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CENTRAL EUROPEAN PERSPECTIVES ON INVESTOR-STATE ARBITRATION: PRACTICAL EXPERIENCES AND THEORETICAL CONCERNS

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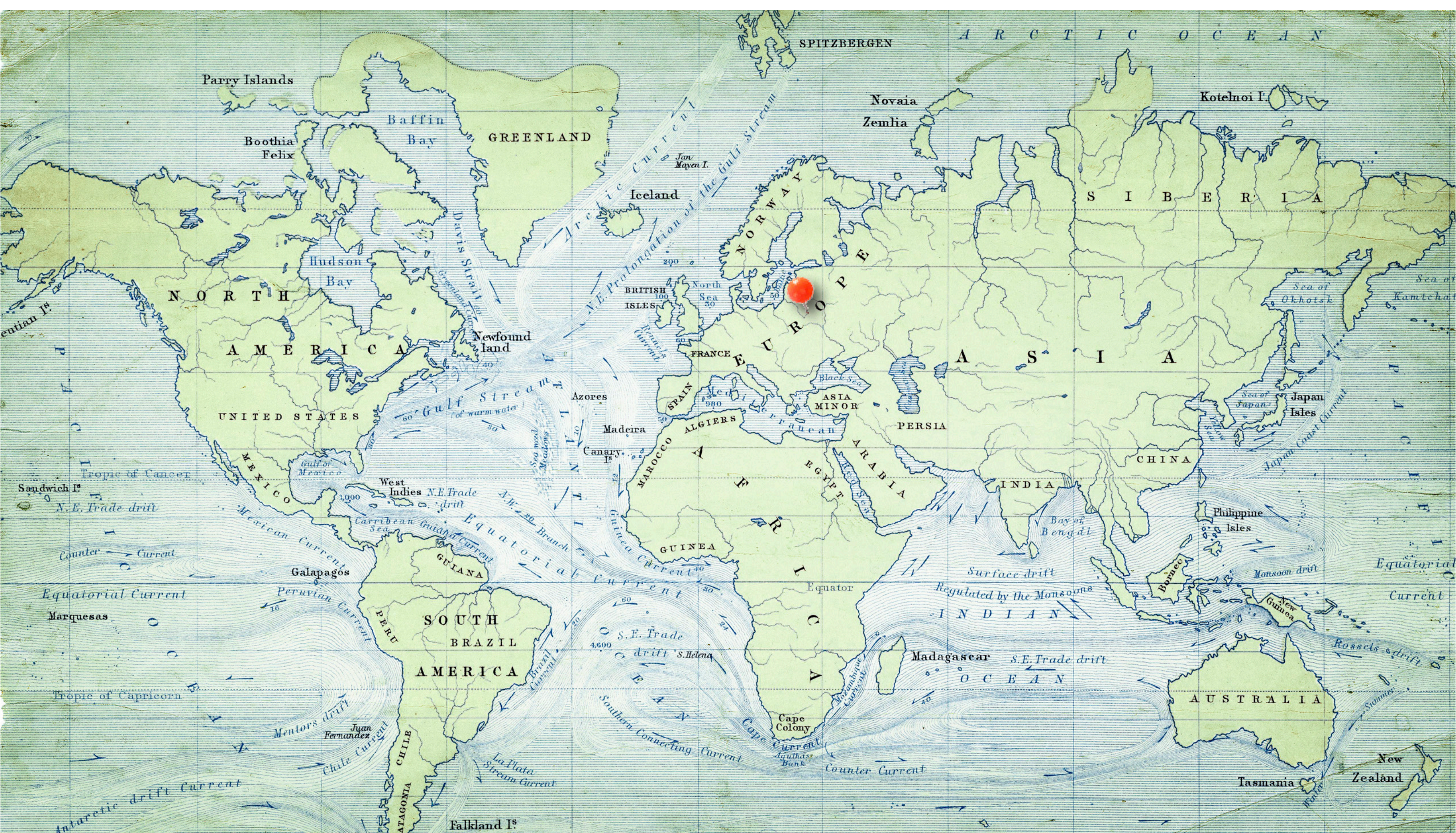

CENTRAL EUROPEAN PERSPECTIVES ON INVESTOR-STATE ARBITRATION: PRACTICAL EXPERIENCES AND THEORETICAL CONCERNS

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ABOUT THE INVESTOR-STATE ARBITRATION PROJECT

Launched in November 2014, this project is addressing a central policy issue of contemporary international investment protection law: is investor-state arbitration (ISA) suitable between developed liberal democratic countries?

The project will seek to establish how many agreements exist or are planned between economically developed liberal democracies. It will review legal and policy reactions to investor-state arbitrations taking place within these countries and summarize the substantive grounds upon which claims are being made and their impact on public policy making by governments.

The project will review, critically assess and critique arguments made in favour and against the growing use of ISA between developed democracies — paying particular attention to Canada, the European Union, Japan, Korea, the United States and Australia, where civil society groups and academic critics have come out against ISA. The project will examine the arguments that investor-state disputes are best left to the national courts in the subject jurisdiction. It will also examine whether domestic law in the countries examined gives the foreign investor rights of action before the domestic courts against the government, equivalent to those provided by contemporary investment protection agreements.

CIGI Senior Fellow Armand de Mestral is the lead researcher on the ISA project. Contributors to the project are Marc Bungenberg, Charles-Emmanuel Côté, David Gantz, Shotaro Hamamoto, Younsik Kim, Céline Lévesque, Csongor István Nagy, Luke Nottage, Ucheora Onwuamaegbu, Carmen Otero, Hugo Perezcano, August Reinisch and David Schneiderman. A conference was held in Ottawa on September 25, 2015. The papers presented at that conference are in the process of being issued as CIGI Papers and will ultimately appear as a collective book.

ABOUT THE AUTHOR

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Csongor graduated from the Eötvös Loránd University of Sciences (ELTE, dr. jur.) in Budapest in 2003, where he also earned a Ph.D. in 2009. During his studies he was a member of the István Bibó College of Law and Political Sciences and of the Invisible College. He received a master's of law degree (2004) and an S.J.D. (2010) from the Central European University (CEU) in Budapest and New York. He pursued graduate studies in Rotterdam, Heidelberg and Ithaca, New York (Cornell). He had visiting appointments in The Hague (Asser Institute), Munich (Max Planck Institute), Brno (Masarykova University), Budapest (CEU Business School), Hamburg (Max Planck Institute), Edinburgh (University of Edinburgh), London (British Institute of International and Comparative Law) and Bloomington, Indiana (Indiana University). He was Eurojus legal counsel in the European Commission's representation in Hungary and has been a member of the Budapest Bar since 2008.

