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INTEGRATION BY STEALTH:

HOW THE EUROPEAN UNION GAINED COMPETENCE OVER FOREIGN DIRECT INVESTMENT

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Abstract: How are policy competences allocated between different actors? This article contributes to the literature on institutional development through an in-depth case-study of the conditions under which the competence over the negotiation of agreements on foreign direct investment (FDI) was transferred from the national level to the European Union (EU) in the 2009 Lisbon Treaty. Most analysts assume that this competence shift was a rationally designed delegation, intended to maximize European bargaining power in international investment negotiations and conceived as an important element of a teleological drive to make the EU a meaningful external actor. This article tells a different story--one where the competence shift happened by stealth as a result of a combination of neo-functionalist Commission entrepreneurship and historical accident, against the preferences of the Member States. The article also assesses whether the conditions under which the competence was transferred have implications on the implementation of the new policy.

Keywords: BIT; Common Commercial Policy ; EU; FDI; investment ; Lisbon Treaty; trade

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"[The] attainment [of a civil princedom] depends not wholly on merit, nor wholly on good fortune, but rather on what may be termed a fortunate astuteness." (Machiavelli 1532)

Who gets to decide which foreign investors are allowed in and under what conditions their investments are protected has become a highly salient and politicized issue in the European Union (EU) in the context of the negotiation of the Transatlantic Trade and Investment Partnership (TTIP). The controversy has also arisen from the transfer of the competence over foreign direct investment (FDI) from the national level to the European Union in the 2009 Treaty on the Functioning of the European Union (TFEU, hereafter referred to as the Lisbon Treaty), which folded FDI under the Common Commercial Policy (CCP) and granted new trade -and thus investment- policy powers to the European Parliament.

This new EU competence over international investment policy could potentially have major implications since the EU is the first sender and the first recipient of FDI worldwide (24.8% of outward FDI stock and 29.7% of inward FDI stock in 2013) (UNCTAD 2014). The EU can now take over the negotiation of all international investment agreements for the Member States in order to liberalize foreign markets, protect European investments abroad, and settle investment disputes; it can also harmonize the rules governing the establishment of foreign investments inside Europe. The EU has been actively using this new competence: it has been involved in recent years in bilateral trade and investment negotiations with its major economic partners –Canada, the United States, and Japan- and has been negotiating a Bilateral Investment Treaty (BIT) with China.

Scholars of FDI are now busy dissecting the implications of this institutional change. Lawyers are finessing how competences are really divided between the EU and the Member States under the new regime (Bischoff 2011; Bungenberg 2011; Herrmann 2010; Chaisse 2012; Krajewski 2005; Herrmann

2014; Reinisch 2014; Bungenberg and Reinisch 2014; Karl 2004; Ceyssens 2005). Economists are asking how the new competence will affect economic growth and competitiveness (Blomkvist 2011; Goetz 2015). Political scientists are exploring whether the new supranational competence will enable the EU to finally leverage its collective power of bargaining (Niemann 2013; Meunier 2014a). Few studies have asked, however, why competence was politically delegated in the first place (Meunier 2014a; Niemann 2013; Reinisch 2014; Woolcock 2012).

Was the competence over foreign investment policy transferred to the supranational level, as intergovernmentalism would expect, as a rationally designed delegation by the Member States intended to maximize European bargaining power in international investment negotiations or, as neo-functionalism would expect, as the result of spillovers? This article is making an historical institutionalist argument showing that the competence shift, which ran counter to the preferences of all Member States and was not initiated by pressure groups, occurred by stealth as a result of Commission entrepreneurship and historical serendipity (or "fortunate astuteness" as the opening quote from *The Prince* suggests). The conditions under which this transfer happened have implications for the subsequent development of the policy. Because the supranationalization of foreign investment was not a decision consciously taken by policy-makers after intergovernmental bargaining and legal ambiguities were not resolved prior to the institutional shift, the political debate is occurring in the implementation phase, just as the EU is negotiating simultaneously with all its major partners. Legal problems have emerged as a result which, in turn, may impact the political and economic dynamics of EU investment negotiations.

This article contributes to the literature on European integration through an in-depth case-study of the puzzling circumstances under which the competence shift over foreign investment policy took place, which revives the old arguments on Commission "policy entrepreneurship" to explain regional

integration processes (Majone 1994; Pollack 1997; Haas 1958; Lindberg 1963). The first section contrasts two canonical theories of European integration, liberal intergovernmentalism and neo-functionalism, to explain the competence shift and highlights their observable implications. Section Two analyzes the diverging preferences of central policy actors (Commission, Member States, and interest groups) on updating the formal rules of the EU to reflect the new reality of FDI. Drawing on interviews, press reports, and position papers, Section Three retraces the historical steps that led to the inclusion of foreign direct investment under the CCP in the Lisbon Treaty, while Section Four develops the central historical institutionalist argument about "integration by stealth." The conclusion addresses the meaningfulness of this shift by assessing how the conditions under which the competence was transferred impact the implementation of the new policy.

