

Titi, Catharine

Research Report

EU investment agreements and the search for a new balance: A paradigm shift from laissez-faire liberalism toward embedded liberalism?

Columbia FDI Perspectives, No. 86

Provided in Cooperation with:

Columbia Center on Sustainable Investment (CCSI) - A joint center of Columbia Law School and the Earth Institute, Columbia University

Suggested Citation: Titi, Catharine (2013) : EU investment agreements and the search for a new balance: A paradigm shift from laissez-faire liberalism toward embedded liberalism?, Columbia FDI Perspectives, No. 86, Columbia University, Vale Columbia Center on Sustainable International Investment (VCCI), New York, NY

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<https://hdl.handle.net/10419/253920>

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Columbia FDI Perspectives

Perspectives on topical foreign direct investment issues by
the Vale Columbia Center on Sustainable International Investment

No. 86 January 3, 2013

Editor-in-Chief: Karl P. Sauvant (Karl.Sauvant@law.columbia.edu)

Managing Editor: Jennifer Reimer (jreimer01@gmail.com)

EU investment agreements and the search for a new balance: A paradigm shift from laissez-faire liberalism toward embedded liberalism?

by

Catharine Titi*

In July 2012, in an internal document, the European Commission's Directorate-General for Trade suggested that future EU investment agreements (EUIAs) should incorporate regulatory flexibility in the same way in which EU free trade agreements (FTAs) safeguard parties' policy space. Since it is expected that a number of treaties on the EU's negotiating agenda will be concluded in the near future, and given the policy shift that has already taken place in Canada and the US,¹ it is time to start thinking about a new balance in a move away from investment treaties' traditional laissez-faire liberalism toward WTO law's embedded liberalism,² a model whereby liberalization is embedded within a wider framework that enables public regulation in the interest of domestic stability.³

Investment agreements -- most particularly European bilateral investment treaties (BITs) -- contain some of the last vestiges of international economic law's laissez-faire liberalism. In contrast with trade agreements, European investment treaties tend to be short documents, single-mindedly focused on investment protection and displaying stubborn laconism where the public interest is concerned. France, Germany and the Netherlands -- among Europe's most prolific investment treaty negotiators -- rarely digress from this approach, as exemplified by their model BITs.

But, the wind of change is slowly shaking things up.

First, until recently the right to regulate was almost exclusively encountered in UNCTAD and (less frequently) OECD publications. Although it has essentially been a taboo phrase in more economically liberal circles, it has entered the investment negotiation vocabulary. Recent

* Catharine Titi (cathy_titi@hotmail.com) is a Research Assistant at the University of Siegen in Germany. The author wishes to thank Andrea Bjorklund, Armand de Mestral, Federico Ortino and an anonymous reviewer for their helpful peer reviews. **The views expressed by the author of this *Perspective* do not necessarily reflect the opinions of Columbia University or its partners and supporters. *Columbia FDI Perspectives* (ISSN 2158-3579) is a peer-reviewed series.**

¹ See their Model BITs of 2004.

² The distinction is borrowed from Daniel Kalderimis "Investment treaties and public goods," *Transnational Dispute Management*, vol. 7 (2010), e.g., pp. 5-6.

³ *Ibid.*, p. 6.

developments have signalled the need for change, underlined by Latin American withdrawals from the investment law system, an impending termination of South African BITs and the Australian Government's rejection of investor-state dispute settlement, a policy currently also pursued by Australia in the context of the Trans-Pacific Partnership Agreement. Most crucially, this concern for regulatory space was made explicit, as early as 2004, with the US and Canadian Model BIT revisions, and has been confirmed and mildly strengthened with the US Model BIT of 2012.

Disillusionment with investment treaties' laissez-faire liberalism is a possible factor influencing EU investment policies. While individual Member States may be reluctant to abandon their tried-and-tested ways, the EU has already expressed its support for the right to regulate in a number of recent documents, including a European Parliament Resolution of 2011 and, reportedly, the Council's negotiating directives authorizing negotiations of investment chapters in comprehensive agreements with, in a first step, Canada, India and Singapore and, later, Egypt, Jordan, Morocco, and Tunisia. Although in its July 2012 document the Commission seems to draw a line between investment liberalization and investment protection, it has upheld the compatibility of both with the right to regulate and has suggested that an explicit reservation of policy space would contribute to a higher degree of consistency and predictability of arbitral awards.

This would reflect the Commission's past approach, namely that EU FTAs, as well as EU political framework agreements, have espoused concern regarding parties' regulatory discretion. The embedded liberalism of these treaties, *à la* WTO, is evident in their significant regulatory language, found in the form of preamble statements, provisions on the non-relaxation of environmental and labor standards, respect for democracy and human rights (in the EU framework agreements) and, importantly, exceptions for the protection of the parties' essential security interests; in this light, these treaties appear to adopt a nuanced rhetoric of economic liberalization, desirous of achieving a middle ground between the promotion of trade liberalization and making allowances for regulatory action in the public interest. The Commission seems to be inclined to continue this approach in its investment treaties, as it addresses questions related to the right to regulate.

With negotiations of the first EU investment agreements ongoing, it is of course not possible to reflect on these developments with any finality. But, to all intents and purposes, a new European treaty model appears to be taking root -- a model that, for the first time in Europe, will address the state parties' regulatory concerns, as well as incorporate investment protection at the pre-establishment stage. Its possible greater convergence with the North American model would contribute to a more uniform approach on both sides of the Atlantic, and may even facilitate the conclusion of a prospective multilateral investment agreement in the future. Whatever the reasons behind this policy reappraisal, whether or not linked to the influence of trade agreements or disillusionment with the Washington Consensus, the political context in which EU investment policy is being elaborated or the guiding principles of the EU's external action, investment law stands at the threshold of a new generation of investment agreements -- at least in Europe. If this is a paradigm shift, it may just be the right one.

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