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 that case and, if it has not, to arrange for the prior involvement procedure to be initiated."[181]

Another issue raised in the 2/13 Opinion concerned the compatibility of the procedure set up in the agreement with EU law from the point of view of the scope of the CJEU's jurisdiction. As clarified in the draft explanatory report of the agreement, Article 3(6) is intended to enable the CJEU to assess the compatibility of a provision of EU law with the ECtHR, meaning, in essence, that the Court can rule only on the "validity of a legal provision contained in secondary law or on the interpretation of a provision of primary law."[182] From this, it follows that the agreement "excludes the possibility of bringing a matter before the Court of Justice in order for it to rule on a question of interpretation of secondary law by means of the prior involvement procedure," with the ultimate result that if "the

177. *See* Opinion 2/13, *supra* note 171, at ¶ 224.
178. *Id.* at ¶ 225.
179. *Id.* at ¶¶ 236-48.
180. *Id.* at ¶¶ 238-40.
181. *Id.* at ¶ 241.
182. *Id*. at ¶ 242.

Court of Justice were not allowed to provide the definitive interpretation of secondary law, and if the ECtHR. . . . had itself to provide a particular interpretation from among the plausible options," there would most certainly be "a breach of the principle that the Court of Justice has exclusive jurisdiction over the definitive interpretation of EU law."[183]

2. Applicable Law, Prior Involvement and the Allocation of Powers between the EU and its Member States

The various constraints identified by the CJEU in Opinion 2/13 with regard to the applicable law, the division of powers between the EU and its Member States, and the principle of prior involvement may extend beyond the relationship with the ECtHR, and thus represent a serious obstacle to the operation of other kinds of dispute resolution mechanisms, including investor-State arbitral tribunals. This is clear by looking at the Commission's Concept Paper on the TTIP of May 2015, mentioned above, which observed that the agreement should make it clear that: (a) "the application of domestic law does not fall under the competence of ISDS tribunals"; (b) "domestic law can be taken into account by ISDS tribunals only as factual matter"; and (c) "any interpretations of domestic law made by ISDS tribunals are not binding on domestic courts."[184]

According to the Commission, therefore, the autonomy of the EU legal order – namely of the CJEU – could be guaranteed only if arbitral tribunals were required to apply international law (that is, both the provisions of the agreement and other rules of international law applicable to the parties) rather than the law of the host State. It should be noted that in this context, the "law of the host State" means national *and* EU law, since the latter prevails over and is part of the former. In this light, the exclusion of EU law from the scope of jurisdiction of arbitral tribunals is at odds with a general, consolidated trend in international investment law, which regards domestic law as part of the sources of law applicable to investment disputes.[185] Thus,

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183. *Id.* at ¶ 246.

184. *See* Commission Concept Paper, *supra* note 10, ¶ IV.3.

185. *See generally* HEGE ELISABETH KJOS, APPLICABLE LAW IN INVESTOR-STATE ARBITRATION: THE INTERPLAY BETWEEN NATIONAL AND INTERNATIONAL LAW (2013); Ole Spiermann, *Investment Arbitration: Applicable Law*, *in* INTERNATIONAL INVESTMENT LAW 1373-90 (Marc Bungenberg, Jörn Griebel, Stephan Hobe, & August Reinisch eds., 2015) (writing on the applicable law in investor-State arbitration from the standpoint of the

from the Commission's Concept Paper it can be inferred that any matters that are relevant to the review of the claim brought under the agreement, but which are not directly governed by it, will fall outside the tribunals' jurisdiction. If relevant, the interpretation of national and EU law will be examined only as a factual matter and will follow the prevailing approach taken by domestic courts and authorities; the legality of EU or Member States' measures under EU or national law will not be reviewed. However, it is unclear what the role of the arbitral tribunals and their task of "taking into account" domestic (national and EU) law as "factual matter" actually involves. Is it plausible to believe that in order to apply the provisions contained in the agreement, no interpretation of national and/or EU law in the context of a proceeding before arbitral tribunals will be necessary? Will arbitral tribunals retain the competence to allocate powers between the EU and the Member States? In other words, will they have jurisdiction to attribute responsibility for acts or omissions that allegedly constitute a violation of the rights of an investor and, therefore, to identify the respondent in the case (i.e. the EU and/or the State)? Of course, these questions apply *mutatis mutandis* also to the 2015 TTIP Proposal, which replaces arbitral tribunals and ISDS clauses with ICS mechanisms, as well as to CETA 2016 and the EU-Vietnam FTA. Furthermore, the assonances between the tribunals envisaged by both agreements and the ECtHR for being both permanent institutions are certainly more striking than those between the ECtHR and investor-State arbitration. This means that as the relationship between the ECtHR and the CJEU was found problematic by the CJEU, the same may happen with regard to the relationship between the latter and permanent investment tribunals.

With respect to the role of EU law in the reasoning of investment tribunals, it must be observed, as a preliminary consideration, that third-country investors usually seek to challenge EU and Member States' acts and obtain monetary compensation. That being said, when we consider that an investment tribunal must assess whether a provision of a FTA has been infringed by a Member State or the EU, it is difficult to imagine how it could possibly do so without

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relationship between domestic and international law); Collins C. Ajibo, *The Governing Law in Investor State Arbitration: the BIT, International Law, and Choice of Law Clause*, INT'L ARB. L. REV. 125 (2015).

interpreting national and/or EU primary and secondary law.[186] Indeed, investment tribunals and the CJEU may have competing jurisdiction with regard to issues of EU law to be applied to the dispute rather than to the particular circumstances of the dispute itself.[187] The argument that investment tribunals, in examining the measures adopted by the EU and its Member States, should treat EU law as a matter of fact rather than law and confine themselves to a merely incidental role is unconvincing. In fact, an accurate analysis of EU law is an essential function to be performed by investment tribunals and, *de facto*, a precondition for assessing the compatibility of an EU or national legal act with the agreement.[188] Although the jurisdiction of an investment tribunal is restricted to the adjudication of a particular dispute and, therefore, to the interpretation and application of the specific free trade and investment agreement, the assessment on the protection of investment standards may, by its very nature, have an impact on a number of EU policies such as those relating to the internal market, competition and trade-related matters (the environment, public health, labor, etc.). Furthermore, it is possible that investment tribunals will give a different and broader definition of "investment" and "investor" than that under EU law, resulting in foreign companies relying on the standards contained in the

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186. *See* Von Papp, *supra* note 165, at 1040 (citing Eureko B.V. v. The Slovak Republic, Award on Jurisdiction, Arbitrability, and Suspension, PCA Case 2008-13 (Oct. 26, 2010), para. 290) ("While arbitral tribunals tend to stress that their jurisdiction is limited to alleged breaches of the relevant BIT, this does not mean that questions of EU law remain outside the reach of their jurisdiction."); *Contra* Schill, *supra* note 164, at 384-387; Stephan Schill, *Luxembourg Limits: Conditions for Investor-State Dispute Settlement Under Future EU Investment Agreements*, TRANSNAT'L DISP. MGMT. 11 (2013), https://www.transnational-dispute-management.com/article.asp?key=1943; Angelos Dimopoulos, *The Involvement of the EU in Investor-State Dispute Settlement: A Question of Responsibilities*, COMMON MKT. L. REV. 1671, 1699-1700 (2014) [hereinafter The Involvement of the EU in Investor-State Dispute Settlement].

187. *See* Von Papp, *supra* note 165, at 1040.

188. *See* Inge Govaere, *Beware the Trojan Horse: Dispute Settlement in (Mixed) Agreements and the Autonomy of the EU Legal Order*, *in* MIXED AGREEMENTS REVISITED 192 (Christophe Hillion, & Panos Koutrakos eds., 2010); Steffen Hindelang, *The Autonomy of the European Legal Order: EU Constitutional Limits to Investor-State Arbitration on the Basis of Future EU Investment-Related Agreements*, *in* COMMON COMMERCIAL POLICY AFTER LISBON: EUROPEAN YEARBOOK OF INTERNATIONAL ECONOMIC LAW 1387-98, 194-95 (Marc Bungenberg, & Christoph Herrmann eds., 2013); H. LENK, *Investor-state arbitration under TTIP. Resolving investment disputes in an (autonomous) EU legal order*, SIEPS 2015:2 (2015), http://www.sieps.se/sites/default/files/Sieps%202015_2%20web.pdf.; Schill, *supra* note 164, at 37–54.

investment agreement before the international tribunals (but not before the CJEU).

