THE INTERACTION BETWEEN EU LAW AND INVESTMENT LAW

Columbia Law School

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Judge Allan Rosas

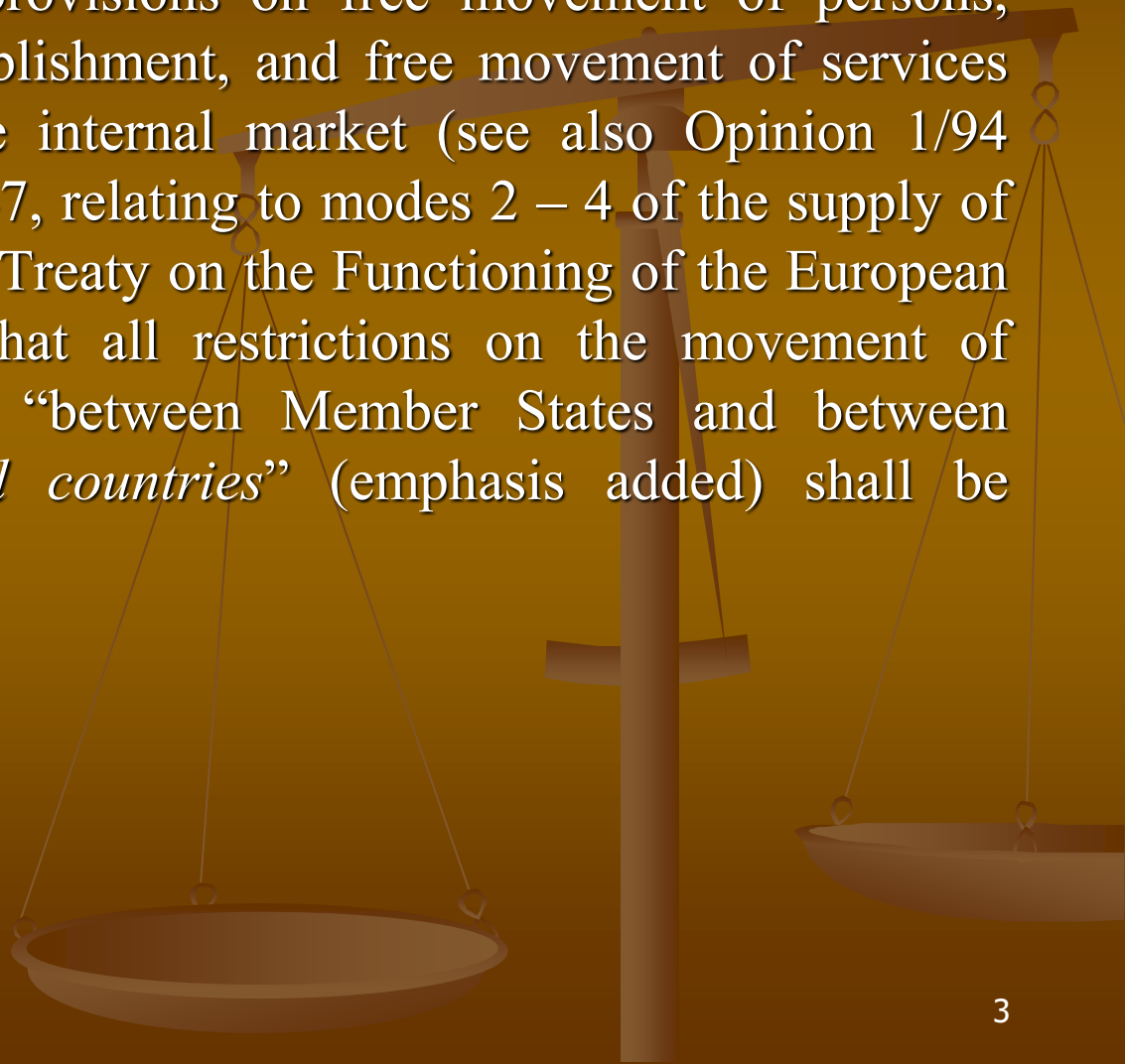
European Court of Justice

The EU internal market and the four (five) freedoms: free movement of goods, persons (including right of establishment), services and capital

These concepts do not as such correspond to the four modes of supply of services, as conceived in international trade law, although there is some overlap. Cross-frontier supply (mode 1) corresponds to the free movement of services; consumption abroad (mode 2) and temporary presence (mode 4) also to the free movement of persons and commercial presence (mode 3) also to the right of establishment.