1. ALTERNATIVE EXPLANATIONS FOR THE COMPETENCE SHIFT IN FDI POLICY

Unlike trade, foreign investment is not governed by a multilateral institution. And unlike trade, the 1957 Treaty of Rome, which created the European Economic Community, did not bring foreign investment under supranational reach. For decades, therefore, individual Member States negotiated their own bilateral investment treaties, which deal mostly with foreign investment protection and post-establishment regulations. Indeed, EU countries had been particularly active in concluding BITs. By the time of the Lisbon Treaty, Member States had about 1200 extra-EU BITs with 148 countries, accounting for almost half of investment agreements in the world. As for inward FDI, both the promotion and the vetting of inbound foreign investment have taken place entirely at the national level.

Nevertheless, although the formal EU rules governing international investment policy had not changed during the period of FDI explosion, the practice of international investment policy in the EU had become very complex. Member States were still responsible for concluding their own investment

agreements, but the Commission had started, in practice, to handle market access and pre-establishment conditions for European investments in the multilateral and bilateral free trade agreements it was negotiating collectively. Why was FDI finally folded under the Common Commercial Policy in the 2009 Lisbon Treaty?

Competence shift as a result of intergovernmental bargaining

One hypothesis for the 2009 transfer of FDI competence to the supranational level is offered by liberal intergovernmentalism, which focuses on the centrality of bargains between national governments and is evidenced by deliberation (Hoffmann 1966; Moravcsik 1998; Bickerton, Hodson, and Puetter 2015). In this view, Member States would have chosen, after intergovernmental bargaining, to delegate investment policy to the supranational level because it presented the most rational and effective way for them to achieve their economic objectives.

National economic preferences on investment policy have been influenced by the central role of European countries in the explosion of FDI since the 1980s. By 1999, companies based in the EU accounted for two thirds of all investment outflows, and extra-EU FDI surpassed intra-EU FDI for the first time in 1997. Today, the EU is the world's largest exporter of FDI, with over $9 trillion in FDI stock abroad -twice as much as the U.S. stock abroad and almost half of the total value of FDI stock in the world. As for inflows, the EU is also the world's biggest recipient of foreign direct investment with about one third of FDI stock worldwide (UNCTAD 2014).

It could be argued that given the FDI stakes held by European countries, the national and confusing nature of international investment policy had been costly for Member States. First, national competence imposed a cost on bargaining leverage - the absence of unison leading Europe to "punch below its weight" on at least two counts: market access and shaping the international context (Thomas 2012; Elsig 2013; Niemann and Bretherton 2013; Conceição-Heldt and Meunier 2014). Because each

Member State was negotiating on its own, it could not harness the market power of the whole EU and as a result force large economies to reciprocate by opening their own domestic market to foreign investment in return. Similarly, the EU has not been able to impose to the rest of the world its norms, values, and rules for fashioning international investment regimes in a way commensurate with its place as the world's leading exporter and recipient of FDI (Bungenberg 2011). Others, especially the United States, have created *de facto* global norms for investment agreements, which the EU could not match, whether for human rights, labor standards, or sustainable development. This became particularly apparent in the early 2000s as the major economic powers, led by the U.S., started to drift away from the multilateral trade regime and moved instead to a strategy of competitive liberalization through preferential trade agreements including investment provisions.

When it came to inbound investments, another cost had been the competition between Member States induced by this cacophony. Countries, as well as sub-regional units (such as U.S. states), typically use a variety of incentives to attract FDI, such as tax breaks and infrastructure improvements. Unlike regional subunits, however, European countries are also competing with each other through regulatory and policy incentives. Though limited by stringent EU rules on state aid, this competition can occur through national regimes for screening foreign investments, which can be more or less lax, and through policies which are still national, such as citizenship and residency (e.g. Hungary granting automatic residency to those who invest 250,000 euros) and even foreign policy (e.g. leaders no longer meeting with the Dalai Lama in order to attract Chinese FDI) (Meunier 2014b; Burgoon and Raess 2014). From the perspective of some individual Member States, this cacophony can be seen as a benefit when they win the investment. From the perspective of the collectivity, however, this competition is costly if it leads to a regulatory race to the bottom.