The breach of the CJEU's interpretive monopoly is significant not only because the Court could lose its exclusive jurisdiction to interpret and apply EU law, but also because the awards rendered by the tribunals, stemming directly from jurisdictional institutions established by the international agreement, have a binding nature; in order to be effective, the awards must be respected by domestic courts, including the CJEU.[189] This applies also to CETA 2016, where it is stated in Article 8.41 that "[a]n award issued pursuant to this Section shall be binding between the disputing parties and in respect of that particular case" and additionally that "a disputing party shall recognise and comply with an award without delay."

Since international agreements are binding on the Member States and EU institutions pursuant to Article 216.2 TFEU,[190] being "an integral part of the EU legal order"[191] and in a primacy status vis-à-vis secondary law (but not vis-à-vis the EU treaties), the CJEU must interpret EU law in accordance with those agreements and the awards delivered by the tribunals established therein.[192] Moreover, as investment awards are enforced in conformity with either the New York Convention or ICSID Convention, it is impossible for the EU to respect international obligations related to the enforcement of the awards and simultaneously to prevent their implementation in the EU legal order.[193] What has been noted with regard to intra-EU BITs holds true also in the case of extra-EU agreements: an interpretation of EU law that is not in compliance with an investment award will probably induce foreign investors to bring a claim before the investment tribunal and potentially lead to exorbitant requests for compensation. Moreover, the lack of permanence and the absence of an official doctrine of precedence of arbitral tribunals may attenuate the constraints vis-à-vis the CJEU while creating additional problems of consistency that may endanger the relationship between the

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189. *See generally* JULIEN FOURET, ENFORCEMENT OF INVESTMENT TREATY ARBITRATION AWARDS: A GLOBAL GUIDE (2015).

190. "Agreements concluded by the Union are binding upon the institutions of the Union and on its Member States."

191. *See Haegeman*, *supra* note 60, [1974] E.C.R 449; Case C-366/10 Air Transport Association of America v. Secretary of State for Energy and Climate Change, Case C-366/10, [2011] E.C.R. I-0000, ¶ 50.

192. For more on the Consistent Interpretation Doctrine, see *supra* note 76.

193. LENK, *supra* note 188, at 45.

tribunals and the EU legal order.[194] In this respect, it remains to be seen whether the establishment of permanent tribunals foreseen in CETA 2016 and in the EU-Vietnam FTA will justify a new perspective on the scope and legal force of the awards once they become operational. Specifically, a reading of Article 8.41 of CETA 2016 which limits the binding effect of the award to that "particular case" and between the disputing parties seems to exclude radical changes to this effect[195]. However, the 2015 TTIP Proposal[196] does not include such a self-restraint dimension of investment awards, from the point of view of their enforcement, as there is no reference to the particular case or dispute.

The above analysis implies that a mechanism of prior involvement of EU institutions, including the CJEU, is needed. Obviously, such a mechanism should not be equivalent to that envisaged in the draft accession agreement to the ECtHR, which has already been struck down by the CJEU. It could be inspired by it, though. Should an EU provision be interpreted in order for an investment tribunal to adopt a decision, the CJEU would be primarily enabled to interpret it and/or assess its validity in light of the FTA. The difference with the procedure set up in the draft accession agreement would be that primary law and secondary law provisions could be subjected to the interpretation of the Court. This could be the right way to avoid a negative response from the CJEU should an opinion on the compatibility of the FTA with EU law be requested pursuant to Article 218(11) TFEU. In this regard, unless amended, the application *sic et sempliciter* of Article 267 TFEU (i.e., of a preliminary ruling procedure started by the investment tribunal and subject to such provision) does not seem to be the right solution since it lays down two cumulative conditions. First, investment tribunals should qualify as "tribunals" or "courts," and second, in the exercise of their public authority, they should be considered as judicial bodies "of the Member States."[197] Regarding the first condition, as far as the permanent dispute settlement system foreseen in CETA 2016 and in the FTA with Vietnam is concerned, there do not seem to be

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194. *But see* Jürgen Basedow, *EU Law in International Arbitration: Referrals to the European Court of Justice*, J. INT'L ARB. 367, 379 (2015) (considering arbitration panels permanent "in an institutional sense since ICSID is a permanent arbitration institution").

195. See in the same vein Article 31(1), Ch. 8, of the EU-Vietnam FTA, *supra* note 3.

196. 2015 TTIP Proposal, *supra* note 3, Article 30(1).

197. *See* TFEU, *supra* note 31, art. 267(b), 2012 O.J. C 326/47, at 164.

insuperable obstacles for the application of Article 267 TFEU. As to arbitral tribunals, the CJEU held that commercial arbitrators fall outside the scope of Article 267 TFEU.[198] Nevertheless, it should be stressed that investor-State arbitration covers disputes between a State and an investor rather than between private parties (as in commercial arbitration). As a consequence, some commentators have rightly argued that the Court's reasoning cannot be transferred *tout court* to this system.[199] The issue raised by the second condition, however, is more serious. Simply considering the possibility of meeting this condition means assuming that the agreement concerned is a mixed agreement – that is, one concluded by the EU and the Member States. Whether or not that is the case, it is hard to find a strong basis in the CJEU's case law[200] for arguing that, in the context of EU agreements, investment tribunals can be considered judges of a Member State.[201]

Another important issue arises from the analysis of the opinions rendered by the CJEU on a number of agreements containing procedures similar to that envisaged in Article 267 TFEU.[202] According to the CJEU, national judges must be considered "ordinary" within the EU legal order and entrusted with the task of implementing EU law; as such, they cannot be replaced by international tribunals.[203] As clarified in Opinion 1/09, Article 267 TFEU provides for the power or obligation of national courts to refer questions on the interpretation and validity of EU law so as to ensure its harmonious interpretation and application across the Union.[204] Based on the CJEU's case law, one can thus envisage the possibility

198. Nordsee Deutsche Hochseefischerei GmbH v. Reederei Mond Hochseefischerei Nordstern AG & Co. KG, Case 102/81, [1982] E.C.R. 1095.

199. Steffen 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*, 39 LEGAL ISSUES ECON. INTEGRATION 179, 202 (2012) [hereinafter Circumventing Primacy of EU Law]; Von Papp, *supra* note 165, at 1058-60.

200. Paul Miles and Others v. Écoles Européennes, Case C-196/09 [2011] E.C.R. I-5139.

201. *See also* Bermann, *supra* note 28, at 406; Burgstaller, *supra* note 166, at 219-20. *Contra* Jürgen Basedow, *supra* note 194, at 378-81; Dimopoulos, *Compatibility of Future EU Investment Agreements*, *supra* note 161, at 469; *see also* Genentech, Inc. v. Hoechst GmbH & Sanofi Aventis Deutschland GmbH, Case C-567/14, EU:C:2016:177, ¶ 59, n.34.

202. *See* Opinion 1/91, *supra* note 162, at 11, 54-65; Opinion 2/92, *supra* note 162, at 11, 37; Opinion 1/09, *supra* note 162, at 12.

203. *See* Opinion 1/09, *supra* note 162, at ¶ 80.

204. *See* Tobias Lock, *Taking National Courts More Seriously? Comment on Opinion 1/09*, 4 EUR. L. REV. 576 (2011) (commenting on the impact of the Opinion on the status accorded to national courts).

of a mechanism similar to that foreseen in Article 267 TFEU only upon the condition that the reference to a "judge of a Member State" will be ruled out provided that investment tribunals are subject to the binding opinions rendered by the CJEU upon their request.

An alternative to Article 267 TFEU, to be inserted in the FTAs, therefore, may be a solution only if it will not replicate all weaknesses that have been already found inconsistent with EU law by the CJEU in its jurisprudence.

Having discussed the question of the applicable law and the need for a mechanism of prior involvement, the matter of the allocation of powers between the EU and Member States must be now addressed. In this regard, the relevant and applicable legal source that would allow identification of the respondent to an action brought by an investor is Regulation 912/2014.[205] As is well known, this act provides a framework for managing financial responsibility linked to investor-to-State dispute settlement tribunals established by international agreements to which the EU is a party in case of investment disputes brought by foreign investors.[206] The European Commission, in consultation with the Member State, undertakes identification of the respondent in case of disagreement; it is for the CJEU to determine the allocation of responsibility between the EU and Member States. However, Article 19 of the Regulation, which regulates cases where no agreement is reached, does not make any reference to the CJEU. This remains an issue to be clarified by EU institutions; other aspects need to be addressed through rules in mixed EU free trade and investment agreements so that the regulation may be complemented and rendered more effective.[207] It remains to be seen what the CJEU will state in its future opinion on the FTA with Singapore since its findings will be relevant to other agreements as well.[208] Alternatively, the CJEU could be called upon to give a

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205. *See* Directive 2014/912 art. 6 and art. 9 of the European Parliament and of the Council on Establishing a Framework for Managing Financial Responsibility Linked to Investor-to-State Dispute Settlement Tribunals Established by International Agreement to which the European Union is a party, 2014 O.J. L. 257/127.