For the notion of investment, the right of establishment (corresponding to mode 3 with regard to the supply of services) and the free movement of capital are particularly important.

Whereas the EU Treaty provisions on free movement of persons, including the right of establishment, and free movement of services are as such limited to the internal market (see also Opinion 1/94 EU:C:1994:384, paras 42-47, relating to modes 2 – 4 of the supply of services), Article 63 of the Treaty on the Functioning of the European Union (TFEU) provides that all restrictions on the movement of capital and on payments "between Member States and between Member States *and third countries*" (emphasis added) shall be prohibited.



The European Court of Justice (ECJ) has ruled that if in situations involving the access of third country nationals, both the free movement of capital and another economic freedom are relevant, one should look at the main objective of the legislation restricting the freedoms and if this is, say, free movement of services, the free movement of capital becomes "merely an unavoidable consequence of the restriction on the freedom to provide services" (on free movement of services see, eg Case C-452 Fidium Finanz EU:C:2006:631, para 48; on establishment, see, eg Case C-196/04 Cadbury Schweppes EU:C:2006:544, paras 32-33), implying that third country nationals would not be able to rely on Article 63 TFEU to have direct access to the EU internal market.

For the purposes of investment in the form of shareholdings, the ECJ has characterized establishment (Article 49 TFEU) as "shareholdings which enable the holder to exert a definite influence on a company's decisions and to determine its activities" (see, eg Case C-190/12 Emerging Markets Series of DFA Investment Trust Company EU:C:2014:249, paras 26 and 27; Case C-686/13 X AB EU:C:2015:375, paras 18-19) while "shareholdings acquired solely with the intention of making a financial investment without any intention to influence the management and control of the undertaking" must be examined exclusively in the light of the free movement of capital (C-190/12, para 28), covered by Article 63 TFEU.

Whilst this constellation relates to the dichotomy between Articles 49 and 63 TFEU, the matter is complicated by the fact that Article 64 (1) and (2) TFEU, which concern restrictions and regulations on the free movement of capital to and from third countries, refer to measures involving, inter alia, "direct investment – including in real estate" as well as "establishment". These notions are also to be found in the nomenclature annexed to a directive on capital movement adopted in 1988 (Council Directive 88/361/EEC [1988] OJ L178/5) which, whilst no longer in force, has been considered in ECJ case law to continue to have "indicative value" (eg Case C-182/08 Glaxo Wellcome EU:C:2009:559, para 39).