ACRONYMS AND ABBREVIATIONS

BIT	bilateral investment treaties
CC	Constitutional Court
CJEU	Court of Justice of the European Union
EC	European Community
ECT	Energy Charter Treaty
EEC	European Economic Community
EU	European Union
ICC	International Chamber of Commerce
ICSID	International Centre for Settlement of Investment Disputes
ISA	investor-state arbitration
MNV	Hungarian national asset management corporation
MVM	Hungarian electricity company
SCC	Stockholm Chamber of Commerce
TEU	Treaty on European Union
TFEU	Treaty on the Functioning of the European Union
UNCITRAL	United Nations Commission on International Trade Law

EXECUTIVE SUMMARY

This paper presents the experiences of Central Europe with investment arbitration. The European Union's Central European member states are the litmus test of the policy issues of investor-state arbitration (ISA): they are part of the standard investment protection system, are featured by the state's strong market presence and intervention in the competitive process and have attracted the vast majority of European investment cases. The paper explores the Central European treaty and policy landscape and analyzes investment protection issues pertaining to the region (intra-EU bilateral investment treaties [BITs], non-expropriation cases concerning national regulatory sovereignty, the fairness of national court or administrative proceedings and the exercise of contractual rights).

INTRODUCTION

Central Europe presents an excellent case for analyzing the policy issues of ISA. While almost all Central European member states of the European Union are part of the standard investment protection system, the region has seen most of the cases launched against EU defendants (by EU and non-EU claimants). Central European countries have been regarded as transitional economies (they joined the club of market economies a quarter century ago) and, after the privatization wave of the 1990s, the region has been characterized by the state's strong market presence and various (sometimes haphazard) state interventions in the competitive process.

The accession of Central European countries to the European Union (which occurred in three waves: in 2004, 2007 and 2013) brought to light the problem of "intra-EU BITs" (that is, the EU-law compatibility of BITs among member states). Older member states refrained from concluding BITs among themselves and from applying the few they executed. However, in the last two decades, Central European countries (not part of the European Union at that time) entered into numerous BITs with older member states. With the enlargement of the European Union, these became intra-EU treaties, subjecting new member states to contradictory obligations. In a remarkable matter (*Micula v Romania*),[1] the tribunal enjoined Romania to pay compensation for revoking certain tax benefits for their incompatibility with EU state aid law, while, soon after, the European Commission ordered (in a formal decision) Romania to recover the compensation, since it qualified as illegal state aid (the compensation for the revocation of illegal state aid stepped into the latter's place and equally qualified as illegal state aid). As a result of these clashes between BITs and EU law, the Commission launched infringement proceedings with the purpose of wiping out intra-EU BITs and putting an end to this headache-producing dilemma.[2]

The purpose of this paper is to present Central European member states' experiences with investment arbitration, examining the legal questions peculiar to the region. First, it explores the treaty and policy landscape. Second, it analyzes the problem of intra-EU BITs. Third, it provides a selection of Central European non-expropriation cases. In these procedures, arbitral tribunals judged measures that are part of the core of national regulatory sovereignty (such as national privatizations, regulation of prices and curbing of monopolies), the fairness of national court or administrative proceedings and the exercise of contractual rights. The paper ends with the author's conclusions.

THE TREATY AND POLICY LANDSCAPE IN CENTRAL EUROPE: CONFORMISM AND MAVERICKS

The Central European picture on BITs and investor-state dispute settlement is fairly uniform. All member states of the region that joined the European Union in 2004 or afterwards (in 2007 and 2013), with the exception of Poland, are parties to the International Centre for Settlement of Investment Disputes

1 See *Micula v Romania*, Award, 11 December 2013, ICSID Case No ARB/05/20 [*Micula*]; EC, Commission, Press Release, IP/15/4725 "State aid: Commission orders Romania to recover incompatible state aid granted in compensation for abolished investment aid scheme" (30 March 2015) ["EC Romania Press Release"]; *Micula v Commission*, joined Cases T-646/14, T-624/15, T-694/15 and T-704/15 [*Micula* (General Court)]. On December 2, 2015, the applicants withdrew their application; hence, on February 29, 2016, the court removed the case from the register.

2 EC, Commission, Press Release, IP/15/5198 "Commission asks Member States to terminate their intra-EU bilateral investment treaties" (18 June 2015), online: <europa.eu/rapid/press-release_IP-15-5198_en.htm>.

(ICSID) 1965 Washington Convention (ICSID Convention).[3] However, non-ICSID (typically ad hoc) arbitration is still widely used. Most Central European member states joined the ICSID Convention in the early 1990s (Estonia and Lithuania: 1992; Czech Republic: 1993; Slovak Republic and Slovenia: 1994);[4] Romania and Hungary joined the ICSID Convention earlier, during the socialist era (in 1975 and 1987, respectively), Latvia and Croatia in the late 1990s (1997 and 1998), while Bulgaria joined in 2001.

Due to the region's relative uniformity, the analysis of the treaty and policy landscape is fairly asymmetric, as two countries merit closer scrutiny: Poland and Hungary.

Poland has been averse to joining the ICSID Convention; anecdotal evidence suggests that the main reason has been that the ICSID tribunals' awards are final and conclusive and enforceable in the signatory states without any possibility to reject recognition and enforcement with reference, for example, to public policy.[5] Awards rendered in investor-state arbitral proceedings are recognized and enforced in Poland under the 1958 New York Convention, which does allow the rejection of recognition and enforcement with reference to local public policy.[6]

Apparently, the lack of further review did not deter other Central European member states from joining the ICSID Convention.

Hungary, while part of the standard international regime, tried to remove the roadblocks to international investment arbitration through the introduction of a set of idiosyncratic national rules that excluded the possibility to use arbitration in cases concerning (Hungarian) national assets. Although the rules enacted in 2011 and 2012 passed the test of the Hungarian Constitutional Court (CC),[7] they proved to be unsustainable from a business perspective and were, for the most part, repealed in 2015.

The Hungarian regime rested on two pillars: entities in charge of national assets were prohibited from stipulating arbitration (either foreign or Hungarian);[8] and disputes concerning national assets were pronounced non-arbitrable.[9]

These provisions were challenged before the CC. However, the CC held that the provisions in question either did not infringe treaty law or the tension could be lifted by Hungary, for example, through making a reservation or denouncing the relevant convention. Although acknowledging that the Parliament needed to take the necessary measures, it failed to adopt any disposition calling on the Parliament to do so.

As to the domain of investment protection, the CC established, as a constitutional requirement, that the new provisions may not affect existing BITs, and it was the government's duty to ensure the harmony between the provisions concerned and future BITs.[10] The rules covered investor-state disputes, including cases in which the foreign state acted as a private investor, but did not cover genuine inter-state disputes.[11]

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3 ICSID, Convention on the Settlement of Investment Disputes Between States and Nationals of Other States, 18 March 1965, 575 UNTS 159, Can TS 2013 No 24 (entered into force 14 October 1966, accession by Canada 1 December 2013) [ICSID Convention]. The following dates designate signature, ratification and entry into force. Czech Republic: 23 March 1993, 23 March 1993, 22 April 1993; Slovak Republic: 27 September 1993, 27 May 1994, 26 June 1994; Hungary: 1 October 1986, 4 February 1987, 6 March 1987; Estonia: 23 June 1992, 23 June 1992, 23 July 1992; Latvia: 8 August 1997, 8 August 1997, 7 September 1997; Lithuania: 6 July 1992, 6 July 1992, 5 August 1992; Slovenia: 7 March 1994, 7 March 1994, 6 April 1994; Croatia: 16 June 1997, 22 September 1998, 22 October 1998; Romania: 6 September 1974, 12 September 1975, 12 October 1975; Bulgaria: 21 March 2000, 13 April 2001, 13 May 2001. See "List of Contracting States and Other Signatories of the Convention", online: <https://icsid.worldbank.org/apps/ICSIDWEB/icsiddocs/Documents/List%20of%20Contracting%20States%20and%20Other%20Signatories%20of%20the%20Convention%20-%20Latest.pdf>.