206. *See* Dimopoulos, *The Involvement of the EU in Investor-State Dispute Settlement*, *supra* note 186; Jan Kleinheisterkamp, *Financial Responsibility in European International Investment Policy*, INT'L & COMP. L. QUARTERLY 499 (2014).

207. *See* Dimopoulos, *Compatibility of Future EU Investment Agreements*, *supra* note 161; Schill, *supra* note 164 (highlighting that the Statement submitted by the European Communities to the Secretariat of the Energy Charter pursuant to Article 26(3)(b)(ii) of the Energy Charter Treaty, OJ L 69, 115 (9 March 1998)).

208. *See supra* note 8.

separate opinion for each agreement. What seems certain, however, is that the system established in the Regulation imposes on foreign investors the obligation to undergo proceedings that are lengthier and more complex than those envisaged for EU investors. Moreover, with regard to the allocation of competences between the EU and Member States, we can only wait and see whether third-country negotiators will be open to accepting the involvement of EU institutions (the CJEU in particular) in the course of investment proceedings.

A final point must be made with respect to the operation of the principle of autonomy, and particularly the question of whether and how CETA 2016, the EU-Vietnam FTA and the 2015 TTIP Proposal take into account the need to safeguard and comply with said principle.

As a preliminary remark, it is clear that the Commission considered Opinion 2/13 in drafting the 2015 TTIP Proposal, which lays as a model for both CETA 2016 and the EU-Vietnam FTA. Regarding the allocation of responsibility between the EU and its Member States, the Proposal provides that the claimant must request that the EU determine who is the respondent – the EU or one of its Member States. A similar provision is contained in CETA 2016 and the EU-Vietnam FTA.[209] By affirming this, the Commission prevents the Tribunal from carrying out this assessment solely in line with the customary rules on State responsibility.[210] The relevant act would be Regulation 912/2014; it will be up to the Commission, in consultation with the Member State, to determine which entity will act as the respondent. From this point of view, therefore, there are no particular obstacles to the establishment of investor-State adjudication.

From the TTIP Proposal, it also emerges that the Commission was well aware of the Court's findings in Opinion 2/13 with regard to the need to respect its interpretive monopoly. Indeed, a number of articles contained in the Proposal restrict the investment tribunals' reliance on applicable law to international law, to the exclusion of national and EU law. In exercising its jurisdiction, the Tribunal can apply the TTIP and other rules of international law applicable between the parties, but not domestic law.[211] Where relevant, the interpretation of domestic law can be assessed "as a matter of fact"

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209. *See* CETA, *supra* note 3, art. 8.21; EU-Viet. Free Trade Agreement, Ch. II of Ch. 8, Sect. 3, *supra* note 3, art. 6.

210. *See* Fontanelli, *supra* note 171.

211. *See* 2015 TTIP Proposal, *supra* note 3, arts. 13.2-13.3.

and must follow the prevailing interpretation of the domestic courts and authorities.[212] Moreover, the Proposal states that the Tribunal's interpretation of domestic law will not be binding upon domestic authorities and that they will not review the legality of State measures under domestic law.[213] Thus, in allowing the assessment of domestic (national and EU) law only as a matter of fact, the Commission followed the approach outlined in its Concept Paper of May 2015, in relation to which we have already expressed our doubts. Moreover, the Commission affirms that the tribunals may be "required to ascertain the meaning" of provisions of national law.[214] Considering investment tribunals cannot interpret EU law (if they did, they would breach the principle of the autonomy of the EU legal order), the sentence is obscure. It seems difficult, if not impossible, to draw a distinction between "ascertaining the meaning" of and "interpreting" a given provision. Again, it is hard to believe that a tribunal will or should not closely examine a provision of national or EU law in order to rule on the TTIP. In any event, relying on a supposed dividing line between "interpretation" and "application" does not appear decisive. If it is true that "interpretation" means determining the meaning of particular provisions of an agreement while "application" refers to the conformity of certain actions taken by the State(s) with the terms of that agreement, it is equally true that the application always involves interpretation which, vice versa, generally (but not always) leads to an application of the law.

Finally, it must be pointed out that the Proposal does not address the question of prior involvement precisely because it intends to solve the question of the autonomy of the EU legal order and the CJEU in the interpretation of the treaties and secondary law *ex ante*, that is, by excluding domestic law from the applicable law. It follows that the problem with this exclusion lies in the fact that since most investor-State cases will need an interpretation of EU law, the lack of a mechanism aimed at ensuring a sound interpretation of EU law by the CJEU – and thus compliance with the treaties – is capable of jeopardizing the feasibility of the entire proposal.

Which of the above elements has been transposed in CETA 2016 and in the EU-Vietnam FTA? The great majority of them: while the reference to the ascertainment of the meaning of domestic law's

212. *Id.*
213. *Id.* at 13.4.
214. *Id.* at 13.2.

provisions has been ruled out, the idea that EU law shall be excluded from the applicable law has been strictly followed. The same holds true for all corollaries attached to the narrowing of the applicable law's scope and extent: (1) the treaty and international law rules and – this is a novelty compared to the Proposal – principles are the only applicable sources of law, and (2) domestic law may be interpreted only as a matter of fact.[215] This means that the criticalities mentioned above on the lack of a system of prior mechanisms apply all the same. Moreover, as foreseen in CETA 2016 and in the EU-Vietnam FTA, the establishment of an appellate tribunal entrusted with a number of tasks aimed at reviewing awards the lower tribunal renders might complicate matters. Indeed, it is stated that the appellate tribunal may "uphold, modify or reverse a Tribunal's award based on (a) errors in the application or 'of applicable law' and on (b) manifest errors in the appreciation of the facts, including the appreciation of relevant domestic law."[216]

In light of the above, the question of the incompatibility of a system of investor-State dispute settlement with the principle of autonomy must be taken seriously, because investment tribunals are *naturally* required to interpret EU law whether directly or indirectly (not simply incidentally) in order to assess the conformity of measures adopted by Member States or the EU with the agreement (and, more generally, international law). While the issue of the distribution of responsibility between national authorities and the EU could be solved by the application of Regulation 912/2014, a new mechanism of prior involvement of the EU, namely the CJEU and/or the European Commission, is needed. A mechanism inspired by the preliminary procedure envisaged in Article 267 TFEU but different than the latter in a number of aspects, as it has been already pointed out, might prevent investment tribunals from curtailing the exclusive jurisdiction of the CJEU. Needless to say, this can be an adequate solution only if the Court's opinion will be regarded as binding upon the investment tribunals in the engagement with EU law. As previously mentioned, a softer alternative would institutionalize the intervention of the European Commission as an *ex ante* privileged interpreter of EU law before the said tribunals.

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215. *See* CETA, *supra* note 3, art. 8.31, at ¶ 1-2.; EU-Viet. Free Trade Agreement, Ch. II of Ch. 8, Sect. 3, *supra* note 3, art. 16, ¶ 2.

216. *See* CETA, *supra* note 3, art. 8.28, at ¶ 2; EU-Viet. Free Trade Agreement, Ch. II of Ch. 8, Sect. 3, *supra* note 3, art. 13, ¶ 2.

Another solution could be to opt for a procedure that follows the legal framework set up by the Agreement on the European Economic Area ("EEA Agreement") vis-á-vis the relationship between the European Free Trade Association ("EFTA") Court and the EU,[217] and draw from it possible solutions for ensuring the respect of the principle of autonomy in relation to the functioning of the investment tribunals established by free trade and investment agreements. The EEA Agreement, along with its annexes and protocols, contains a number of provisions aimed at preventing conflicts with the EU legal order. A system of continuous exchange of information between EFTA, EEA and EU institutions is established, including between the EFTA Court and the CJEU. From a jurisdictional viewpoint, the EEA Agreement puts in place a system aimed at preserving a homogeneous interpretation of the Agreement, i.e. at ensuring that EU law and the CJEU's case law are not contradicted by the EFTA Court.[218] In this respect, an important tool envisaged in the Statute and the Rules of Procedure of the EFTA Court is represented by the role assigned to the European Commission. From a joint reading of Article 36 of the EFTA Court Statute and Article 89 of the Rules of Procedures, it can be inferred that the Commission has both *jus standi* and *jus locus standi in judicio* before the EFTA Court. So far the Commission has always submitted its written observations in the disputes before the Court, and as a result has exerted a strong influence on the case law tendencies of the latter. Regarding investor-State proceedings, a possible strategy aimed at protecting the autonomy of EU law could be to institutionalize the intervention of the Commission for all disputes so that it may act as a privileged (and authentic) interpreter of EU law in all cases brought before the tribunal when interpreting EU law is the precondition for the settlement of a dispute. Of course, it remains to be seen whether the CJEU would accept this mechanism, considering that in this case the Commission (rather than the Court)

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217. *See* Daniele Gallo, *From Autonomy to Full Deference in the Relationship between the EFTA Court and the ECJ: The Case of the International Exhaustion of the Rights Conferred by a Trademark* 4, (Eur. U. Inst, Working Paper No. 78, 2010); *see generally* Agreement on the European Economic Area, 1994 O.J. L 1 [hereinafter EEA Agreement].