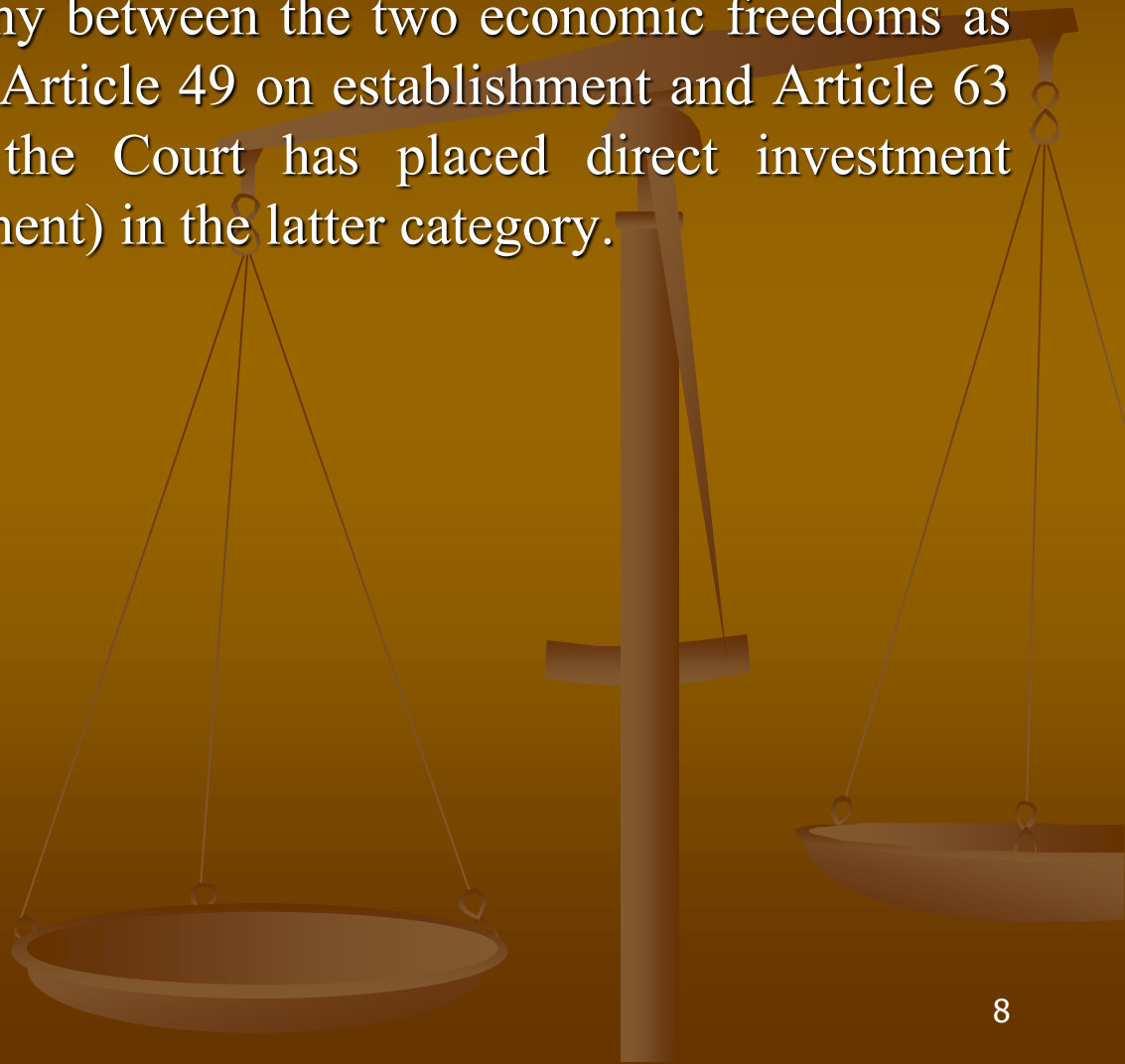
In view of these references to “establishment” and “direct investment” in the context of EU Treaty provisions on capital movement (Article 63 TFEU), the ECJ has, with respect to holdings and participation in undertakings, seen it fit to describe the relations between these notions as well as that of “portfolio investment” as follows (see, eg Case 182/08 Glaxo Wellcome, paras 40, 47; Case C-81/09 Idrima Tipou EU:C:2010:622, paras 48, 51):

Establishment, as was already noted above, implies holdings which enable the holder “to exert a definite influence on a company’s decisions and to determine its activities”.

Direct investment implies participation in an undertaking through the holding of shares which “confers the possibility of participating effectively in its management and control” (and thus participation which does not necessarily imply establishment)

Portfolio investment means the acquisition of shares on the capital market “solely with the intention of making a financial investment without any intention to influence the management and control of the undertaking”

With regard to the dichotomy between the two economic freedoms as recognized in the TFEU, ie Article 49 on establishment and Article 63 on movement of capital, the Court has placed direct investment (arguably short of establishment) in the latter category.



Whilst Article 49 TFEU is as such limited to establishment in the internal market and Article 63 TFEU concerns capital movements both between the Member States and between them and third State, Article 207 TFEU, as modified by the Treaty of Lisbon (entry into force 1 December 2009), lays down the principal rules for the Union's external trade policy, denominated common commercial policy. According to Article 3(1) TFEU, the common commercial policy belongs to the areas of Union exclusive competence. Unlike the earlier versions of this provision, Article 207(1) TFEU provides that the common commercial policy shall be based on uniform principles, particularly with regard, inter alia, to "foreign direct investment".

The external (international) dimension of investment law has traditionally been principally handled by the EU Member States, which moreover have maintained a number of "intra-EU" bilateral investment agreements (BITs) between themselves.