Given the costs incurred by European countries as a result of the EU's formal cacophony, with each state negotiating individually, and informal confusion, resulting from the juxtaposition of supranational and national responsibilities, it may thus have seemed rational to shift competence to the EU level. If liberal intergovernmental dynamics were at play in this case, we should observe national governments, each pursuing their economic self-interest, discussing the pros and cons of this new institutional arrangement prior to the competence shift. Debates, meetings, and memos will be evidence that intergovernmental dynamics contributed to determining the nature and timing of this shift. We should also observe pressures created on national governments by interest groups and social actors in order to fashion the national position defended by their administration at the European level on the issue.

Competence shift as a result of neo-functionalist spillovers

An alternative hypothesis for the competence shift over international investment policy lies in neo-functionalist arguments, which expect the impetus for policy change to have come from spillovers, either functional or institutional (Pierson 1996; Schmitter 2003; Niemann 2013). A functional spillover argument would place the causes of integration of international investment policy in prior European integration in adjacent policy fields, such as trade, coupled with the explosion of FDI worldwide and the growing blurriness between trade and investment. An institutional spillover argument emphasizes the responsibility of EU institutional actors in bringing about the shift.

The 2009 shift towards further integration could indeed have been the result of functional spillovers since the competence for the negotiation of international investment agreements had "crept" over the years to the Commission in practice (Niemann 2013). Trade and investment had become so intertwined that the EU had insidiously gained some practical competence over FDI policy as time went by because of its "single voice" over trade (Meunier and Nicolaïdis 1999; Elsig 2002; Meunier 2005;

Kerremans 2006; Dür and Zimmermann 2007). In multilateral trade negotiations, the EU Commission was in charge of negotiating the Agreement on Trade-Related Investment Measures (TRIMS), the General Agreement on Trade in Services (GATS), and the so-called "Singapore issues" on government procurement, trade facilitation, trade and competition, and trade and investment–even if Member States contested in practice that delegation. Alongside Member States, the EU had negotiated the ill-fated Multilateral Agreement on Investments (MAI) in the OECD (Henderson 1999; Young 2002) and is a member of the Energy Charter Treaty -a multilateral investment treaty with 47 contracting parties designed to protect investments in the energy sector. At the bilateral level, the EU has negotiated a plethora of comprehensive free trade agreements which include investment chapters on market access and protection (e.g. with South Korea, Mexico, and South Africa). From a practical, functional standpoint, it was no longer clear who was in charge for Europe given the increasingly blurred lines between trade and investment. As Ramon Torrent has argued, the contradictory overlapping of national, supranational, bilateral and multilateral rules on foreign direct investment had become a total "mess" (Torrent, 2011). Shifting formally the competence over foreign investment regulation to the supranational level may therefore have seemed like a "long overdue" step in this incremental evolution to rectify an institutional "anomaly" (European Parliament 2010, 9).

A second type of neo-functional dynamics would be autonomous pressures for change from supranational actors. As we know from the European integration literature, EU institutions, chief among them the European Commission and the European Court of Justice, have demonstrated historically a tendency for political entrepreneurship and efforts to expand their power and autonomy (Burley and Mattli 1993; Alter and Meunier 1994; Majone 1994; Pollack 1997; Haas 1958; Lindberg 1963). This is both because the officials in these institutions believe in the teleological goal of ever closer union and because supranational actors are the most likely to benefit from further Europeanization of policy competences. If institutional spillover pressures were at play in this case, we should observe that

supranational institutions put the competence shift on the agenda and engineered its passage. A central question is how these supranational actors can escape the constraints and control of the Member States, acting through the Council, and play an autonomous role. Here, the literature has emphasized several possible answers, including institutional gaps in the principal-agent relationship (Egan 1998; Pollack 1997; Da Conceição 2010), agenda-setting powers (Tsebelis and Garrett 2001) and more generally opportunities provided by critical junctures (Pierson 1996; Fioretos 2007).

2. DIVERGENT PREFERENCES OVER THE COMPETENCE SHIFT

This section examines the preferences of the Commission, the Member States, and various interest groups vis-à-vis the supranationalization of FDI policy. It reveals that far from unanimously embracing the transfer, the Member States and most interest groups were either indifferent or downright opposed to subsuming FDI under the Common Commercial Policy. Only the Commission was strongly in favor of the competence shift.

Commission preferences

The preferences of the Commission have been clearly and persistently in favor of transferring FDI policy to the EU level for more than a decade before it actually happened. First, for practical reasons, a comprehensive EU-wide investment policy would be simpler for the Commission to handle than the confused competence cacophony. Second, officials in DG Trade believed that exclusive EU competence would improve European competitiveness and help obtain better market access and investment protection for EU investors. Third, exclusive competence would increase the relative power of the Commission as an institution and of DG Trade in particular.