218. The principle/objective of "legal homogeneity" is envisaged in paragraphs 4 and 15 of the Preamble and in Articles 1, 6, 105, 106, 107, 111 of the EEA Agreement, *supra* note 217, 1994 O.J. L 1, and in Article 3, paragraph 1 of the Agreement Between the EFTA States on the Establishment of a Surveillance Authority and a Court of Justice, 1994 O.J. L 344, according to which EEA law aims at creating a dynamic and homogeneous area by extending EC rules—EU rules as foreseen by the Treaty of Lisbon—to a wider regional context.

would exercise the interpretative monopoly. It is clear that the introduction of a prior involvement of the CJEU or the Commission in the interpretation of EU law would lead or, *de facto,* force the EU institutions to grant a similar right to the EU's co-contracting parties, or better, their constitutional or supreme courts.[219]

In conclusion, there seems to be another legal tool to be used in order to safeguard the principle of EU autonomy. In the 2015 TTIP Proposal,[220] as well as in the CETA 2016[221] and in the EU-Vietnam FTA[222] it is stated that Parties (the EU and its partners), through the committees provided therein, where serious concerns arise as regards matters of interpretation of provisions on investment protection and resolution of disputes, "may adopt decisions interpreting those provisions", which are binding on both the Tribunal and the Appeal Tribunal. This provision, therefore, cannot apply to a particular case brought before the permanent tribunals; yet it may apply *pro futuro* in order for the EU to clarify provisions to be applicable in settling disputes between investors and the Parties of the agreement so that conflicts with the EU legal order might be considerably reduced.

III. WHAT ROLE SHOULD STATE-TO-STATE ARBITRATION AND (GREATER) INCLUSIVE ADJUDICATION PLAY IN EU FREE TRADE AND INVESTMENT AGREEMENTS?

A. State-to-State Arbitration between Diplomatic Protection and Interpretive Claims and its Relationship with Investor-State Dispute Resolution Systems

We have explained why, in our opinion, State-to-State arbitration should not be the *only* remedy available under EU FTAs. As already noted, this does not mean that State-to-State arbitration ought to be abandoned and replaced by investor-State arbitration or permanent tribunals.[223] Rather, as argued below, its inclusion in EU agreements can only be beneficial. Therefore, this mechanism should be envisaged in addition to, and not as a replacement for, investor-State adjudication. As a consequence, this Section will also

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219. *See* Schill, *supra* note 164, at 386.

220. *See* 2015 TTIP Proposal, Ch. II, *supra* note 3, art. 13, ¶ 5.

221. *See* CETA, *supra* note 3, art. 8.31, ¶ 3.

222. *See* EU-Viet. Free Trade Agreement, Ch. II of Ch. 8, Sect. 3, *supra* note 3, art. 16, ¶ 4.

223. *See supra* Section I.A.

investigate possible strategies for ensuring an effective coordination between the two mechanisms in question. As it has been already noted in the previous Sections, this analysis, albeit being mostly devoted to investor-State arbitration, may apply also to CETA 2016 and EU-Vietnam FTA. "May" since there is no praxis at the international level through which identifying the rules governing the relationship between State-to-State arbitration and the functions performed by permanent tribunals. What can be inferred from the reading of both CETA 2016 and the EU-Vietnam FTA is that the *erga omnes* (*de jure* or *de facto*) effect of awards that are generally rendered by international permanent tribunals is excluded in both agreements, as mentioned in the previous Section.[224] In CETA 2016, for instance, it is laid down that "[a]n award issued pursuant to this Section shall be binding between the disputing parties and in respect of that particular case."[225] Therefore, as there seems not to exist relevant differences with the legal force of investor-State arbitration awards, the coordination mechanism concerning investor-State arbitration and inter-State arbitration may represent a source of inspiration, *mutatis mutandis*, also for agreements that envisage a system of permanent tribunals.

It must be pointed out that earlier BITs, modeled on Friendship, Commerce and Navigation Treaties, originally provided for State-to-State arbitration, while investor-State arbitration clauses began to be introduced only in later BITs.[226] More specifically, it was not until 1969, with the Chad-Italy BIT, that the first investor-State arbitration clause was included in a treaty, and not until 1990 that a tribunal asserted its jurisdiction in a dispute between an investor and a host State.[227] Indeed, diplomatic protection as conceived in the 1950s and 1960s was the only mechanism that allowed States to take action to protect their nationals on the level of (public) international law, a sphere from which, at the time, non-State actors were excluded by definition. Due to this exclusion, the system of adjudication of

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224. Article 30 of the 2015 TTIP Proposal, instead, follows a different approach. *See supra* Section II.B.

225. *See* CETA, *supra* note 3, art. 8.41, ¶ 1; EU-Viet. Free Trade Agreement, Ch. II of Ch. 8, Sect. 3, *supra* note 3, art. 31(1).

226. For an historical overview see Roberts, *supra* note 38, at 2-5. For an overview of inter-State dispute settlement systems contained in BITs, see Paul Peters, *Dispute Settlement Arrangements in Investment Treaties*, NETH. Y.B. INT'L L. 91, 102–17 (1991).

227. *See* NATHALIE BERNASCONI-OSTERWALDER, STATE–STATE DISPUTE SETTLEMENT IN INVESTMENT TREATIES: BEST PRACTICES SERIES—2014 1 (2014).

disputes of alien investors in a foreign State faced a serious problem that could only be resolved through the *fictio* of diplomatic protection, which, by treating a violation of the rights of a foreign national as a violation of the rights of their State of nationality, allowed the latter to vindicate that violation at the international level.[228]

Today, nearly all modern BITs include provisions that give access to two avenues of dispute resolution, each with a different scope of *ratione personae*: a State-to-State clause for disputes concerning the interpretation and/or application of the treaty, and an investor-State arbitration clause to be activated in case of a violation of the treaty by the host State if the investor concerned has suffered loss or damage as a result of the violation. A good example of a typical BIT State-to-State dispute settlement clause can be found in the 2012 US Model BIT, whose Article 37 reads: "any dispute between the Parties concerning the interpretation *or* application of this Treaty, that is not resolved through consultations or other diplomatic channels, shall be submitted on the request of either Party to arbitration for a binding decision or award by a tribunal in accordance with applicable rules of international law" (*emphasis added*).[229] Under many treaties, however, a State can initiate a claim against another State on matters concerning the "interpretation *and* application" of the treaty.[230] Thus, in case of disputes that have not been resolved through consultations or other diplomatic channels, claims may be brought to obtain an interpretation or, in the context of diplomatic protection, to seek the application of the treaty should a violation of any of its provisions be alleged by a contracting party and redress be sought by said party on behalf of its investors. While the purpose of diplomatic protection, like that of investor-State arbitration clauses,[231] is to protect nationals abroad (including investors) and obtain reparations for internationally wrongful acts, interpretive claims have a different goal. Rather than reparations and damages,

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228. Greg Lourie, *Diplomatic Protection Under the State-to-State Arbitration Clauses of Investment Treaties*, AUS. Y.B. INT'L ARB. 511, 511 (2015). For a general discussion of this theme see GIORGIO SACERDOTI, BILATERAL TREATIES AND MULTILATERAL INVESTMENTS ON INVESTMENT PROTECTION 261-65 (1997).

229. 2012 U.S. Model Bilateral Investment Treaty, art 37, ¶1, available at https://ustr.gov/sites/default/files/BIT%20text%20for%20ACIEP%20Meeting.pdf.

230. *See* German Model Bilateral Investment Treaty, art. 9, available at http://www.italaw.com/sites/default/files/archive/ita1025.pdf. On the notions of "interpretation" and "application" see Roberts, *supra* note 38.

231. *See* NATHALIE BERNASCONI-OSTERWALDER, *supra* note 227, at 3-4.

they simply seek clarification of the meaning and/or scope of treaty obligations – which is not always a precondition for determining a treaty breach.