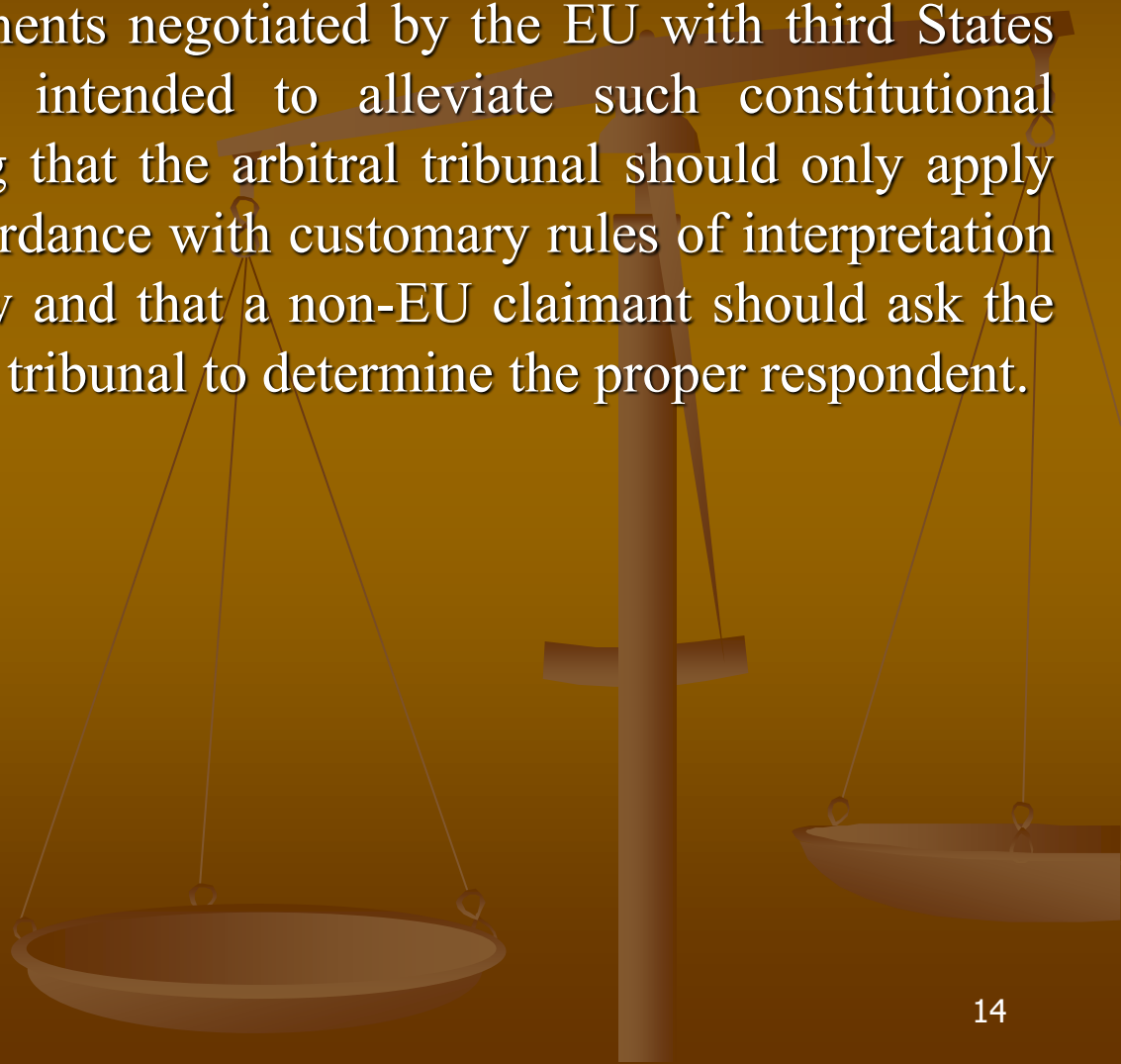
Following the entry into force of the Treaty of Lisbon (2009), investment law and policy has more explicitly become part of the Union's common commercial policy (see, eg Commission Communication, COM(2010) 343 final "Towards a Comprehensive European International Investment Policy"). The EU has started to include in trade agreements negotiated with third States, apart from provisions relating to goods, services, intellectual property rights, and so on, elaborate provisions on investment, including on investor-to-state arbitration (ISDS). These provisions normally cover both direct investment (including establishment) and portfolio investment.

In 2014, the European Parliament and the Council adopted a legislative act establishing a framework for managing financial responsibility and the allocation of responsibilities between the Union and its Member States for the conduct of ISDS investment disputes (Regulation (EU) No 912/2014, [2014] OJ L257/121). As a general rule, the Union shall act as a respondent where the dispute concerns treatment afforded by Union bodies whereas this responsibility shall be incumbent on a Member State where the dispute concerns treatment afforded by it; there are rules on cooperation between the Commission and the Member States and the Commission may, under certain circumstances, take over responsibility for a dispute which, according to the general rule, would have seen a Member State as the respondent.