The issue of inclusion of FDI under the Common Commercial Policy was initially raised by the Commission during the Intergovernmental Conference (IGC) that led to the Treaty of Maastricht in 1992

but was quickly abandoned for lack of Member State support (Devuyst 1992, 72; Young 2002, 30). It was reopened again by the 1996 Commission opinion for the IGC that resulted in the 1997 Treaty of Amsterdam, but even though the competence shift figured in the initial draft, it was quickly dropped out of Member State opposition (Young 2002, 45; European Commission 1995, 57–60). That IGC took place in the tense context created by Opinion 1/94 of the European Court of Justice (ECJ), which was tasked with determining who, of the Commission or the Member States, was responsible for negotiating and concluding agreements over trade in the growing field of services (Young 2002, 42–44; Meunier and Nicolaïdis 1999, 488–91). The reform of the CCP to include trade in services was already sufficiently contentious without compounding it with the issue of international investment.

The Commission reintroduced yet again the issue of extending EU competence to investment policy in its opinion for the 2000 IGC that led to the Treaty of Nice. Commission President Romano Prodi specifically insisted on the absolute necessity of speaking with one voice in that domain (Young 2002, 46). But the political context was not ripe then for two main reasons. First, the imminent enlargement of the EU to a dozen more countries, all with disparate interests, lent a sense of urgency to the negotiation over the reform of Article 133 governing trade policy –this was not the time to tack yet another new issue onto the already busy agenda (Meunier and Nicolaidis 2011, 279–81). Second, the trade and investment dimensions of globalization had recently become a hot political issue leading to massive mobilizations worldwide. Just two years earlier, the negotiations conducted since 1995 under the auspices of the OECD for the Multilateral Agreement on Investment (MAI), which aimed to ensure that host governments would treat foreign and domestic firms similarly in order to facilitate international investment, had been derailed for lack of support by the negotiating parties (especially France) and by vigorous public demonstrations organized by a diverse collection of non-state actors (Kobrin 1998; Henderson 1999; Young 2002). To the very public failure of the MAI succeeded the following year the very public failure to launch the Millennium Round of World Trade Organization (WTO) negotiations in

Seattle, where an eclectic collection of anti-globalization activists again mobilized and protested that "the world is not for sale" (Klein 1999; Bové and Dufour 2002). Since the Nice IGC took place in this context, FDI policy was once again excluded from the scope of the revised CCP –even if the Nice Treaty extended EU competence to most trade in services, including service-related investment.

After failures at the Maastricht, Amsterdam, and Nice IGCs, the Commission insisted again that foreign investment regulation be included under the CCP during the IGC that led to the Constitutional Treaty, especially in light of the impending enlargement (Lamy 2002). The request made by Trade Commissioner Pascal Lamy to the Convention's Working Group VII on External Relations to include the regulation of investment policy was rebuffed and FDI policy was not included in the articles on trade policy prepared for the Constitutional Treaty.[1]

Member State preferences

By contrast, Member States did not share the Commission's clear preference for a competence shift. Yes, the arguments about the costs of cacophony and confusion could be compelling for some, but overall they were dominated by the costs of relinquishing sovereignty –and by the personal costs for national investment negotiators. Indeed, the Member States who were not downright opposed to the competence transfer were neither in its favor.

A political economy analysis of policy preferences over FDI suggests that for outbound investment, the offensive preferences of Member States are overall similar, even if their companies invest abroad to different degrees. Some EU countries have no or virtually no outward FDI. Other EU Member States have been massive foreign investors outside the EU over the past three decades, led by the UK, Germany, France, Italy and the Netherlands (and the special case of Luxembourg), which has

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[1] Author interview with Pascal Lamy, 2014.

enabled them to be internationally competitive, both through outsourcing and through expanded market access (Eurostat 2014). All want to open external markets for their own investments and obtain maximum protection for these investments.

Preferences are more diverse when it comes to defensive inbound FDI, and Member States were not ready to give up their ability to regulate who invests what on their own territory. European countries are overall among the most open in the world to foreign investment, as reflected in the OECD's FDI Restrictiveness Index (OECD 2012). Western European countries are some of the largest hosts of FDI stock in the world, especially the UK, France, Germany, Belgium, the Netherlands, and Spain. Nevertheless, concern and backlash about foreign investment by multinationals, primarily American, emerged in some European countries in the 1960s (Servan-Schreiber 1968) and again in the big era of globalization in the 1990s, with France at the forefront (Kuisel 2011). Consequently, many European countries adopted rules regulating inbound investment, notably in their national security dimension, throughout the 2000s.