4 The dates refer to the entry into force of the ICSID Convention.

5 ICSID Convention, *supra* note 3, arts 53–54.

6 See Świątkowski Marek, "Investment Treaty Arbitration" in *Arbitration in Poland* (Warsaw: Court of Arbitration at the Polish Chamber of Commerce, 2011) 159 at 166–67; Convention on the Recognition and Enforcement of Foreign Arbitral Awards, 10 June 1958, 330 UNTS 39, Can TS 1986 No 43 art V(2)(b) (entered into force 7 June 1959) [New York Convention]. Poland made a reservation to article I(3) of the New York Convention and, hence, applies the convention only to differences arising out of legal relationships, whether contractual or not, that are considered commercial under national law.

7 Case number: II/03736/2012; number of the Constitutional Court's judgment: 14/2013 [CC judgment]. For an analysis of the CC's judgment, see Csongor István Nagy, "The Hungarian Constitutional Court's judgment on Hungary's new anti-arbitration rules" in Marcel Szabó, Petra Lea Láncos & Réka Varga, eds, *Hungarian Yearbook of International Law and European Law 2014* (The Hague & Portland, Oregon: Eleven Publishing, 2015) 629.

8 *Act CXCVI of 2011 on National Property*, s 17(3).

9 *Act LXXI of 1994 on Arbitration*, s 4.

10 CC judgment, *supra* note 7, paras 40–41, 48–52.

11 *Ibid*, para 47.

The CC also found that the new provisions did not infringe the ICSID Convention either, since Hungary had various methods to bring Hungarian law in line with the ICSID Convention.[12]

The conformity of the above provisions with the 1961 Geneva Convention[13] was more difficult to demonstrate. The CC held that in the event article II(1) of the 1961 Geneva Convention does authorize public entities to enter into arbitration agreements (that is, the court, notwithstanding the clear treaty language, did not take the existence of such a right as granted), the convention ensures the possibility for Hungary to opt out.[14] The mechanism suggested by the court was rather odd: although such a reservation limiting the right to arbitration was time-barred (article II(2) provides that such a reservation can be made only "[o]n signing, ratifying or acceding to" the convention), Hungary could denounce the convention on the basis of article X(9) and then re-enter it, this time with the reservation permitted by article II(2).[15] Such a denunciation would take effect 12 months after the secretary-general received the notification of denunciation.

Contrary to constitutional scrutiny, these provisions did not stand the proof of business reality: in fact, they failed very early, suggesting that arbitration is not only a "take it or *leave it*" but even a "take it or *leave*" rule of international economic relations. The reason why they were tried and found wanting was not legal — it was business. Hungary concluded an inter-state agreement with Russia on the expansion of the nuclear energy plant in Paks (the country's only nuclear plant); Russia was not only a contractor, constructing new establishments, but also a creditor financing the project. Although the agreement concerned national assets, it stipulated arbitration. After the incompatibility of these measures was raised in the parliamentary debate,[16] the issue was addressed in the law. However, the result appears to be saliently controversial. While the statutory language of the adopted provisions is fairly clear in that the earlier prohibition is abolished, the explanatory memorandum attached to these (which, as a matter of practice, is regarded as an authoritative guidance of interpretation by the courts) alleges that the amendment does not signify a backing down: "the provision has no new norm-content," the memorandom stated, and its only purpose is to make clear that international treaties have precedence over national rules.[17]

INTRA-EU BITS AND EU LAW

The last waves of enlargement, for historical reasons, revealed new dimensions of intra-EU investor-state dispute settlement. Although intra-EU BITs are not problems related specifically to Central European member states, it was the accession of these countries that brought them to light.

There appears to have been a general agreement among founding member states not to apply pre-existing BITs;[18] after the foundation of the European Economic Community (EEC), apart from some exceptions, member states refrained from concluding BITs with sister states. Although Germany entered into such an agreement with Portugal in 1980 and Greece in 1981, these treaties have not been applied since the accession of Greece in 1981 and of Portugal in 1985. Hence, the problem of intra-EU BITs had long remained theoretical.

During the half century between the foundation of the EEC and the enlargements in 2004, 2007 and 2013, Central European countries concluded numerous BITs with the then members of the European Union. After the accession, these agreements became intra-EU treaties[19] and put a new subject on the table of international legal scholarship.

12 *Ibid*, paras 55–57. For instance, according to article 25(3) of the ICSID Convention, state entities' assent to the jurisdiction of ICSID can be made dependent on the state's approval. Furthermore, under article 25(4) of the ICSID Convention, contracting states can exclude certain classes of disputes from the jurisdiction of the ICSID, and this reservation can be submitted at any time.

13 European Convention on International Commercial Arbitration, 21 April 1961, 484 UNTS 364 (entered into force 7 January 1964).

14 CC judgment, *supra* note 7, paras 64–65.

15 *Ibid,* para 75.

16 *Act VII of 2015 on the investment related to the maintenance of the capacity of the Nuclear Plant of Paks, as well as on the amendment of certain connected acts* (in Hungarian: *"2015.* évi *VII. törvény a Paksi Atomerőmű kapacitásának fenntartásával kapcsolatos beruházásról, valamint az ezzel kapcsolatos egyes törvények módosításáról"*).

17 *Ibid*. For a general overview on the Hungarian developments, see Csongor István Nagy, "The Lesson of a Short-Lived Mutiny: The Rise and Fall of Hungary's Controversial Arbitration Regime in Cases Involving National Assets" (2016) 27 Am Rev Intl Arb 239.

18 See Eric Teynier, "L'applicabilité des traités bilatéraux dans les investissements entre Etats membres de l'Union Européenne" (2008) 5 Les Cahiers de l'Arbitrage 12.

19 *Ibid*.

Intra-EU BITs lie at the heart of investor-state disputes involving Central European states: approximately two-thirds of the cases in the region are intra-EU matters.[20] This means that terminating intra-EU BITs (as demanded by the Commission and advocated by, among others, the Czech Republic and Slovakia[21]) would do away with the overwhelming majority of investment arbitration cases in the region.

The relationship between BITs and EU law in intra-EU matters may boil down to two inter-related questions: the general compatibility of intra-EU BITs with EU law (that is, can BITs be maintained among EU member states at all?) and the liability of member states for the commands of EU law.[22]

General Compatibility of Intra-EU BITs with EU Law

The general compatibility of intra-EU BITs with EU law has generated a heated debate and a good deal of uncertainty in Europe. As a rule of thumb, EU law does not tolerate bilateralism in intra-EU matters (provided they come under its purview) and overrules agreements concluded by two or more member states.[23] The crucial question is, however, whether BITs address the same subject matter as EU law.[24]

While old member states appear to champion intra-EU BITs,[25] reasoning that the protection afforded by these treaties is both legitimate and necessary, new member states, understandably, tend to reject the validity of these instruments.