As already emphasized above,[232] the boundaries between the concepts of "interpretation" and "application" are blurred as any dispute on the application of a treaty necessarily presupposes an interpretation of the provisions to be applied. However, although the application of a norm implies by its very nature the interpretation of that norm, the reverse, while relatively common, is not always the case. Indeed, the contracting parties to a treaty may well seek clarification of the meaning of one or more provisions that are unrelated to a specific situation or to a dispute regarding the violation of the treaty itself. Moreover, it should be noted for the sake of completeness that diplomatic protection claims are not the only type of claims that could be brought in connection with a dispute concerning the application of an investment treaty.[233] In fact, a State could seek purely declaratory relief, acknowledging that the other party has violated the agreement. This does not mean, however, that there is a clear-cut distinction between diplomatic protection and declaratory relief claims; when a State requests adjudication on alleged violations of the rights of its nationals committed by the other contracting party, the assessment and determination of whether the latter has breached its obligations under the treaty is an inevitable task to be performed.[234] For this reason, and since to our knowledge there is as yet no clear case law on claims for declaratory relief, our discussion will focus on the more crucial distinction between diplomatic protection and interpretive claims.[235]

With regard to both types of claims, it appears that despite being frequently provided for in modern-day BITs and FTAs, State-to-State arbitration has actually been used as a dispute resolution mechanism only in three cases: *Italy v. Cuba*[236] (a diplomatic protection claim

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232. *See* Roberts, *supra* note 38, at 3.

233. *See* Lourie, *supra* note 228, at 514.

234. *Id.*

235. In her discussion of declaratory relief claims, NATHALIE BERNASCONI-OSTERWALDER, *supra* note 227, at 15 (citing, among other cases, *Mexico v. United States* (in the Matter of Cross-Border Trucking Services), NAFTA Chapter 20 State-to-State Arbitration, Final Report of the Panel, February 6, 2001, paras. 15-24).

236. *See* Republic of Italy v. Republic of Cuba, Ad hoc Arbitration, Interim Award, 15 March 2005; see *also* Republic of Italy v. Republic of Cuba, Ad hoc Arbitration, Final Award, 15 January 2008; *see also* Michele Potestà, *Interstate Arbitration—Bilateral Investment*

concerning the application of the treaty), *Peru v. Chile,*[237] and *Ecuador v. United States*[238] (interpretive claims). Notwithstanding the small number of cases, it cannot be denied that the existence of these relatively recent disputes, as well as the current practice of States regarding investment dispute resolution systems provided for in BITs and FTAs, signals a trend towards a revaluation and re-emergence of State-to-State arbitration, given the concerns raised by investor-State arbitration. Indeed, some States have recently decided not to include an investor-State clause, opting instead for a State-to-State remedy.[239]

Turning now to an analysis of the European context and EU law, it is important to recall that no case concerning the agreements concluded by individual Member States with third countries has yet been decided under State-to-State dispute settlement provisions.[240] As for FTAs, containing investment chapters, that were negotiated so far, but not yet in force pending finalization of the text by the Commission, final approval by the Parliament and Council and/or completion of ratification procedures by Member States (such as, *inter alia*, CETA 2016,[241] FTA with Singapore,[242] and FTA with Vietnam[243]), it is possible to infer that they all contain a chapter on State-to-State arbitration, which is applicable also to investment disputes. In most agreements, indeed, it is specified that an investor of a contracting party may submit his claim against the host State "[w]ithout prejudice to the rights and obligations of the Parties" under the chapter on Dispute Settlement.[244] In light of this, it seems quite probable that other agreements under negotiation will provide for a

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Treaties—Diplomatic Protection—Exhaustion of Local Remedies—Definition of Investment, 106 AM. J. INT'L L 341 (2012); Giorgio Sacerdoti, & Matilde Recanati, *Approaches to Investment Protection Outside of Specific International Investment Agreements and Investor-State Settlement*, *in* INTERNATIONAL INVESTMENT LAW 1839-62 (Marc Bungenberg, Jörn Griebel, Stephan Hobe, & August Reinisch eds., 2015).

237. *See* Empresas Lucchetti, S.A. and Luchetti Peru, S.A. v. Republic of Peru, ICSID Case No. ARB/03/4, (Feb. 7, 2005).

238. *See* Republic of Ecuador v. U.S., PCA Case No. 2012-5 (Perm. Ct. Arb. 2012). See in particular, Jarrod Wong, *The Subversion of State-to-State Investment Treaty Arbitration*, 53 COLUM. J. TRANSNAT'L L. 6, 10-14, 27-30 (2014).

239. *See, e.g.,* Agreement Between Japan and the Republic of the Philippines for an Economic Partnership Agreement (2006) and Malaysia-Australia Free Trade Agreement (2012); *see also* BERNASCONI-OSTERWALDER, *supra* note 227, at 1.

240. *See Is Investor-State Dispute Settlement*, *supra* note 74, at 660.

241. *See* CETA, *supra* note 3, Ch. 29.

242. *See* EU-Singapore FTA, *supra* note 69, at Chapter 15.

243. *See* EU-Viet. FTA, *supra* note 3, at "Dispute Settlement."

244. *See* CETA, *supra* note 3, art. 8.18.

similar mechanism. Therefore, in line with the rule of customary international law[245] that a direct claim of an individual may co-exist with the right of his home State to espouse a claim, the EU has chosen not to regard the inclusion of an investor-State system of dispute settlement in FTAs as a means to rule out inter-State arbitration. This is certainly a reasonable choice, since a hybrid system that includes both remedies seems to be the best solution to reach a fair balance between the interests of the State and the investors, one which has the advantage of responding to the concerns that (more or less recently) have been raised in relation to investor-State arbitration.

There are several reasons why State-to-State arbitration – foreseen in addition to investor-State remedies – may offer a useful remedy for settling certain disagreements between the EU and its trade partners and/or, in general, for clarifying certain treaty provisions. With regard to claims brought in the context of diplomatic protection, it might be an appealing option for investors when they fear discrimination or retaliation by a host State if they initiate investor-State arbitration proceedings. In addition, small investors who wish to avoid the expenses of bringing a direct claim against the host State may prefer that their case be brought by their home State. This holds true especially when injuries concern numerous investors and could lead to class actions.[246]

A State-to-State dispute resolution system seems even more attractive for the EU, its Member States, third-country partners, and investors when we consider it from the view of interpretive claims. In this case, since what is at stake is the adjudication of a dispute between an investor and a host State on treaty provisions that are not directly connected with the application of substantive standards, the rationale for the inclusion of State-to-State arbitration rests on a number of observations. Rather than having a variety of rulings by different tribunals on specific investment disputes, the mechanism of State-to-State interpretive claims would ensure interpretive authority and thus make it possible to resolve uncertainties as to the meaning, scope, and extent of the rights and obligations of States towards one other and investors. These claims could be used by the EU institutions and/or EU Member States and treaty partners to shed light on the

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245. As stated in the Commentary to Article 16 of the International Law Commission's Draft Articles on Diplomatic Protection, "the customary international law rules on diplomatic protection and the rules governing the protection of human rights are complementary."

246. *See* Roberts, *supra* note 38, at 14-15.

content and limits of one or more provisions, especially where interpretation may potentially have an impact on numerous investors in the host State. In this perspective, State-to-State arbitration could help reduce the proliferation of far-fetched claims that have a limited chance of success. From the point of view of the host State, it could serve as a tool for determining whether a certain measure is compatible with the treaty: a single ruling would be a much better solution than facing multiple investment claims. Moreover, on interpretive claims, the EU and its partners should make clear in the agreements that the concept of "dispute" as a prerequisite for initiating State-to-State arbitration proceedings is to be understood in a broad sense, that is, as comprising both disagreement between the parties and silence or failure to respond to a request for a joint interpretation.[247] This seems necessary especially in light of recent case law, namely the *Ecuador v. United* States[248] ruling, in which the tribunal observed that there was no "dispute" because there was no "positive opposition" by a party against another on the interpretation of the treaty.[249]

Regarding the more operational yet crucial issue of how best to ensure an effective coordination between investor-State arbitration and State-to-State arbitration[250] in EU free trade and investment

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247. *See also* Clovis J. Trevino, *State-to-State Investment Treaty Arbitration and the Interplay with Investor–State Arbitration Under the Same Treaty*, 5 J. INT'L DISP. SETTLEMENT, 2014, 199, 202-04. On the ambiguous meaning of "dispute," *see* Christoph Schreuer, *What is a Legal Dispute?*, *in* INTERNATIONAL LAW BETWEEN UNIVERSALISM AND FRAGMENTATION: FESTSCHRIFT IN HONOUR OF GERHARD HAFNER 959-60 (Isabelle Buffard, James Crawford, Alain Pellet, & Stephan Wittich eds., 2008).