A bureaucratic analysis of preferences also explains why no Member State supported the shift. The competence transfer would remove all power and raison d'être, let alone individual perks, to national investment negotiators who had been criss-crossing the planet to conclude BITs (Poulsen and Aisbett 2016).[2] These bureaucratic experts are the ones who drafted their countries' position on the issue, as it was seen as requiring technical expertise, and recommended to keep the competence national.

As a result, no Member State championed the cause of shifting foreign investment policy to the supranational level. During the Amsterdam IGC, a few liberal governments of small Member States (Belgium, Ireland, Finland, the Netherlands and Sweden) had timidly supported the inclusion of FDI in

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[2] Author interview with Pascal Lamy, April 2016, and with Commission official, May 2016.

the CCP, but most countries resisted strongly the shift, including France, Germany and the UK (Young 2002, 45). For FDI exporters, the worry was great that a supranational regime regulating investments would prompt more restrictions on their own foreign investments. As for inbound FDI, EU countries are employing a variety of methods which put them in competition with one another, such as national investment promotion agencies, incentives, and FDI screening. The Member States that do benefit from this regulatory competition, especially through laxer screening procedures, have no incentive to push for a more cohesive approach to FDI policy. The Member States that do have stringent screening rules did not want to transfer in practice the authority over inbound investment policy to the EU either, because it might jeopardize their own national security should such a screening mechanism be forfeited by the majority of Member States. As for the other Member States, they may fear that the transfer of such authority to the EU would create a more restrictive, protectionist investment regime, and therefore oppose such a transfer on liberal grounds. The bottom line is: no Member State took up the cause of the competence shift as the European Constitutional Treaty was being drafted in 2003.

Pressure groups preferences

Although FDI decisions are primarily an economic consideration driven by market forces, they are also deeply shaped by the economic, political, and legal rules governing investment in the host country. As a result, pressure groups have fought over the design of these rules, but none was really the instigator of the competence shift.

When the idea of a common EU investment policy started to surface during the 1990s, as annual global flows of FDI had risen from $60 billion in 1985 to $315 billion in 1995 throughout the world, leading academics argued that it was necessary to regulate FDI (Graham 1996). So did international business organizations and large multinational corporations, which preferred a more uniform policy framework for investments instead of the highly complex and variegated patchwork of existing national

and bilateral rules. As a result, the WTO, the OECD, and other international organizations started to craft and negotiate multilateral investment regulations.

The EU-wide business organization Business Europe (formerly UNICE), as well as other EU-wide business associations such as the European Services Forum, supported the EU's handling of investment agreements with a single voice at the time of the Convention, but they were not particularly proactive about it (BusinessEurope 2003). These same organizations again approached the EU to demand a single EU investment agreement with China in order to tackle barriers to European FDI in China in 2011 (European Commission 2011). But even these organizations, which wanted a unified stance for outbound FDI, did not favor a unified stance for inbound FDI. UNICE/Business Europe specifically declared to have "serious concerns over proposals to create a Committee on Foreign Investment in the United States or CFIUS-type review procedure to vet foreign proposals for mergers and acquisitions" (BusinessEurope 2008).

Moreover, not all business organizations supported the competence shift. Many national business associations actually opposed the shift and let it be known before the signing of the Lisbon Treaty. After the Treaty came into force, the lobbying by European business organizations against the new sweeping powers of the EU over FDI policy intensified, particularly coming from the German Industry Federation (BDI), the United Kingdom's Confederation of British Industries (CBI), and the French MEDEF (Corporate Europe Observatory 2010).

As for non-business groups and non-governmental organizations –such as environmental groups, labor groups, consumer groups, and intellectuals intent on protecting national culture- many reprised their opposition dating back to the failed MAI negotiations and expressed their opposition to a transfer of the competence over international investment policy to the supranational level.

3. THE INTEGRATION BY STEALTH OF FDI POLICY

Despite the lack of interest group pressure and Member State support, when not downright opposition, the Lisbon Treaty formally transferred FDI competence to the EU level anyway. This section recounts how this competence shift happened.