While it became customary for respondent states to raise the objection of "intra-EU matter" (as regards jurisdiction), this argument has been consistently rejected by arbitral tribunals.[26] On the other hand, the European Commission has been clearly rejecting the validity of intra-EU BITs (in a few

20 Cecilia Olivet, *EU Investment Policy and Intra-EU BITs: The case of Czech Republic* (Amsterdam: Transnational Institute, 2012) at 2, online: <just-trade.org/sites/just-trade.org/files/publications/BRIEFING%20on%20intra-EU%20BITs%20and%20Czech%20Republic-JUST-TRADE.pdf>

21 *Ibid* at 4.

22 *Cf* Thomas Eilmansberger, "Bilateral investment treaties and EU law" (2009) 46 CML Rev 383 at 413.

23 Court of Justice of the European Union (CJEU), *Commission v Italy*, C-10/61, [1962] ECR I-1 [*Commission v Italy*]; CJEU, *Matteucci v Communauté française of Belgium*, C-235/87, [1988] ECR I-05589 [*Matteucci*]; CJEU, *Exportur SA v LOR SA*, C-3/91, [1992] ECR I-05529.

24 At first glance, the question may appear to be strange, since, under article 207 of the Treaty on the Functioning of the European Union (TFEU), the European Union has the competence to conclude BITs with third countries. EC, *Treaty on the Functioning of the European Union,* [2008] OJ, C 115/01 [TFEU].

25 "A clear majority of Member States prefers to maintain the existing agreements, in particular with view to the provisions on expropriation, compensation, protection of investments and investor-to-state dispute settlement", (EC, Economic and Financial Committee, *Annual EFC Report to the Commission and the Council on the Movement of Capital and the Freedom of Payments*, Doc No 17363/08 (23 November 2007) at 15, online: <register.consilium.europa.eu/doc/srv?l=EN&f=ST%2017363%202008%20INIT>; "Most Member States did not share the Commission's concern in respect of arbitration risks and discriminatory treatment of investors and a clear majority of Member States preferred to maintain the existing agreements", (EC, Economic and Financial Committee, *Annual EFC Report to the Commission and the Council on the Movement of Capital and the Freedom of Payments*, Doc No 17446/09 (10 December 2009) at 17, online: <register.consilium.europa.eu/doc/srv?l=EN&f=ST%2017446%202009%20INIT>; "The EFC acknowledges that some Member States still consider that intra-EU BITs are needed in order to maintain protection of their investors", (EC, Economic and Financial Committee, *Annual EFC Report to the Commission and the Council on the Movement of Capital and the Freedom of Payments*, Doc No 17870/10 (14 December 2010) at 23, online: <register.consilium.europa.eu/doc/srv?l=EN&f=ST%2017870%202010%20INIT>.

26 In *Eastern Sugar v Czech Republic*, Partial Award, 27 March 2007, SCC Case No 088/2004 (UNCITRAL), the dispute emerged before the Czech Republic's accession to the EU, although the arbitral award was rendered subsequently. Accordingly, the tribunal could have (conveniently) avoided the examination of the issue of "intra-EU matter" with reference to EU law's temporal scope. However, it analyzed the substantive issues, and the tribunal came to the conclusion that EU law did not exclude the application of the BIT for three reasons: the signatory states did not intend EU law to supersede the BIT (para 167); EU law and the BIT do not clash, because they do not cover the same subject matter; and the two regimes do not contain conflicting requirements. As to the concern of discrimination, the tribunal held that, should this be the case, it is up to those other countries and investors to claim their equal rights; however, "the fact that these rights are unequal does not make them incompatible" (para 170). In *Binder v Czech Republic*, Award on Jurisdiction, 6 June 2007 (UNCITRAL) at para 62, it was ascertainable that the act allegedly violating the BIT occurred before accession, and thus the tribunal seems to have held that the clash between EU law and the BIT was excluded *ratione temporis*. However, the tribunal analyzed the relationship between the two regimes in detail and did not recoil from going into the intricacies of the issue. It established that the Czech Republic's accession to the EU had no impact on the BIT for two reasons. First, there was no conflict, not only as to the BIT's expropriation but also its "treatment" provisions (arbitrary or discriminatory treatment, full protection of investments and revenues, full protection and security of investments) (para 63). Second, it established that the Czech-German BIT entailed no discrimination. Although the tribunal admitted that the possibility to have recourse to investment arbitration is, in itself, a benefit (being "in practice the best guarantee that … [the] investment will be protected against undue infringements by this State"), it came to the conclusion that this plight involved no discrimination (para 65). In *Eureko BV v Slovak Republic*, Award on Jurisdiction, Arbitrability and Suspension, 26 October 2010, PCA Case No 2008-13 (UNCITRAL) [*Eureko*], the tribunal held that BITs were not nullified and its jurisdiction was not impaired by EU law, asserting that the issues of incompatibility may arise only if the BIT and EU law erect contradictory requirements; and, if they do, "[a]ny such incompatibility would be a question of the effect of EU law as part of the applicable law and, as such, a matter for the merits and not jurisdiction" (paras 271–72, 283). According to the tribunal, the only exception would be if ISA were, in itself, contrary to EU law (para 273). However, notwithstanding the Commission's efforts and arguments (discrimination, deprivation of EU institutions of their exclusive competences, violation of the principle of mutual trust), the tribunal rejected this outright (para 274). The intra-EU jurisdictional defence was also touched upon in *United Utilities (Tallinn) BV v Estonia,* Procedural Order No 2, 17 June 2015, ICSID Case No ARB/14/24 [*United Utilities*]: Estonia considered submitting it; however, in the end, it refrained from spelling it out — presumably because this defence had consistently failed before arbitral tribunals.

arbitral proceedings, as *amicus curiae*, it consistently argued that EU law overruled BITs in European "domestic" matters. As well, on June 18, 2015, it launched a few "pilot" infringement proceedings against five member states (Austria, the Netherlands, Romania, Slovakia and Sweden) to have intra-EU BITs abolished and started a consultation with the rest of the member states to have intra-EU BITs terminated (aside from Ireland and Italy, which had already terminated all their intra-EU BITs).[27]

Under public international law, the issue of compatibility centres around the question of subject matter: do the subject matters of intra-EU BITs and of EU law overlap? If they do, for various reasons, EU law would probably have precedence over intra-EU BITs. If the subject matter of investment treaties does not come under the scope of EU law, obviously no conflict emerges. According to article 59 of the Vienna Convention on the Law of Treaties, an earlier treaty is considered to be terminated if the parties conclude a later treaty covering the same subject matter and the provisions of the two instruments are irreconcilable (or the parties' intent to terminate the earlier agreement is ascertainable).[28] Accordingly, the first question to be answered is whether BITs and EU law have the same subject matter.