248. *See* Republic of Ecuador v. United States of America (PCA Case No. 2012-5), http://www.italaw.com/cases/1494#sthash.R0ecUZCV.dpuf.

249. *See* Jarrod Hepburn & Luke Eric Peterson, *US-Ecuador Inter-State Investment Treaty Award Released to Parties; Tribunal Members Part Ways on Key Issues*, INV. ARB. REP. (Oct. 30, 2012), https://www.iareporter.com/articles/us-ecuador-inter-state-investment-treaty-award-released-to-parties-tribunal-members-part-ways-on-key-issues/.

250. On such relationship, see Michele Potestà, *State-to-State Dispute Settlement Pursuant to Bilateral Investment Treaties: Is There Potential?*, *in* INTERNATIONAL COURTS AND THE DEVELOPMENT OF INTERNATIONAL LAW 761-65 (Nerina Boschiero, Tullio Scovazzi, Cesare Pitea, & Chiara Ragni eds., 2013); Michele Potestà, *Towards a Greater Role for State-to-State Arbitration in the Architecture of Investment Treaties?*, *in* THE ROLE OF THE STATE IN INVESTOR-STATE ARBITRATION 264-71 (Shaheeza Lalani & Rodrigo Polanco Lazo eds. 2015) [hereinafter *Towards a Greater Role For State-to-State Arbitration*]; Ben Juratowitch, *supra* note 38, at 22-35 (2008); Chang-fa Lo, *Relations and Possible Interactions between State-State Dispute Settlement and Investor-State Arbitration Under Bits*, 6 CONTEMP. ASIA ARB. J. 1, 10-26 (2013); Greg Lourie, *supra* note 228; BERNASCONI-OSTERWALDER, *supra* note 227; Roberts, *supra* note 38; Trevino, *supra* note 247.

agreements,[251] it should be noted that there are neither precise rules under customary law nor general investment treaties that give a clear indication of how the two mechanisms interrelate.[252] Clear solutions are even less feasible when innovative, permanent investor-State dispute settlement systems are at stake. As anticipated above, the analysis will be focused, in particular, on investor-State arbitration in their interplay with State-to-State arbitration.

Most BITs do not contain any provision on the interplay between State-to-State arbitration and investor-State arbitration and are silent as to whether the latter should be prioritized over the former.[253] Moreover, it is important to point out that the rule of exhaustion of local remedies, defined by the International Court of Justice as a "well-established rule of customary international law,"[254] applies within the framework of inter-State arbitration only in the case of a diplomatic protection claim.[255] Indeed, the rule does not have the status of customary law with respect to other inter-State claims.[256]

Although we cannot speak of a potential conflict between State-to-State arbitration and investor-State arbitration, or of competing jurisdiction in the strict sense (the "disputes" are not the same; they are between different parties, have different objects, and are based on different legal grounds), the lack of clear rules on their interaction may entail a number of tensions between parallel or subsequent proceedings and lead to inconsistency due to conflicting decisions. In order to avoid such tensions, it is our belief that EU FTAs should contain rules to govern the proceedings.

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251. Although outside the scope of this article, an interesting issue is that of recourse to WTO law as a new form of diplomatic protection in parallel with investment arbitration. *See* Titi, *supra* note 32, at 265-87.

252. *See* Lo, *supra* note 250, at 4. *But see* Article 13.12 of the China-New Zealand BIT, Agreement between the Government of New Zealand and the Government of the People's Republic of China on the Promotion and Protection of Investments, Nov. 22 1988, 1787 UNTS 186.

253. *Contra* Wong, *supra* note 238, at 13-14, 33-48.

254. Interhandel (Switzerland v. United States of America), Judgment of March 21, 1959, ICJ Rep 6, at 25.

255. As demonstrated by the award rendered by the Tribunal in Republic of It. v. Republic of Cuba, Sentence P**r**éliminaire, [Interim Award] (Ad Hoc Arb. Trib. Mar. 15, 2005) (Fr.); Republic of It. v. Republic of Cuba, Sentence finale [Final Award] (Ad Hoc Arb. Trib. Jan. 15, 2008) (Fr.).

256. *See also* Potestà, *State-to-State Dispute Settlement Pursuant to Bilateral Investment Treaties: Is There Potential?*, *supra* note 250, at 252-53, 259-64.

In order to address the matter of coordination,[257] the timing of the inter-State remedial channel *vis-à-vis* the investor-State proceedings should be taken into account.[258] In its turn, this factor must be considered in relation to another crucial element: the nature of the claim as diplomatic protection or interpretive.[259]

With regard to diplomatic protection claims, it is our opinion that agreements should include a provision modeled on Article 27(1)[260] of the ICSID Convention,[261] which reads:

> No Contracting State shall give diplomatic protection, or bring an international claim, in respect of a dispute which one of its nationals and another Contracting State shall have consented to submit or shall have submitted to arbitration under this Convention, unless such other Contracting State shall have failed to abide by and comply with the award rendered in such dispute.[262]

Put differently, this means that if an investor has consented to submit or has already submitted a dispute by using the investor-State mechanism, the investor's home State may not initiate a State-to-State diplomatic protection claim unless the host State fails to abide by the arbitral award. Thus, this provision would protect the host State from the risk of multiple simultaneous claims. As for cases where the investor-State award has already been rendered, the provision should specify that the investor's home State may not institute State-to-State

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257. On the relevance of the good faith principle, see Lo, *supra* note 250.

258. *Contra* Wong, *supra* note 238, at 35-46. The author maintains the priority of investor-State arbitration over State-to-State arbitration. In particular, he argues that the two arbitral regimes should be treated as mutually exclusive, precluding State-to-State arbitration of any dispute that may be properly resolved through investor-state arbitration.

259. *See* Potestà, *Towards a Greater Role for State-to-State Arbitration, supra* note 250; *see also* Roberts, *supra* note 38, at 66-68 (analyzing claims for declaratory relief); Lourie, *supra* note 228, at 515.

260. For an analysis of this provision in light of the most recent case law, see Wong, *supra* note 238, at 30-35.

261. Of course, if the parties to the agreement chose the ICSID framework, the problem would be solved *ex ante*, whereas if they chose UNICTRAL or other systems which lack a provision similar to Article 27, that would lead to considerable uncertainty. This is why the best solution seems to be the insertion of a norm that regulates the matter. As foreseen in CETA, *supra* note 3, art. 8.23, ¶ 2: "A claim may be submitted under the following rules: the ICSID Convention; the ICSID Additional Facility Rules where the conditions for proceedings pursuant to paragraph (a) do not apply; the UNCITRAL Arbitration Rules; or any other arbitration rules on agreement of the disputing parties."

262. This model has been adopted in some BITs, such as the Agreement between the UK and Mexico for the promotion and reciprocal protection of investments, signed on May 12, 2006.

proceedings for the purpose of exercising diplomatic protection except, once again, where the respondent State fails to abide by the arbitral award. On the other hand, where the investor has neither submitted nor consented to submit a dispute, the diplomatic protection claim may be pursued even in the absence of specific provisions on its interplay with investor-State arbitration. Indeed, as observed by Ben Juratowitch, "exhaustion of international, as opposed to domestic, remedies is certainly not a prerequisite to diplomatic protection."[263]

With regard to interpretive claims, EU free trade and investment agreements should include a provision clarifying: (1) whether, and to what extent, parallel or subsequent proceedings (investor-State and State-to-State) could be undertaken, and (2) the legal effect of a tribunal's award on the other tribunal. The first situation is where a party initiates inter-State arbitration proceedings, the tribunal renders the award, and then an investor-State tribunal is called upon to rely on the same provision under examination by the inter-State tribunal, thus interpreting it, in order to assess whether there has been a violation of the treaty. In this case, the investor-State tribunal will have to read the award for purposes of treaty interpretation, thus recognizing its binding character. This means that the award is to be considered binding on treaty parties, investors, and future State-to-State and investor-State tribunals. Therefore, its legal effect is very similar to that of a joint interpretive agreement between the treaty parties. As noted by the International Court of Justice, "an agreement as to the interpretation of a provision reached after the conclusion of the treaty represents an authentic interpretation by the parties which must be read into the treaty for purposes of its interpretation."[264] Therefore, EU FTAs may contain a clause under which a decision on the interpretation of treaty provisions delivered by a State-to-State arbitral tribunal must be binding not only on the contracting parties to the treaty, but also on investor-State tribunals if these are called upon to adjudicate a dispute requiring an interpretation of the same treaty provisions.[265] Such a clause would ensure greater certainty and

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263. Juratowitch, *supra* note 38, at 35.