The inclusion of FDI policy in the Convention

The new EU-wide policy on FDI was not initially planned as the Member States proceeded to launch the "Convention on the Future of Europe" expected to usher in a new European constitution. During the Convention, the Common Commercial Policy had been folded into the busy Working Group VII on the EU's External Action, which also covered the creation of an external action representative, an external action service, defense, foreign aid, development issues, etc. As a result, trade policy received little attention in the deliberations of the working group. There was some limited debate about the existence of mixed competences and qualified majority voting in the field of services, mostly led by Sweden and Finland, as well as copious discussions about an enhanced role of the European Parliament over trade policy decisions, but the issue of foreign direct investment was not raised, except by Trade Commissioner Pascal Lamy –but to no avail.[3] The final report of the working group, prepared by the Convention's Secretariat under the presidency of Jean-Luc Dehaene (Belgium), did not include any reference to investment policy (European Convention Secretariat 2002).

The Praesidium met to discuss the recommendations of the working group on April 22 and 23, 2003 at Val Duchesse. This was a particularly contentious meeting: European policy-makers were arguing over foreign policy barely a month after the start of the U.S.-led intervention in Iraq, which had divided Europe. After the president of the Praesidium, Valéry Giscard d'Estaing, left the meeting, the

[3] Author interview with Pascal Lamy, 2014.

discussion continued, chaired by Dehaene, on more technical issues including the two existing articles on the Common Commercial Policy (now Articles 23 and 24 of Part II, Title B in the draft constitutional text). John Bruton, former Prime Minister of Ireland now representing national parliaments in the Praesidium, spontaneously suggested that some reference needed to be made in the provision on Objectives to the "removal of obstacles to foreign direct investment" (FDI had fueled the rapid economic growth of Ireland, then known as the Celtic Tiger).[4] Michel Barnier, then EU Commissioner for Regional Policy who was acting as representative of the Commission in the Praesidium, thus proposed to make the change operational via the EU competence by also adding "foreign direct investment" in the provision describing the CCP –which happened without further discussion.[5]

The Praesidium endorsed the text of draft articles at the end of the day. As the French expression goes, this opportunistic four-word add-on went "like a letter in the mail"; it was not even mentioned in the summary of the proceedings (European Convention Secretariat 2003).

From draft to the final Constitutional Treaty

The next step was the discussion of the draft text prepared by the Praesidium in the full Convention. As expected, the chapter on external action proved to be the most controversial. The Common Commercial Policy was almost forgotten amidst the deluge of several thousands of amendments proposed on the EU's Common Foreign and Security Policy and the External Action Service.

Ninety-nine amendments were raised concerning the CCP, only 32 of which were about FDI (European Convention 2003). These all asked to strike down the inclusion of "foreign direct investment" from EU competence. Some of these amendments argued that FDI fell under the free circulation of capital, instead of trade policy, and was governed as a result by mixed competences or even national

[4] Author correspondence with John Bruton, December 2015.
[5] Author interview with EU Commission official, November 2012.

competence. Others asked that FDI be subjected to unanimity voting. Some claimed that "Foreign Direct Investment is an entirely different field from trade policy and its inclusion in the Common Commercial Policy would represent an immense and possibly unintended increase in EU competence" (Voggenhuber et al. 2003). One amendment explained that even though the Commission might have been justified, the article needed to be made more precise: "We understand that inclusion of "foreign direct investment" is intended to address a Commission request to be able to conduct negotiations on a multilateral investment treaty in the WTO rather than to remove Member State competence to conduct bilateral investment activity. We would support the intention. However, we see the need to use a more precise term than "foreign direct investment"" (Hain 2003).

Only a few amendments noticed the stealthy actions of the secretariat and/or the Commission. One wrote that "there was no such recommendation for the inclusion of foreign direct investment from the working group" (Earl of Stockton 2003), while another one commented that "The inclusion of a reference to foreign direct investment in the draft is another example of the secretariat taking a unilateral decision to greatly extend the scope of the article, despite there having been no such recommendation from the working group" (Heathcoat-Amory 2003).

The majority of these anti-FDI amendments came from very prominent French, German and British politicians such as Dominique de Villepin (France's foreign affairs minister), Joschka Fischer (Germany's foreign affairs minister), and Peter Hain (a member of the British cabinet who was representing the Blair government at the Convention). In spite of the prominence of its backers, these amendments asking for the exclusion of FDI from EU competence were a drop in the bucket of all the other controversies surrounding the proposed changes to the EU's capacities for external action.

The sweeping extension of EU competence over foreign investment policy was not much noticed in business or academic circles either, with few exceptions, such as the Confederation of British

Industries which denounced the Constitution's excessive centralization of foreign and commercial powers with the EU Commission, and legal scholars who tried to interpret the meaning of these three words (Karl 2004; Ceyssens 2005).

When the IGC approved the draft treaty establishing a Constitution for Europe in June 2004, the two articles (renamed III-216 and III-217) enshrining the inclusion of foreign direct investment under the CCP were left intact (Conference of the Representatives of the Governments of the Member States 2004).