One arrives at the same conclusion under article 30, which deals with successive treaties and follows the principle that later treaties abrogate earlier treaties *(lex posterior derogat legi priori)*, provided they have the same subject matter.[29] In the event that "all the parties to the earlier treaty are parties also to the later treaty" (as in the event of intra-EU BITs) and the later treaty does not specify otherwise and article 59 does not apply, "the earlier treaty applies only to the extent that its provisions are compatible with those of the later treaty."[30]

Seemingly, under EU law the exclusionary effect may be triggered by a mere conflict, that is, EU law excludes conflicting national law even if the subject matters do not overlap. However, the question of scope may still be relevant, since a conflict may emerge only if both regimes apply in a given matter.[31] While article 351 TFEU addresses the question of treaties concluded with third countries before accession,[32] it is hard to find a specific provision on intra-EU treaties. Nonetheless, the jurisprudence of the CJEU makes it clear that, in matters where it applies, EU law has supremacy over pre-existing inter-member-state treaties and, hence, the latter cannot be maintained if they conflict with EU law. Intra-EU BITs may infringe EU law in numerous regards: they may entail discrimination between EU investors on the basis of nationality, violating article 18 TFEU; they may encroach on the exclusive jurisdiction of the CJEU, violating articles 267 and 344 TFEU; they may counter the principle of mutual trust and sincere cooperation between EU member states, as embedded in article 4(3) Treaty on European Union (TEU); or they may create opportunities for forum shopping.[33] However, all these allegations lead us back to our starting question: does EU law's scope extend to investment protection cases, or, to put it inversely, do these cases come under EU law's subject matter? The prohibition of discrimination on the basis of nationality (article 18 TFEU) operates only "[w]ithin the scope of application of the Treaties"[34];

27 The Commission is of the view that after the enlargement, the "'extra' reassurances [provided by BITs] should not be necessary, as all Member States are subject to the same EU rules in the single market, including those on cross-border investments (in particular the freedom of establishment and the free movement of capital). All EU investors also benefit from the same protection thanks to EU rules (e.g. non-discrimination on grounds of nationality). By contrast, intra-EU BITs confer rights on a bilateral basis to investors from some Member States only: in accordance with consistent case law from the European Court of Justice, such discrimination based on nationality is incompatible with EU law." EC, Commission, Press Release, IP/15/5198 "Commission asks Member States to terminate their intra-EU bilateral investment treaties. Brussels" (18 June 2015), online: <europa.eu/rapid/press-release_IP-15-5198_en.htm>.

28 "A treaty shall be considered as terminated if all the parties to it conclude a later treaty relating to the same subject-matter and: (a) It appears from the later treaty or is otherwise established that the parties intended that the matter should be governed by that treaty; or (b) The provisions of the later treaty are so far incompatible with those of the earlier one that the two treaties are not capable of being applied at the same time." Vienna Convention on the Law of Treaties, 23 May 1969, 1155 UNTS 331, art 59 (entered into force 27 January 1980) [Vienna Convention].

29 *Ibid*, art 30.

30 *Ibid,* art 30(3).

31 *Commission v Italy*, *supra* note 23: "[I]n matters governed by the EEC treaty, that treaty takes precedence over agreements concluded between Member States before its entry into force, including agreements made within the framework of GATT"; *Matteucci*, *supra* note 23: "22. Moreover, the Court has consistently held (see in particular the judgment of 27 February 1962 in Case 10/61 Commission v Italy ((1962)) ECR 1) that, in matters governed by the EEC Treaty, that Treaty takes precedence over agreements concluded between Member States before its entry into force."

32 "The rights and obligations arising from agreements concluded before 1 January 1958 or, for acceding States, before the date of their accession, between one or more Member States on the one hand, and one or more third countries on the other, shall not be affected by the provisions of the Treaties. To the extent that such agreements are not compatible with the Treaties, the Member State or States concerned shall take all appropriate steps to eliminate the incompatibilities established. Member States shall, where necessary, assist each other to this end and shall, where appropriate, adopt a common attitude." TFEU, *supra* note 24, art 351.

33 See Nikos Lavranos, "Member States' bilateral investment treaties (BITs): lost in transition?" (2011) Hague YB Intl Law 281 at 299–300.

34 TFEU, *supra* note 24, art 18.

arbitral proceedings may encroach on the CJEU's exclusive jurisdiction only if the CJEU does have jurisdiction to judge expropriation and other claims related to the nullification of benefits.

While it is easy to see that intra-EU BITs are, by their very nature, discriminatory, since they confer benefits (substantive standards and an effective dispute settlement mechanism) on the investors of a particular member state but not on all of them, it is more difficult to establish that the subject matters of the BITs and EU law completely overlap. It is also difficult to prove that the CJEU has the power to award compensation in cases where national governments expropriate investors' assets.

It is worthy of note that the CJEU did exempt double taxation treaties from the rigor of the prohibition of discrimination,[35] and there are close parallels between intra-EU BITs and intra-EU double taxation treaties. In both cases, the alleged discrimination occurs between the nationals of two other member states (and not between a foreigner and a national), both intra-EU BITs and intra-EU double taxation treaties are extremely good for the internal market, both do something EU law has no competence to do and the application of the principle of non-discrimination to both would ruin these schemes, which are otherwise very beneficial to free movement.

The most important benefit of BITs is the existence of the rules on the protection of the investment (property), such as expropriation and other "treatment" standards (for example, fair and equitable treatment) and the very effective dispute settlement mechanism.[36] While it could be argued that notwithstanding its enormous practical significance, procedure is accessory to substantive protection, these substantive standards are, however, not reproduced in EU law. Although the respect of fundamental (human) rights is one of the cornerstones of the European Union (it is a precondition of membership[37] and is listed among the core values of the European Union),[38] EU law contains no generally applicable effective mechanism to compel member states to respect fundamental rights and freedoms, including expropriation claims.[39] While the Charter of Fundamental Rights (the EU federal "bill of rights"), among others, does provide for the protection of property,[40] it is, in principle, applicable to the institutions and bodies of the European Union and applies to member states only when and to the extent they are implementing EU law.[41] Likewise, the general principles of law recognized by the CJEU (such principles being the precursors of the Charter) established requirements that were applicable to EU actors but not to member states.[42] The rationale behind this approach is that the Charter was not meant to control member states but to limit the power of the "federal" government; as, in a democratic society, no public authority may exist without human rights limits, the CJEU established very early that the European Union has to respect human rights even if those rights are not explicitly provided for in

35 See Hanno Wehland, "Intra-EU investment agreements and arbitration: is European Community law an obstacle?" (2009) 58 Intl & Comp L Q 297 at 315–317; CJEU, *D. v Inspecteur van de Belastingdienst/Particulieren/Ondernemingen buitenland te Heerlen*, C-376/03, [2005] ECR I-05821, paras 59–62; CJEU, *Test Claimants in Class IV of the ACT Group Litigation v Commissioners of Inland Revenue*, C-374/04, [2006] ECR I-11673, paras 90–93.

