The EU-China Comprehensive Agreement on Investment – an Institutional Perspective

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Introduction - the CAI, a contested agreement on investment

On 30 December 2020, the European Commission announced that an agreement between negotiators was reached on an EU-China Comprehensive Agreement on Investment (CAI). On 22 January 2021, the Commission then published the draft agreement (before legal scrubbing and possible substantive amendments that cannot be ruled out). Ever since its announcement, there has been an animated debate about the substance, the timing and geopolitical repercussions of the agreement. Substance-wise the agreement was almost immediately criticised because of its alleged meagre human rights conditionality (see for example here and here). In terms of timing it was suggested that the agreement has been rushed through so that it could be announced before the end of the German Council Presidency of the EU. Lastly both in terms of timing and geopolitical ramifications, which Henry Gao also looks into in this Weekend Edition, it was questioned (see here and here) whether announcing the agreement less than a month before a new US President would assume office was a sensible way to signal the strategic autonomy of the EU or whether it jeopardised a re-forging of the Atlantic alliance. This debate will no doubt continue with the prospect of the subsequent phases through which an international agreement comes into being. Anticipating the signature and conclusion of the agreement, this contribution will focus on this institutional dimension of the procedure through which the EU commits itself to the terms of the CAI. In particular, it will address: the qualification of the CAI as a mandatory EU-only agreement, the lack of provisional application of the agreement, and the internal EU procedure through which the EU ratifies the agreement.

> **The EU-China Comprehensive Agreement was almost immediately criticised because of its alleged meagre human rights conditionality**

A mandatory EU-only agreement

The CAI has been described as a *sui generis* agreement because it is a trade agreement that does not deal with trade in goods, and an investment agreement that does not cover investment protection. As noted in the introduction by Isabelle Van Damme to this Weekend Edition, despite its name, the CAI therefore is not a comprehensive agreement. As noted by Johanna Jacobsson, it will not replace or supersede existing agreements between the Member States and China. Furthermore, it will be concluded as an EU-only agreement, although that had not been envisaged as such at the start. Of course, while EU-

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only agreements may well be comprehensive there is a clear correlation between the scope of international agreements and their nature (mixed or EU-only): the broader an agreement's scope, the higher the chances that it covers issues which come under reserved national competences or shared competences, rather than exclusive EU competence. As will be recalled in the following sections, whenever an agreement covers at least one such issue the agreement becomes mandatory, respectively facultatively, mixed.

The original negotiating directives

In October 2013, the Council of the EU and the Member States adopted negotiating directives for the Commission. The fact that this was a joint effort is not without importance: The directives were not merely adopted by the Council under Article 218(2) TFEU but also by the Member States who collectively (but in their individual capacity) authorised the Commission to negotiate the CAI with China on their behalf. This solution was chosen because, in the opinion of the Member States, national competences were also at issue. In the pre-Lisbon era, one solution used for resolving this type of shared competence issues was to have a double-headed delegation consisting of the Commission and the rotating presidency (see for example the directives for the negotiation of the association agreement with Ukraine, see also the chapter by Smyth, p. 305). Here however, the Commission (rather than the rotating presidency) was mandated by the Member States to act on their behalf.

Still, at the time the negotiating directives were adopted, the Commission objected to the Council's decision to have the Member States also grant a collective authorisation to the Commission by noting the areas which the Council thought came under shared competence (portfolio investment, dispute settlement, property and expropriation aspects in fact fell under EU exclusive competence). Obviously, this statement was made before the Court of Justice's clarification of the EU's post-Lisbon trade and investment competences in Opinion 2/15. In that Opinion, the Court rejected the Commission's claim that the EU held an exclusive competence over portfolio investment (paragraph 238). It also held that rules on dispute settlement are typically ancillary to the main substantive provisions and thus fall within the same competence

of the latter (paragraph 276). As a result, the mechanism to settle disputes between the parties did not come under the EU's exclusive competence (given that the FTA included rules on portfolio investment). The investor-State dispute settlement (ISDS) mechanism removed disputes from the jurisdiction of national courts and therefore the Court held that it could not even be qualified as ancillary to begin with (paragraph 292).