From the Constitution to the Lisbon Treaty

After the Constitutional Treaty failed to be ratified as a result of popular rejection through referenda in France and the Netherlands in 2005, the Member States reworked the constitution in what came to be known as the Treaty of Lisbon, which they signed in December 2007 and which came into force two years later. The Irish presidency did not want to reopen substantive issues during the IGC that followed the failure of the constitution. Trade policy was thus left intact. In the end, the paragraphs in the articles extending the scope of trade policy to foreign direct investment (now renamed Art. 206 and 207) made it into the new treaty untouched from the version hastily conceived in the Praesidium.

The simple three word addition of "foreign direct investment" in the Lisbon Treaty changed the complex, multi-layered situation governing FDI in Europe and radically reformed, *de jure*, the competences over FDI policy. According to Article 207 TFEU, "The common commercial policy shall be based on uniform principles, particularly with regard to changes in tariff rates, the conclusion of tariff and trade agreements relating to trade in goods and services, and the commercial aspects of intellectual property, <u>foreign direct investment</u>, the achievement of uniformity in measures of liberalization, export policy and measures to protect trade such as those to be taken in the event of dumping or subsidies. The common commercial policy shall be conducted in the context of the principles and objectives of the

Union's external action." Therefore, foreign direct investment is now exclusively part of the Common Commercial Policy: in principle, it is up to the Commission to negotiate BITs, to protect EU outbound FDI abroad, and presumably to regulate inbound FDI on behalf of the Member States.

4. EXPLAINING THE COMPETENCE SHIFT

Why did the competence shift happen? It certainly was not the result of intergovernmental bargaining since the outcome ran counter to the preferences of all Member States. Neither was it the result of pressure from business groups, which were divided on the issue and not proactive in any way. The competence shift resulted from a combination of historical serendipity, Commission entrepreneurship, and procedural constraints.

The competence shift first and foremost originated in smart agency by the Commission. FDI made its way into the draft Treaty through serendipitous historical circumstances. If not for the last minute inclusion of "foreign direct investment" in the Common Commercial Policy article through the prompt action of Commission representatives who were in the right place at the right time at the Praesidium, FDI probably would not have become an exclusive competence of the EU until at least the following treaty revision. Stealth being the key here, the Commission did not broadcast the proposed shift.[6]

To some extent, Member States suffered from "bounded rationality", as Lauge Poulsen has argued to explain the diffusion of modern investment treaties in developing countries (Poulsen 2015). It is not surprising that the amendments decrying the stealthy inclusion of the FDI provisions came from the Big Three, as they had the best inter-ministerial coordination and bureaucratic capacity to write hundreds of amendments. However, even those politicians who noticed the stealth inclusion of the

[6] Author interview with Pascal Lamy, 2014.

competence shift in the final draft and tried to derail it failed, in part for procedural reasons. Like all amendments, the ones on FDI were discussed by the Praesidium, which was mindful that the Praesidium itself had made the modification to the Treaty article, that the competence shift was justified on the basis of the evolution of the world economy, and that the arguments against the shift were not convincing.[7] In the remainder of the Convention, FDI was no longer raised, so the Praesidium assumed that there was a consensus on it. Subsequently, the Lisbon Treaty was adopted without reopening the non-controversial areas of the Constitution, so that is how FDI was formally transferred to the EU.

Member States governments also did not derail the FDI competence shift, even though they did not support it, because it was not a political priority amidst an extremely busy agenda. This was a question of prioritization. At the Praesidium, the chapter on external relations produced thousands of amendments, in particular on CFSP. Member States had to pick their battles. While there was effectively a discussion on trade, no Member State prioritized an amendment on FDI to discuss in the second round of amendments.[8] In isolation, the Member States would have fought the competence shift, but given the time and resource constraints they had to devote to the complex Constitution, they chose to fight more important issues.

The subsequent development of FDI policy following the entry into force of the Lisbon Treaty in December 2009 confirms the hypothesis that the competence shift occurred by stealth and not as a result of intergovernmental bargaining. A vigorous political debate emerged in the implementation phase because the deliberation had not happened prior to the passage of the Treaty. The Commission produced several documents to clarify and map the future of European investment policy (European Union 2012; European Commission 2010; European Union 2014). The European Parliament, which had gained new competences over trade and therefore FDI under Lisbon (Van den Putte, De Ville, and Orbie

[7]Author interview with Commission official, November 2012.
[8] Author interview with Commission official, November 2012.