36 For an analysis of the convergence between human rights protection and BITs, see Timothy G Nelson, "Human rights law and BIT protection: areas of convergence" (2011) 12(1) J World Investment & Trade 27.

37 Copenhagen criteria, established by the European Council in Copenhagen on 21–22 June 1993 (Conclusions of the Presidency), Doc No SN 180/1/93 REV 1.

38 According to article 2 TEU, the European Union "is founded on the values of respect for human dignity, freedom, democracy, equality, the rule of law and respect for human rights, including the rights of persons belonging to minorities." EC, *Treaty on European Union*, [2002] OJ, C 325/5, art 2.

39 See e.g. András Jakab, "Supremacy of the EU Charter in National Courts in Purely Domestic Cases" in András Jakab and Dimitry Kochenov, eds, *The Enforcement of EU Law and Values: Ensuring Member States' Compliance* (Oxford: Oxford University Press, forthcoming), online: <ssrn.com/abstract=2512865>; Michael Dougan, "Judicial review of Member State action under the general principles and the Charter: defining the 'scope of Union law'" (2015) 52 CML Rev 1201.

40 EC, *Charter of the Fundamental Rights of the European Union*, [2000] OJ, C 364/01, art 17.

41 The scope of the charter is based on the principle that the federal bill of rights applies to the federal government and the national bill of rights applies to the national government. According to article 51(1) of the charter, "[t]he provisions of this Charter are addressed to the institutions and bodies of the Union with due regard for the principle of subsidiarity and to the Member States only when they are implementing Union law." Article 51(2) emphasizes that the "Charter does not establish any new power or task for the Community or the Union, or modify powers and tasks defined by the Treaties." See Koen Lenaerts, "Exploring the limits of the EU Charter of Fundamental Rights" (2012) 8:3 Eur Const L Rev 375 at 377: "However, from the fact that the Charter is now legally binding it does not follow that the EU has become a 'human rights organisation' or that the ECJ has become 'a second European Court on Human Rights' (ECtHR)."

42 See Piet Eeckhout, "The EU Charter of Fundamental Rights and the Federal Question" (2002) 39 CML Rev 945 at 958–69.

EU law. This culminated in the Charter, which, likewise, was not meant to be a general human rights "watchdog" but a clog on the EU's "federal" government.[43]

Although the CJEU has interpreted the term "implementing Union law" fairly widely,[44] the core principle of the EU constitutional architecture was not called into question. It is worth referring to the CJEU's judgment in *Siragusa*,[45] where the court encountered a genuine investment protection case: Siragusa made alterations to his property in a landscape conservation area and was ordered to restore the site to its former state; he argued that the acts of Italy impaired his right to property enshrined in article 17 of the Charter. It is easy to parallel this fact pattern with the archetype of investor protection cases.

The CJEU came to the conclusion that the Italian authorities were not implementing EU law[46] and confirmed that the purpose of the Charter is to ensure the protection of fundamental rights in the sphere of EU activity (that is, it is not meant to shelter fundamental rights from member states in general).[47]

Taking the above constitutional architecture into account, it is easily understandable that investors are hesitant to accept the argument that intra-EU BITs are superseded by EU law, where, as far as member state action is concerned, EU law provides for no substantive protection of property, and that they perceive the revocation of the BITs as an impairment of their legitimate expectations. In this sense, intra-EU BITs are an element of the European Union's big human rights question; thus, the predicament should be solved as part of that.

An alternative way of making intra-EU BITs redundant would be the creation of an EU-wide investment protection system.[48] Such a regional duplicate could indeed do away with the problem, but it would also confirm that fundamental rights are not protected effectively in the European Union and may also interfere with the endeavours to find the proper arrangement for protecting human rights against member states.

The debate is expected to be put to rest (at least as far as EU law is concerned), as on March 3, 2016, the German Federal Supreme Court (Bundesgerichtshof) submitted a preliminary question to the CJEU concerning the general compatibility of intra-EU BITs with EU law.[49]

Can State Acts Mandated by EU Law Violate BITs?

A large number of intra-EU investment disputes emerged from cases in which EU law (in particular, state aid law) nullified benefits granted before accession. The claimed benefits were lawfully promised but became unlawful subsequently, when the accession entered into force. In these cases, the state entered into an agreement with an investor (or created a legitimate expectation), and at or after the

43 See Filippo Fontanelli, "The implementation of European Union law by Member States under Article 5 1(1) of the Charter of Fundamental Rights" (2014) 20:2 Colum J Eur L 193 at 197–98:

> The story of how EU law has come to take human rights seriously is well known. Very roughly, it became clear that the economic focus of European Community (EC) law would not prevent possible encroachment on fundamental rights of the individual, including the right to property, which is at the core of the common market. Because of the primacy-plus-disapplication combination noted above, member states' courts — in particular, constitutional tribunals — stood up to avert the possibility that human-rights-blind Community law could displace fundamental rights guarantees. The risk was that the uniformity of EC law would be hostage to national preferences. To defuse this risk, the ECJ issued a reassurance and a promise. The reassurance was that Community law was inherently compatible with fundamental rights, in the form of general principles. The promise was that the ECJ would be tasked with reviewing, centrally, the validity of EC measures in relation to these ingrained principles, without any need for national courts to subject them to peripheral human rights review.

44 See e.g. *Åklagaren v Åkerberg Fransson*, C-617/10, ECLI:EU:C:2013:105.

45 CJEU, *Siragusa v Sicilia*, C-206/13, ECLI:EU:C:2014:126.

46 *Ibid* at para 30.

47 *Ibid* at para 31:

> [T]he objective of protecting fundamental rights in EU law, which is to ensure that those rights are not infringed in areas of EU activity, whether through action at EU level or through the implementation of EU law by the Member States. 32. The reason for pursuing that objective is the need to avoid a situation in which the level of protection of fundamental rights varies according to the national law involved in such a way as to undermine the unity, primacy and effectiveness of EU law…. However, there is nothing in the order for reference to suggest that any such risk is involved in the case before the referring court. 33. It follows from all the foregoing that it has not been established that the Court has jurisdiction to interpret article 17 of the Charter.

48 See Lavranos, *supra* note 33 at 305.

49 Bundesgerichtshof, Decision, 3 March 2016, Case No I ZB 2/15. The decision (in German) can be found online: <juris.bundesgerichtshof.de/cgi-bin/rechtsprechung/document.py?Gericht=bgh&Art=pm&Datum=2016&Sort=3&nr=74612&linked=bes&Blank=1&file=dokument.pdf>. In its reference, the BGH posed questions as to the compatibility of BITs with articles 344, 267 and 18 TFEU.

accession it was established that this arrangement contained illegal state aid and had to be abolished. This appears to be a temporary issue, as in the event benefits are promised and nullified after the accession, it can easily be argued that the investor should have been aware of the illegality or at least the riskiness of the benefit.[50]

It is worthy of note that cases involving an EU member state and a third country are governed by article 351 TFEU, which provides that rights and obligations arising from treaties with third countries that precede accession "shall not be affected by the provisions of the Treaties."[51] In *Commission v Slovak Republic*,[52] the CJEU held that benefits protected by Slovakia's BITs and the Energy Charter Treaty (ECT)[53] antedating accession persist under article 351 TFEU.[54]

In a federal state, the above scenario would entail no problem of interpretation: as a rule of thumb, the power to enter into BITs is vested in the federal government, which cannot refer to internal legal inconsistencies to escape liability. However, in these cases, the BIT was concluded by the member state, while the withdrawal of the benefit was mandated by the European Union.