Navigating mixity pitfalls

The draft CAI has inadvertently navigated all these obstacles. For political reasons it does not contain rules on investment protection and portfolio investment. Instead, the draft CAI mainly contains provisions on market access, a level playing field, and sustainable development. Taking into account the Court's clarifications in Opinion 2/15, the CAI squarely falls within the EU's exclusive competence. Indeed, the market access provisions pass the Court's test of relating specifically to trade (in services) because they are essentially intended to promote, facilitate or govern trade and have direct and immediate effects on such trade. The level playing field provisions also meet that test or are ancillary (for example transparency provisions). The annexes to the CAI, which were published in March 2021 reveal the exact commitments in the area of transport. Pursuant to Article 207(5) TFEU, transport is largely excluded from the common commercial policy. This means that when the EU wants to include the transport sector in its trade agreements, it cannot rely on the CCP legal basis and must instead rely on the sectoral transport legal bases. Unlike the CCP, the EU's competence in transport is not a priori exclusive in the sense of Article 3(1) TFEU and instead is shared. The EU's competence then only becomes exclusive when the *AETR* test in Article 3(2) TFEU is met. In relation to the CAI, it indeed appears that the Commission negotiated the commitments in such a way that they are covered by exclusive competences (pursuant to either Article 3(1) or (2) TFEU). For instance, apart from those limited transport commitments which the Court in Opinion 2/15 (paragraph 68) classified as coming under Article 207(1) TFEU (that is the CCP) rather than Article 207(5) TFEU, air transport is excluded from the scope of the CAI.

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The rules on sustainable development

The same applies to the provisions on sustainable development. The institutional provisions in this area are in line with those approved by the Court in Opinion 2/15: in terms of dispute settlement, the sustainable development chapter is isolated from the State-to-State Dispute Settlement mechanism, as also highlighted by Johanna Jacobsson, and has its own rather soft mechanism involving a Panel of Experts, just like the free trade agreement (FTA) with Singapore. The substantive provisions on sustainable development in the CAI do not seem to go beyond the bounds which the Court, again in Opinion 2/15, defined for non-trade objectives to be subsumed under the CCP through Articles 205 and 207(1) second sentence TFEU and Article 21 TEU. In that regard, the Court stressed that Singapore and the EU

simply reconfirmed their 'compliance with the obligations that stem from the international agreements concerning social protection of workers and environmental protection to which they are party'. Admittedly, the CAI does include references to ILO Conventions which China has not ratified but it 'merely' imposes a best-efforts obligation on China to 'make continued and sustained efforts on its own initiative to pursue ratification' of those Conventions. This is the same rather weak language as may be found in the FTA with Korea on which a dispute panel recently adopted an opinion (see further below). While some might deplore this soft language from a political point of view, especially in light of the outcome of the dispute with Korea (see below), it would seem that from a legal perspective, this language ensures that the provisions on sustainable development remain an integral part of the CCP (cf. paragraph 147 of Opinion 2/15). Put differently, the question may be asked whether a strict obligation to ratify the ILO Conventions would result in a requirement in the CAI that cannot be subsumed under the CCP any longer and for which the EU only has a shared competence?

No political choice open for facultative mixity

The leaked opinion of the Council Legal Service (CLS) on the Trade and Cooperation Agreement with the UK makes clear what the stakes are in case one provision in an international agreement is covered by shared competence. According to the CLS, if an agreement covers one or several areas where the EU has shared competences which have not yet been exercised, there is a possibility to conclude it as a mixed agreement (paragraph 22). The Council and Member States stress the unfettered(?) political choice which the Council has in opting (or not) to exercise the EU's shared competence. It should be stressed however that this is only so when those parts (under shared competence) are not ancillary to the parts coming under EU exclusive competence. Otherwise, pursuant to the absorption doctrine, the agreement will be a mandatory EU-only agreement. To recall, under that absorption doctrine, if an EU measure pursues two purposes or comprises two components and if one of these is identifiable as the main or predominant purpose or component, whereas the other is merely incidental, the measure must be founded on a single legal basis, namely that required by the main or predominant purpose or component (see for example the judgment in the *Kazakhstan* case, paragraph 37). That centre of gravity of the measure then 'absorbs' the subsidiary or ancillary elements. In light of this doctrine a caveat may apply in respect of the CLS' statement that, if an agreement covers one or more areas outside EU competence, mixity is obligatory. Whether that is the case depends on whether the absorption doctrine can be applied to provisions that come under Member States' reserved competences (Advocate General (AG) Kokott strongly rejected this in her Opinion in the *AMP Antarctique* case (point 82), while AG Wahl seemed more sympathetic in his Opinion on the Marrakesh agreement (point 122), for a discussion, see Chamon, pp. 142-147). These questions, namely whether facultative mixity is entirely subject to a political choice within the Council and the vertical application of the absorption doctrine, remain to be settled by the Court. As discussed in a recent EU Law Live Op-ed, at least Advocate General Hogan in his Opinion in Avis 1/19 on the Istanbul Convention has endorsed the view that the choice is indeed for the Council to make.

In light of the above, it is therefore important to stress again that the entire CAI appears to come under the EU's exclusive competence and that, even as-

suming that facultative mixity boils down to a purely political choice, the CAI is a mandatory EU-only agreement.

Lack of provisional application – maximising the European Parliament's leverage?