264. Case Concerning Kasikili/Sedudu Island (Botswana v. Namibia), Judgment, 1999, I.C.J. 1045, at 1075 (Dec. 1999); *see also* Roberts, *supra* note 38, at 60-61.

265. Of course, the legal effect of an interpretive award will depend on the text of the relevant free trade and investment treaty. Anthea Roberts speaks of highly persuasive effects. *See* Roberts, *supra* note 38, at 59-63.

consistency by creating a binding *erga omnes* effect and acting as a legal precedent.

The second situation is where a party files a purely interpretive claim and, before an award is rendered, an investor files an investment claim whose resolution requires an interpretation of the same treaty provision. EU FTAs should contain a provision stating that the investor-State tribunal has to stay proceedings and await the interpretation to be rendered by the inter-State tribunal. As a consequence, the investor-State tribunal should give primacy to a State-to-State tribunal entrusted with the authority to resolve disputes about the interpretation of the treaty. In the case of an inter-State claim filed after the commencement of investor-State proceedings, but before the deliverance of the award, the agreements should request that the tribunal order a stay of proceedings. Of course, no problems would arise in the case of a State-to-State claim filed by a contracting party dissatisfied with the interpretation given by the investor-State tribunal in its award. As confirmed in most agreements, the award rendered by the investor-State tribunal is binding and becomes *res judicata*. It is essential that agreements are designed in such a way as to prevent the risk that State-to-State arbitration may be used to call into question the finality of awards and the duty of the host State to implement them, or that it may be employed to litigate issues for a second time, generating an additional burden in terms of time and money.

All of the above must be distinguished from the question of participation as *amicus curiae* of the non-disputing Treaty State party in investor-State proceedings.[266] Just as there should be no room for the investor's home State exercising diplomatic protection, home State submissions on questions of treaty interpretation should be foreseen in EU FTAs, representing an important contribution to a better decision-making process.[267] The provision contained in CETA 2016 is welcomed and should be replicated in other agreements,

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266. For an insightful analysis (including some observations on the possible intervention of non-disputing State party not merely as amicus curiae), see Gabrielle Kaufmann-Kohler, *Non-Disputing State Submissions in Investment Arbitration: Resurgence of Diplomatic Protection?*, *in* DIPLOMATIC AND JUDICIAL MEANS OF DISPUTE SETTLEMENT, 307-26 (Laurence Boisson de Chazournes, Marcelo Kohen, & Jorge E. Viñuales, eds., 2012).

267. Examples of treaties that allow for the participation of non-disputing parties include the NAFTA, CAFTA and some national model BITS—those of the US and Canada, for instance—or BITs, such as the US-Chile FTA (2003), Art. 10.19(2), and US-Singapore FTA (2003), Art. 15.19(2).

whether the investor-State system of dispute settlement will imply arbitration mechanisms or be modeled on ICS. Article 8.38 of the CETA reads as follows:

> The Tribunal shall accept or, after consultation with the disputing parties, may invite, oral or written submissions from the non-disputing Party regarding the interpretation of the Agreement. The non-disputing Party may attend a hearing held under this Section. […] The Tribunal shall ensure that the disputing parties are given a reasonable opportunity to present their observations on a submission by the non-disputing Party to the Agreement.[268]

Finally, our observations on the inclusion of State-to-State arbitration in EU FTAs, as well as on their coordination, should also be read in light of Section II of this article, which discusses the clashes between external systems of dispute resolution and the CJEU. In other words, inter-State arbitration could represent a successful remedy for settling disputes and/or interpreting provisions of the agreements in question provided that the principle of autonomy of the EU, namely of the CJEU, is respected. Mechanisms apt at securing the respect of such principle, like a system of prior involvement of EU institutions, are even more important when confronted with State-to-State arbitration; suffice to take into account the *Mox Plant* ruling, mentioned above, as well as the opinions rendered by the CJEU on external inter-State remedies envisaged in the agreements concluded by the EU. In particular, the respect of the autonomy of EU legal order becomes essential in the context of State-to-State interpretive claims in which tribunals, rather than adjudicating single disputes and assessing whether compensation must be awarded, are empowered to exercise purely interpretive functions in relation to a free trade and investment treaty, functions which may frequently require – even more than those performed by investment tribunals adjudicating a specific dispute – an interpretation of EU law.[269]

B. From Arbitral Tribunals toward Transformative Adjudication

In CETA 2016 and EU-Vietnam FTA the EU, along with the third countries concerned, has reaffirmed the same commitment expressed in TTIP toward a system of permanent investment

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268. CETA, *supra* note 3, arts. 8.38(2) and (4).

269. For our extensive discussion, see *supra* Section II.B.

tribunals.[270] The qualifications, approximate salaries, and ethical rules that apply to judges are spelled out in the EU position for the TTIP negotiation and clearly influences the EU-Vietnam FTA and CETA 2016. In these two important agreements[271] the judicial architecture varies in terms of structure even though there is a similar underlying rationale, namely to redress some of the fundamental flaws of the investment arbitration systems expressed by lawyers and civil society alike with respect to the four pillars of public law adjudication: accountability, coherence, independence and openness.[272] As Cecilia Malmström said proudly after the adoption of CETA in 2016, "[b]y making the system work like an international court, these changes will ensure that citizens can trust it to deliver fair and objective judgments."[273] This statement has a twofold function: for the Commission to influence its US counterparts and even more ambitiously transform CETA 2016 and EU-Vietnam tribunal into a multilateral investment court that will eventually eliminate the tribunals.

Some lawyers and scholars alike have already expressed their skepticism toward these investment tribunals because of the overstated benefits of greater coherence and effectiveness in protecting investors through an appeal mechanisms as well as the belief that judges are *per se* more independent and objective than arbitrators in their legal reasoning.[274] It remains undisputed that the

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270. *See* Cecilia Malström, EU Trade Comm'r, Proposing an Investment Court System (Sept. 10, 2015), http://ec.europa.eu/commission/2014-2019/malmstrom/blog/proposing-investment-court-system_en. For an explanation of her achievement: "Today, I've presented a major change in our trade and investment policy. I'm proposing to set up a modern and transparent system for resolving disputes between investors and states—an Investment Court System . . . . Some have argued that the traditional ISDS model is private justice. What I'm setting out here is a public justice system—just like those we're familiar with in our own countries, and the international courts which Europe has so actively promoted in the past." Id.

271. *See* CETA, *supra* note 3, at art. 8.27-8.28; EU-Viet. FTA, *supra* note 3, art. 12-13.

272. *See* GUS VAN HARTEN, INVESTMENT TREATY ARBITRATION AND PUBLIC LAW 153 (2007).

273. *See* Press Release, CETA: EU and Canada Agree on New Approach on Investment in Trade Agreement, (Feb, 29, 2016), http://trade.ec.europa.eu/doclib/press/index.cfm?id=1468; Barrie McKenna, *Canada, EU Revise Trade Deal, Add Investor-State Dispute Tribunal*, THE GLOBE AND MAIL, (Feb. 29, 2016, 9:53AM), http://www.theglobeandmail.com/report-on-business/industry-news/the-law-page/ottawa-says-legal-review-of-canada-eu-free-trade-deal-completed/article28946075/.

274. *See* Barrie McKenna, *Canada, EU Revise Trade Deal, Add Investor-State Dispute Tribunal*, GLOBE & MAIL (Feb. 29, 2016, 9:53 AM), http://www.theglobeandmail.com/report-on-business/industry-news/the-law-page/ottawa-says-legal-review-of-canada-eu-free-trade-

ambitious judicial architecture put forward by the EU in both CETA 2016 and its Vietnam FTA for investment tribunals has deep transformative ambitions. From an institutional perspective a future multilateral investment court aims to replace the various investment tribunals envisaged for every FTA.[275] In substance it remains to be seen whether this new adjudication system transforms the practice and the outcomes of international investment law in a more democratic and egalitarian direction.[276] In light of this transformative ideal, the underlying political economy of the international investment treaty regime shows not only the benefits in protecting foreign investors but also how the costs of pollution and labor violations are easily shifted from the investors to the local communities of the host State.

However, this transformative adjudication model proposal is not merely utopian. Take for instance the letter from Berndt Lange, the MEP chairing the International Trade Committee in the European Parliament to Malmstrom in 2015. Welcoming the TTIP proposal on the Investment Court System Lange reiterates that sustainable development and corporate social responsibility provisions should be mainstreamed throughout the investment chapter.[277]

Along the same line, many environmental and sustainability advocates have long asked for more transparency in large investments in land for forestry, agriculture, or extractive projects that are often agreed to in secrecy, eliminating the voice of the affected communities. These advocates have asked for greater transparency, participation and disclosure to the affected communities in the processes before the government is about to grant the concession to the foreign investors.[278] Not surprisingly, many of these cases have not found avenues for redress before domestic courts for many

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deal-completed/article28946075/; Susan Franck, *Inside the Arbitrator's Mind*. EMORY L.J. (forthcoming 2016) (with James Freda, et al.).