This raises, for one thing, questions of supremacy:[55] obviously, no problem emerges if EU law enters into force with immediate effect and prevails over benefits legally protected by BITs. If BITs are not outright abolished (and, hence, the benefits concerned are not nullified), the question to be answered is whether the "defense of superior orders" provides immunity to member states, as the incriminated decision was made by the EU and not the national government.

Furthermore, the global picture is even more intricate, as arbitral awards may have to be recognized and enforced, and this may occur either in the European Union (where courts are bound by EU law) or outside the European Union. Notably, the ICSID Convention does not enable national courts to reject the recognition and enforcement of investment awards with reference to public policy. In fact, courts of the place of enforcement have, in essence, no review powers over such awards. Hence, arguably, arbitral tribunals may disregard EU law and still adopt an enforceable award.

The Commission has championed the theory that, due to EU law's supremacy, benefits nullified on the basis of EU state aid law may give rise to no valid claims. On the other hand, tribunals have consistently rejected judging the question on the basis of EU law's supremacy, although they adopted diverging approaches regarding the "defense of superior orders."

In *Electrabel SA v Hungary*,[56] the tribunal, in essence, came to the conclusion that the termination, through a national legislative act, of the investor's long-term power purchase agreements with MVM (the Hungarian national electricity giant)[57] was not attributable to Hungary, since this was mandated

50 Eilmansberger, *supra* note 22 at 418–19.

51 TFEU *supra* note 24, art 351:

> To the extent that such agreements are not compatible with the Treaties, the Member State or States concerned shall take all appropriate steps to eliminate the incompatibilities established. Member States shall, where necessary, assist each other to this end and shall, where appropriate, adopt a common attitude. In applying the agreements referred to in the first paragraph, Member States shall take into account the fact that the advantages accorded under the Treaties by each Member State form an integral part of the establishment of the Union and are thereby inseparably linked with the creation of common institutions, the conferring of powers upon them and the granting of the same advantages by all the other Member States.

52 *Commission v Slovak Republic*, C-265/09, [2011] ECR I-08065 [Slovak Republic].

53 *Energy Charter Treaty,* 17 December 1994, 2080 UNTS 95, 34 ILM 360 (entered into force 16 April 1998) [ECT].

54 In 1997, ATEL, a Swiss company, was granted preferential access to the electricity grid in Slovakia. The Commission launched an infringement procedure against Slovakia due to discriminatory treatment. However, the CJEU held that "the preferential access granted to ATEL may be regarded as an investment protected by the Investment Protection Agreement and that, under the first paragraph of Article 351 EC, it cannot be affected by the provisions of the EC Treaty" (Slovak Republic, *supra* note 52 at para 51); "even if it were to be assumed that the preferential access granted to ATEL were not compliant with Directive 2003/54, that preferential access is protected by the first paragraph of Article 351 EC" (*ibid* at para 52).

55 Tamás Kende, "Arbitral Awards Classified as State Aid under European Union Law" (2015) 3:1 ELTE LJ 37 at 48.

56 Award, 25 November 2015, ICSID Case No Arb/07/19 [*Electrabel*].

57 In the mid-1990s, Hungary privatized its power plants. The claimant purchased the majority of the shares in Dunamenti power plant and invested considerable funds for the purpose of retrofitting. Dunamenti had a long-term power purchase agreement with MVM, the Hungarian national electricity company. Such contracts were common at that time and were meant to back the privatization of the power stations: these facilities needed significant retrofitting, and the long-term power purchase contracts were meant, in economic terms, to guarantee the investors that they would be able to sell the electricity they produced (note that, at that time, MVM was the only purchaser of electricity in Hungary and remained a super-dominant undertaking also after the electricity market was opened).

by the Commission's formal decision.[58] Hence, Hungary was not the proper respondent to be sued to the extent its acts were determined by the Commission's state aid decision ("defense of superior orders"). The award suggests that the EU should have been sued instead. However, the tribunal did investigate (although done to implement the Commission decision) those acts as to which Hungary had a certain leeway; these were regarded as Hungary's own acts.

The claimant's expropriation claim was summarily rejected: the power purchase agreement itself was not considered to be a protectable investment, and its termination did not deprive the claimant's investment in the power plant of its value.[59] Hence, the case centred around the ECT's "treatment" provisions.

The tribunal established that the relationship between the ECT and EU law is somewhat special, hence, "the ECT should be interpreted, if possible, in harmony with EU law."[60] As well, the tribunal came to the conclusion that "there can be no practical contradiction between the ECT and EU law in regard to the [Commission's] Final Decision" — "the ECT does not protect the claimant, as against the Respondent, from the enforcement by the Respondent of a binding decision of the European Commission under EU law."[61] However, the European Union itself is not shielded from liability under the ECT.[62]

Nonetheless, the tribunal also established that the immunity Hungary enjoyed as a result of the Commission's state aid decision ranges only to the point where it has no autonomy of action.[63] Once a particular detail is left to the discretion of the member state or is not spelled out by the Commission's decision, the member state's individual liability emerges and the tribunal will scrutinize this under the applicable standards.[64]

Contrary to the above, in *EDF International SA v Hungary*,[65] which was launched by another investor but based on the same fact pattern as *Electrabel*, the tribunal decided for the claimant (in an ad hoc arbitral proceeding conducted under the United Nations Commission on International Trade Law [UNCITRAL] rules).[66] Unfortunately, the award is not publicly available, so the tribunal's arguments cannot be reconstructed.

In *Micula v Romania*,[67] the tribunal condemned Romania for withdrawing certain benefits, although this was mandated by EU state aid law. This case presents the clash between BITs and EU law spectacularly, demonstrating the vicious circle[68] encapsulated in this issue: after Romania provided compensation to the claimants (as ordered by the tribunal), the Commission established that the compensation qualified as state aid (stepping into the place of the illegal subsidy it was meant to make up for) and ordered Romania to recover the original financial benefit provided.

58 EC, *Commission decision of 4 June 2008 on the State aid C 41/05 awarded by Hungary through Power Purchase Agreements* (notified under document C(2008) 2223), [1999] OJ, L 225/53 [*Hungary Decision*].

59 *Ibid* at paras 6.53, 6.57–6.58.