At the same time, ISDS provisions have started to appear in draft broad-based trade agreements negotiated with third States such as Canada (CETA), Singapore, the US (TTIP), Vietnam, India and Japan. The CETA Agreement has already advanced to Commission proposals for signature, provisional application and conclusion. The Singapore draft agreement is currently before the ECJ but the request for an Opinion is limited to the question of competence (Union exclusive competence or competence shared with the Member States?) and does not concern the substantive compatibility of the agreement with the Union constitutional order (Opinion 2/15, oral hearing on 12-13 September 2016).

The inclusion of ISDS mechanisms in EU agreements has not only caused a vivid political debate but also raised legal concerns as to their compatibility with the Union legal order and its judicial system in particular. Earlier case law of the ECJ suggests that international mechanisms for binding third-party settlement may pose problems especially if the substantive provisions of the agreement in question imply a more or less direct "exportation" of Union law to the legal regime established with the third State, if the judicial organ set up by the agreement could determine the (internal) allocation of competence between the EU and its Member States and/or if the agreement curtails the powers of the EU courts (including the national courts of EU Member States) to apply and interpret Union law (Opinions 1/76, 1/91, 1/92, 1/00, 1/09 and 2/13).

The bilateral trade agreements negotiated by the EU with third States contain some provisions intended to alleviate such constitutional concerns, eg by providing that the arbitral tribunal should only apply the agreement and in accordance with customary rules of interpretation of public international law and that a non-EU claimant should ask the EU rather than the arbitral tribunal to determine the proper respondent.



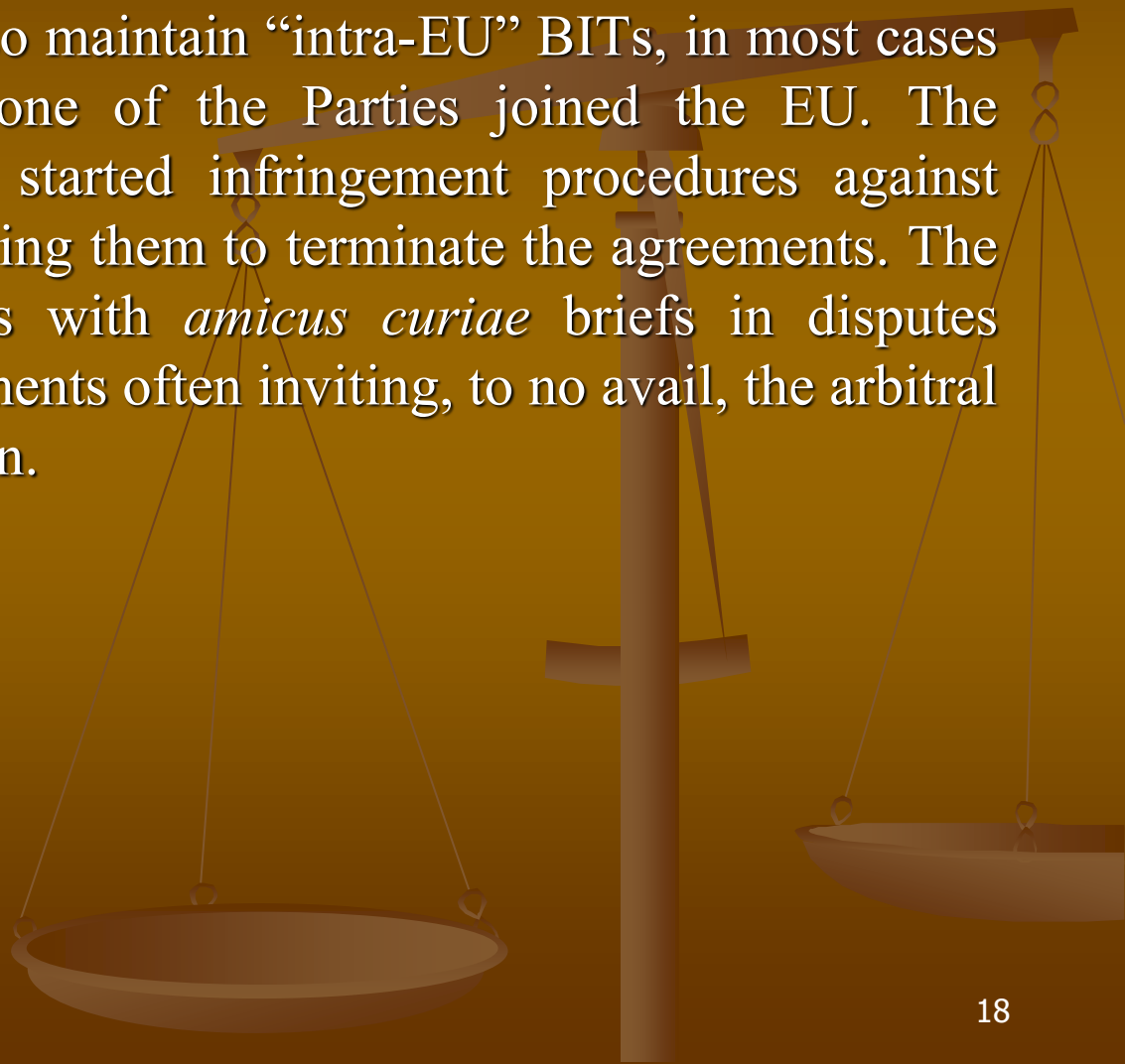
Whereas the Singapore Agreement pending before the ECJ provides for a more classical form of ISDS tribunal (but with arbitrators to be designated to a case from a list established in advance, if need be by the Secretary-General of ICSID), the CETA Agreement with Canada, borrowing from the Commission proposals of November 2015 for TTIP, provides for a more permanent Investment Tribunal (consisting of 15 members), including an Appellate Tribunal, with the ICSID Secretariat as Secretariat of the Tribunal. According to some observers, such a mechanism would not solve but rather accentuate the problems connected to ISDS mechanisms (eg as a permanent tribunal would be inclined to develop an institutionally backed power strategy).