275. *See* CETA, *supra* note 3, arts. 8.27-8.28; EU-Viet. FTA, *supra* note 3, arts. 12-13.

276. *See generally* Karl Klare, *Legal Culture & Transformative Constitutionalism*, 14 S. AFR. J. HUM. RTS. 146, 146-88 (1998).

277. *See* Letter from Bern Lange, Chair of Comm. on Int'l Trade, to Cecilia Malstrom, Eur. Comm'r for Trade (Nov. 11, 2015), https://ec.europa.eu/carol/index-iframe.cfm?fuseaction=download&documentId=090166e5a201630f&title=CM_signed.pdf.

278. *See Transparency in Land-Based Investment: Key Questions and Next Steps*, COLUM. CTR. SUSTAINABLE INV. 4 (Mar. 2016), http://ccsi.columbia.edu/files/2016/03/2016-03-11-CCSI-OCP_Transparency-in-Land-Based-Investment_FINAL.pdf.

reasons, including the fact that foreign investors often represent a source of wealth for the host governments.

Local communities, however, have brought some of these cases against the States that negotiated without respecting indigenous or communal property rights before international human rights courts.[279] For instance, before the Inter-American Commission on Human Rights (IACHR) petitioners used the right of information and transparency in the decision of the Haitian government to attract tourism and the mining industry to Haiti, communities sought redress for human rights violations by the extractive industries in Latin America on both peasants and indigenous communities whose health conditions have deteriorated due to the pollution created by the foreign investors to the air, water, and environment.[280]

While foreign investors have access to international investment courts against the host State when it is in violation of environmental, human rights, labor, or corporate social responsibility norms affecting local communities, indigenous people and workers have limited remedies against these tortious actions by foreign investors. Despite the exceptional case of the US, in which federal courts have redressed these violations through the Alien Tort Statute, this avenue has been severely precluded by the recent *Kiobel* jurisprudence of the US Supreme Court.[281]

In his utopian proposal, Lance Compa argues that TPP represents a possibility to create a truly transformative adjudication mechanism to enforce labor, environmental and consumer protection standards in international trade and investment agreements.[282] Compa

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279. *See generally* S. James Anaya & Maia S. Campbell, *Gaining Legal Recognition of Indigenous Land Rights: The Story of the* Awas Tingni *Case in Nicaragua*, *in* HUMAN RIGHTS ADVOCACY STORIES 117 (Deena R. Hurwitz & Margaret L. Satterthwaite eds., 2009); S. James Anaya & Claudio Grossman, *The Case of Awas Tingni v. Nicaragua: A New Step in the International Law of Indigenous Peoples*, 19 ARIZ. J. INT'L & COMP. L. 1, 15 (2002).

280. *See* Marie Durané, *Situation of the Right to Access to Information in Haiti*, HUM. RTS. BRIEF (Mar. 19, 2015), http://hrbrief.org/2015/03/situation-of-the-right-to-access-to-information-in-haiti/; Marie Durane, Human Rights and Extractive Industries in Latin America, HUM. RTS. BRIEF, (Mar. 21, 2015), http://hrbrief.org/2015/03/human-rights-and-extractive-industries-in-latin-america/.

281. Vivian Grosswald Curran & David L. Sloss, *Reviving Human Rights Litigation After Kiobel,* 107 AMER J. INT'L L. 858 (2013).

282. *See* Lance Compa, *How to Make the Trans-Pacific Partnership Work for Workers and Communities*, NATION (Jan. 14, 2016), http://www.thenation.com/article/how-to-make-the-trans-pacific-partnership-work-for-workers-and-communities/.

envisages a more egalitarian system of redress for human right, labor and environmental violations:

> Consider instead creating an innovative alternative system to enforce trade agreements' labor, environmental, and consumer-protection provisions. Let the same door open to investors wronged by governments swing open for workers and communities harmed by investors. Give civil-society forces the power to bring multinational corporations before a neutral arbitral panel to seek damages for violations of labor rights, environmental standards, consumer protections, and human rights that relevant chapters of the trade agreement purport to guarantee and protect.[283]

Clearly, Compa goes further than the European Parliament not only by mainstreaming environmental sustainability and corporate social responsibility norms but also by creating more equal access to international adjudication for investors as well as workers and local communities. As he puts it "Addressing inequality without fear of investors' challenges" [284] should be one of the priorities of a transformative investment regime in countries where rising inequalities triggered by NAFTA in the US and by the increasing income disparities among European economies. Compa's proposal is that investment arbitration should not interfere with some governmental measures such as setting national minimum wages, guaranteeing the "prevailing wage" in publicly funded project and setting health and safety standards higher than national ones.[285]

In taking an economic development perspective, Roberto Echandi has warned against the escalation of costly litigation in international investment arbitration. Rather than on courts, Echandi focuses on alternative dispute resolution policies and mechanisms that could provide less litigious remedies without going to court.[286] A well-known challenge to the system of investment treaty arbitration is that several developing countries like Argentina and Ecuador have denounced and abandoned the ICSID system in the attempt to create a new regional model within Mercosur. As a result, the engagement

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283. *See id.*

284. *See* Lance Compa, *Labor Rights and Labor Standards in Transatlantic Trade and Investment Negotiations: A US Perspective*, 49 ECONOMIA & LAVORO 87, 88 (2015).

285. I*d.* at 89.

286. *See* Roberto Echandi, *Towards a New Approach to Address Investor-State Conflict: Developing a Conceptual Framework for Dispute Prevention* (NCCR Trade Reg. Swiss Nat'l Ctr. of Competence in Res., Working Paper No. 46, 2011).

between arbitration and law and development scholars led to questioning and further reassessing the outcomes of investment arbitration in terms of greater procedural fairness[287] or in creating new adjudication models in South-South relations.[288]

CONCLUSION

EU trade negotiators have changed the international architecture for the protection of foreign investors through by moving away from a traditional ISDS model and adopting instead a permanent court system with procedural due process guarantees: the ICS. The open question remains, however, whether beyond such procedural innovation also substantive aspirations lie behind the agenda of EU trade negotiators to promote a truly transformative trade and investment regime in their recently negotiated FTAs,[289] rather than simply responding to external and internal political and legal pressures. These include the clashes between EU law and international arbitration as well as the need to safeguard the principle of autonomy of the EU legal order as interpreted by the CJEU's jurisprudence. The new agreements of CETA 2016 and the EU-Vietnam FTA with the creation of permanent investment tribunals and appellate mechanisms demonstrate that EU negotiators have put forward a consistent transformative approach toward international trade and investment regimes that can reinforce their negotiating positions *vis à vis* the U.S. in TTIP, on which the USTR remains lukewarm on the ICS.[290]

While welcoming the ICS as a procedural departure from the traditional ISDS regime, in this article we suggest a new role for the underemphasized State-to-State arbitration and we suggest

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287. *See* Susan Franck, *Development and Outcomes of Investment Treaty Arbitration*, 50 HARV. INT'L L.J. 435 (2009).

288. *See* Roberto Echandi, *What Do Developing Countries Expect from the International Investment Regime?*, *in* THE EVOLVING INTERNATIONAL INVESTMENT REGIME: EXPECTATIONS, REALITIES, OPTIONS 3-21, 6 (Jose E. Alvarez, Karl P. Sauvant, Kamil Girard Ahmed, & Gabriela P. Vizcaino eds., 2011).

289. *See* Anne van Aaken & Tobias A Lehmann, *Sustainable Development and International Investment Law: An Harmonious View from Economics*, *in* PROSPECTS IN INTERNATIONAL INVESTMENT LAW AND POLICY 317-39 (Roberto Echandi & Pierre Sauvé eds., 2013).

290. *See* Michael Froman, Remarks at the close of the Transatlantic Trade and Investment Partnership Negotiating round in Brussels, USTR (Feb. 26, 2016) https://ustr.gov/about-us/policy-offices/press-office/speechestranscripts/2016/February/US-Press-Statement-TTIP-Round-Brussels.

strengthening the substance of the investment clauses in the new FTAs. While the transformative procedural architecture of the ICS is well established we question whether its substantive clauses on the right to regulate and fair and equitable treatment are well-equipped to engage with emerging questions of corporate social responsibility, sustainable development and human rights arising in international investment disputes.