Since the CAI is arguably entirely covered by EU exclusive competences it would seem logical that provisional application is not envisaged for the CAI. While it is true that provisional application is a characteristic feature of mixed agreements, in practice most of the agreements provisionally applied by the EU are EU-only agreements (see Chamon, p. 889). The Trade and Cooperation Agreement (TCA) with the UK is a significant case in point. Unlike the TCA, however, there is no pressing reason why the CAI should be imminently applied. Provisional application results in inter-institutional tensions because the European Parliament is not formally involved in the decision on provisional application (other than being informed thereof) (see Driessen, pp. 759-764; and Passos, pp. 380-393). The commitment of the Commission to propose the provisional application of trade agreements only after the European Parliament has given its consent (see Ursula Von der Leyen's political guidelines for the 2019-2024 European Commission, p. 17) of course bolsters the Parliament's position but it is merely a gentlemen's agreement, as the TCA with the UK illustrates, that cannot be enforced in Court. The Parliament has long made an issue of its limited formal role (see its Resolution of 25 March 2009, paragraph 46). Even if it retains a formal veto power to most international agreements, the threshold for refusing to consent to an international agreement that is already (partially) provisionally applied is much higher than refusing to consent to an international agreement that has only been signed. In addition, the leverage of the EU over the partner with which it has negotiated an agreement diminishes in case of provisional application, as the costs of terminating provisional application are higher than the costs of not ratifying a signed (but not provisionally applied) agreement. That the CAI is not signed or provisionally applied has become especially notable since China imposed sanctions in late March 2021 against several EU citizens, including five MEPs in retaliation to EU sanctions over China's treatment of its Uyghur minority, as also discussed by Henry Gao. Should the Parliament decide to withhold its consent to this agreement, the political and economic costs of such a decision would be lower compared to a situation where the CAI would already be provisionally applied.

> **The entire Agreement appears to fall under the EU's exclusive competence and is a mandatory EU-only agreement**

The internal ratification procedure

In light of the Court's established legal basis test, the substantive legal bases for the Council's decisions on the signature and conclusion of the CAI will probably be Articles 91, 100(2) and 207(4) TFEU. Considering that Article 218(6)(v) TFEU applies, the European Parliament will have to give its consent. Furthermore, because none of the exceptions prescribing unanimity under Articles 218(8) or 207(4) TFEU appear to apply, the Council may adopt its decisions through qualified majority vote.

The European Parliament has been adamant about the integration of sustainable development chapters in the EU's FTAs

It is at least to be expected that the Commission will put forward its proposals based on this premise. This legal backdrop provides the European Parliament with the most congenial political circumstances: it is faced with neither the *fait accompli* of potentially having to shoot down an agreement that is already provisionally applied nor (necessarily) a Council unanimously in favour of an agreement.

On the CAI, the Parliament has been vocal on the human rights conditions in China. The fact that the CAI will be an EU-only agreement and that it will not be provisionally applied will mean that all eyes will be on whether the Parliament regards the human rights conditionality in the CAI as sufficient. In more general terms the European Parliament has been adamant about the integration of sustainable development chapters in the EU's FTAs (see Cooremans & Van Calster, p. 199). For instance, the Trade Agreement with Columbia and Peru (a mixed agreement) was signed in 2012 and has still not entered into force. Instead it is being provisionally applied. In 2012 the Parliament adopted a critical Resolution but still consented to the conclusion of the agreement with Columbia and Peru. Several years afterwards in 2019 however, it remarked that improvements in the area of sustainable development still had to be made. It seems clear that by already consenting to the agreement and given the provisional application, the Parliament's leverage was by then diminished. No doubt the Parliament will also be mindful of experiences under other FTAs. The FTA with Korea was the first to contain a separate chapter dedicated to sustainable development (see Cooremans & Van Calster, p. 192) and also imposed an obligation on Korea to make 'continued and sustained efforts' to ratify a number of ILO Conventions (among which is the same Convention No 29 at issue in the CAI). The enforcement of this obligation has been cumbersome, however. While in January 2021 the panel convened at the request of the EU found that Korea had failed some of its obligations under the FTA, its 'efforts for the past three years satisfy the legal threshold of the provision' requiring it to ratify the fundamental ILO Conventions. The CAI now presents an opportunity to the Parliament to proceed differently in terms of procedure, timing and conditionality.

Also, at a more fundamental level and from a democratic perspective, the CAI could be a watershed moment. Like the Comprehensive Economic and Trade Agreement (CETA) with Canada, it is a much-mediatised trade agreement which seems a perfect topic for debate in a *European* public sphere. The political debate and cleavages around the CAI are essentially the same in every Member State. In the case of CETA, however, the European Parliament was denied its role as the most appropriate forum to hold this European debate, because CETA's mixed character incentivised and resulted in 27 (or 28) national public debates. All this is different for the CAI for which the Parliament will have to tread carefully between different interests: internally, it must be seen as a credible but reliable partner to the other EU institutions and as a defender of their interests and fundamental rights; externally it must ensure that the EU remains to be seen as a credible economic partner and a proponent of fundamental values and rights.