As article 207 TFEU (EU exclusive competence in the field of common commercial policy) is, as far as investment is concerned, limited to "direct investment", many EU Member States argue that the Singapore, Canada and other trade agreements must be concluded as "mixed agreements (EU + Member States), inter alia, because these agreements cover also portfolio investment.

The Commission, for political reasons, accepted that the Canada agreement be concluded as "mixed" (which has caused problems of ratification, notably in a Belgian regional parliament) but, in Opinion 2/15 (see above), the Commission is arguing that the Singapore agreement be concluded as a Union only agreement.

Despite these developments, many bilateral BITs concluded by the EU Member States with non-EU States continue to be in force. Some of them have been found by the ECJ to contain provisions which are incompatible with Union law (Cases C-205/06 Commission v Austria EU:C:2009:118; C-249/06 Commission v Sweden EU:C:2009:119; C-118/07 Commission v Finland EU:C:2009:715). A legislative act adopted by the European Parliament and the Council in 2012 provides for transitional arrangements for such BITs allowing Member States, under some conditions, to maintain, and in some cases even conclude, such agreements (Regulation (EU) No 1219/2012, [2012] OJ L351/40).

Many EU Member States also maintain “intra-EU” BITs, in most cases concluded before at least one of the Parties joined the EU. The European Commission has started infringement procedures against some Member States requesting them to terminate the agreements. The Commission also intervenes with *amicus curiae* briefs in disputes instigated under these agreements often inviting, to no avail, the arbitral tribunal to decline jurisdiction.



Moreover, in a case pending before the EU General Court (former Court of First Instance), an investor is seeking the annulment of a Commission decision (2015/1470 of 30 March 2015) to declare the payment of compensation awarded by an ISDS arbitral tribunal State aid incompatible with the EU internal market law (Cases T-694/15 and T-704/15 Micula). And in a case pending before the ECJ (C-284/16 Achmea), the German Supreme Court is requesting a preliminary ruling from the Court on the compatibility of a bilateral intra-EU BIT ISDS mechanism with Articles 344 TFEU (monopoly of the Union Courts to decide disputes relating to Union law), 267 TFEU (preliminary rulings requested by national courts) or Article 18(1) TFEU (prohibition of discrimination on grounds of nationality).

There is also an on-going debate as to whether not only national courts (such as the German Supreme Court in Case C-284/16) but also ISDS arbitral tribunals could satisfy the requirements of Article 267 TFEU that the body requesting a preliminary ruling be a "court or tribunal" (which would enable such ISDS tribunals to turn directly to the ECJ for binding rulings on the compatibility of such mechanisms with Union law or the interpretation of relevant rules of Union law).