2015), also sought to define the new investment policy through a series of hearings and reports produced by the newly empowered Committee on International Trade (INTA).[9] By contrast, Member States governments argued against the Commission and the European Parliament over definitional issues to keep some sovereignty over FDI. Three issues are proving to be particularly contentious in the implementation phase.

First, confusion reigned initially over the validity of existing BITs, the competence to conclude ongoing negotiations, and the competence to negotiate new treaties. This is the area where Member States have so far expended most political capital. The Commission has been pragmatic in interpreting and implementing the new EU policy sketched by the Lisbon Treaty, especially in the face of opposition, if not “denial”, by Member States.[10] A remaining point of vigorous debate concerns the compatibility with EU law of existing intra-EU BITs; in 2015 the Commission launched infringement proceedings against five Member States (European Commission 2015). Another remaining crucial point of contention is the meaning of “foreign direct investment”, which the Lisbon Treaty did not define (Bischoff 2011; Chaisse 2012). The Commission and Parliament argue that the scope of the new competence also encompasses “portfolio investment”, based on the doctrine of implied powers (European Parliament INTA 2015; European Commission 2010). The Member States claim in a restrictive interpretation that it does not, and therefore that FDI is a shared competence. The answer to this important question, which determines who ratifies the international agreements negotiated by the EU, will likely be a legal one, as the Commission requested in October 2014 the opinion of the European Court of Justice in the context of the EU-Singapore agreement (European Commission 2014). In the meantime, this legal ambiguity is hovering over the ongoing negotiations with third countries and impacting the political and economic dynamics of these negotiations.

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[9] Author conversation with Vital Moreira (former INTA Chair), October 2014.
[10] Author interview with Commission official, November 2012.

Another eminently political battle has emerged in recent years over the nature of investor protection in investment agreements and specifically the controversial Investor-to-State Dispute Settlement (ISDS) arbitration mechanism (Poulsen 2015). The timing of the emergence of this battle, which appeared in 2013 as the EU was starting the Transatlantic Trade and Investment Partnership (TTIP) negotiation with the U.S., also coincided with the growing public realization that investment policy was now the competence of the EU. Led by German interest groups, a pan-European mobilization developed, which resulted in the Commission putting forward in November 2015 a radical proposal for a new investor dispute resolution mechanism with the creation of an Investment Court System (European Commission 2015). This is likely the beginning of a long political and legal battle both against some Member States and international investment partners.

A third major contentious issue concerns the policies governing inbound investment.[11] While the strongest supporter of a common approach has been the European Parliament (European Parliament 2012, 25), the Commission has been divided regarding the necessity of establishing a common vetting system for FDI into the EU. In February 2011, the EU Commissioners for Industry and Entrepreneurship, Antonio Tajani, and the Internal Market, Michel Barnier, wrote a joint letter to Commission President José Manuel Barroso recommending the development of a supranational body to vet inbound FDI (European Commission 2011). DG Trade dismissed this proposal, however, as this might be interpreted as a protectionist move, could alienate Chinese investments in Europe, and have repercussions on European investment abroad whereas, according to then European Trade Commissioner Karel De Gucht, "we need the money" (De Gucht 2012).[12] As for the Member States, not one for now has openly supported this proposal.

[11] Author interview with Commission official, November 2012.
[12] Author interview with Jose Manuel Barroso, 2015.

5. CONCLUSION

By tracing the process through which the EU became responsible for FDI policy, this article provided a case-study of institutional development and competence creep in action. It showed that the competence shift over one of the most important areas of the global economy happened under the radar. Liberal intergovernmentalism cannot account for the process that led to that particular shift, as it occurred in the absence of interest group pressure and Member State support. Instead, functional and institutional spillovers were at play, with external pressures added to Commission entrepreneurship. However, the competence shift did not happen through treachery by the Commission, but rather through a combination of historical serendipity and procedural prioritization among a busy, complex agenda.

Does the formal competence shift matters if Member States do not support implementation? The framework that they reluctantly or inadvertently agreed to in the Treaty is indeed constraining and limiting the contours of the new European FDI policy, locking future developments into a particular path. This seems like an example of historical institutionalism in action. Barring a new treaty revision, the only way out of this path would be through judicial process.

The conditions under which the competence shift happened have implications for the subsequent development of the policy. Because the supranationalization of foreign investment was not the result of bargaining prior to the institutional shift, the political debate is occurring in the implementation phase. Yet this is just as the EU is negotiating simultaneously with its major partners, including the United States and China. While speaking in investment negotiations with a single voice may make the EU a stronger bargainer eventually, the fact that the EU is embarking on these crucial negotiations without having its own house in order may give its partners some influence in shaping its own policy.

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