60 *Ibid* at para 4.130. First, the European Union and its member states were closely involved in the adoption of the ECT, and according to article 207(3) TFEU, the Council and the Commission have to ensure that "the agreements negotiated are compatible with internal Union policies and rules" (paras 4.135–136). Second, the ECT and the European Union have similar objectives: the ECT "is an instrument clearly intended to combat anti-competitive conduct, which is the same objective as the European Union's objective in combating unlawful State aid" (para 4.133). See also paragraphs 4.137 and 4.141. Third, the tribunal also established (para 4.142) that the ECT implicitly recognized that Commission decisions are binding on all member states. See ECT, *supra* note 53, art 1(3): "A 'Regional Economic Integration Organization' means an organization constituted by states to which they have transferred competence over certain matters a number of which are governed by this Treaty, including the authority to take decisions binding on them in respect of those matters."

61 *Electrabel*, *supra* note 56 at para 4.169.

62 *Ibid* at para 4.170.

63 *Ibid* at paras 4.191, 4.196.

64 *Ibid* at paras 6.72, 6.76. Hungary created a scheme for establishing the net stranded costs and for compensating the power plants for these (in case these had not been recovered). The tribunal found that Hungary's own acts were in line with the applicable standards; however, since the last stage of this scheme was still to be carried out at the time of the award, the tribunal reserved the right to decide on this in another award (paras 6.108–109, 6.118). *Cf* Eilmansberger, *supra* note 22 at 413: "The EC law origin of the measure cannot exculpate the host State if it had some discretion as to the interpretation or application of the EC law provisions in question. Relevant BIT investment protection guarantees oblige Member States to exercise this discretion in the most investor-friendly (and investment-sparing) way."

65 Award, 4 December 2014 (UNCITRAL) (Arbitrators: Karl-Heinz Böckstiegel, chair, Pierre-Marie Dupuy, Albert Jan van der Berg).

66 See Douglas Thomson, "EDF wins claim against Hungary" 11 December 2014, online: Global Arbitration Review <globalarbitrationreview.com/news/article/33251/edf-wins-claim-against-hungary/>.

67 See *Micula*, *supra* note 1; "EC Romania Press Release", *supra* note 1 *Micula* (General Court), *supra* note 1.

68 Kende, *supra* note 55 at 50–51 (circularity argument).

The dispute emerged in the context of Romania's introduction and subsequent revocation (during the accession negotiations) of certain economic incentives for companies operating in underdeveloped regions.[69] The tribunal established that there was no real conflict between the BIT and EU law, since at the relevant moment Romania was in the negotiation stage and not subject to EU law.[70]

The tribunal held that notwithstanding the fact that Romania's conduct was, for the most part, reasonable and "appropriately and narrowly tailored in pursuit of a rational policy" (i.e., EU accession), it did undermine the investors' "legitimate expectations with respect to the continued availability of the incentives" and, hence, qualified as unfair or inequitable and was not sufficiently transparent.[71] Romania, with the support of the Commission, sought ICSID annulment of the award, but its plea was rejected.[72]

The disagreement between the decisional practice of arbitral tribunals and the Commission's stance brings about a vicious circle. In *Micula*, after the tribunal rejected the "defense of superior orders" and ordered Romania to pay compensation, the Commission established that the compensation paid for the termination was the equivalent of the illegal state aid it was to make up for.[73] Hence, the beneficiaries were ordered to return the financial benefits received.[74] As the claimants (beneficiaries) appealed to the General Court,[75] it was hoped that the EU judiciary would soon put an end to this headache-producing controversy. However, recently, the applicants withdrew the claim and, hence, the court removed the case from the register.

Nonetheless, it is dubious whether the Commission's efforts are capable of providing watertight protection to member states against their monetary liability for acts adopted in defiance of investment law. Outside the realm of the ICSID Convention (in cases conducted, for instance, under the Arbitration Rules of the Stockholm Chamber of Commerce (SCC), the International Chamber of Commerce Arbitration Rules or UNCITRAL), public policy may serve as a valid defence for the state under the 1958 New York Convention, bilateral agreements or domestic law. However, articles 53 and 54 of the ICSID Convention exclude the review of ICSID awards (which are not subject to any appeal and any public policy review).[76] Accordingly, at least under the ICSID Convention, recognition and enforcement cannot be rejected with reference to public policy.[77]

Although, in *Eco Swiss China Time Ltd v Benetton International NV*,[78] the CJEU held that national courts have to enforce EU public policy in procedures for the annulment of arbitral awards, it also made it clear that this obligation persists only if national law does require the court "to grant an application for annulment founded on failure to observe national rules of public policy."[79] To put it otherwise,

69 Claimants argued that they made substantial investments in the legitimate expectation that these benefits would persist for a 10-year period. During Romania's accession negotiations, the European Union invited Romania to put an end to the subsidy schemes incompatible with EU state aid law; and Romania terminated the incentives in question as from February 22, 2005 (although they were supposed to persist until April 1, 2009). Romania's accession to the European Union entered into force on January 1, 2007, so the incentives were terminated 2.25 years before EU law became applicable in the host country. While the Commission's position expressed during the negotiations was clear, no formal decision required Romania to revoke the incentives, and, in fact, no such formal decision could have been rendered, since during the relevant period Romania was not a member state; however, the Commission made the termination of the subsidies a precondition of accession.

70 *Micula*, *supra* note 1 at para 319.

71 *Ibid* at para 827. Romania failed "to inform the claimants in a timely manner that the regime would be terminated prior to its stated date of expiration" *(ibid)*.

72 *Micula v Romania*, Decision on Annulment, 26 February 2016, ICSID Case No ARB/05/20.

73 See EC, *Commission Decision (EU) 2015/1470 of 30 March 2015 on State aid SA.38517 (2014/C) (ex 2014/NN) implemented by Romania – Arbitral award Micula v Romania of 11 December 2013 (notified under document C(2015) 2112)*, [2015] OJ, L 232/43 at 43–70: "Article 1: The payment of the compensation awarded by the arbitral tribunal established under the auspices of the International Center for Settlement of Investment Disputes (ICSID) by award of 11 December 2013 in Case No ARB/05/20 Micula a.o. v Romania…constitutes State aid within the meaning of Article 107(1) of the Treaty which is incompatible with the internal market. Article 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."

74 *Micula*, *supra* note 1; "EC Romania Press Release", *supra* note 1.

75 *Micula* (General Court), *supra* note 1.

76 ICSID Convention, *supra* note 3, arts 53, 54. It is to be noted that arbitral proceedings under the ICSID Additional Facility Rules do not benefit from this protection.

77 *Cf* Eilmansberger, *supra* note 22 at 427–428.

78 C-126/97, [1999] ECR I-03055.

79 *Ibid* at para 1 of the operative part. "A national court to which application is made for annulment of an arbitration award must grant that application if it considers that the award in question is in fact contrary to Article 101 TFEU, where its domestic rules of procedure require it to grant an application for annulment founded on failure to observe national rules of public policy."

it is a precondition that national law provide for the possibility of public policy review.[80] The ICSID Convention does not provide for such a possibility.

Notwithstanding the above, the enforceability of arbitral awards falling foul of EU state aid law has given rise to diverging interpretations. The Commission, at numerous occasions, advanced (as amicus curiae) that an award going counter to EU law would not be enforceable in the European Union.[81] This position did have an impact on national judicial practice. On January 26, 2016, the Court of First Instance of Brussels pronounced an arbitral award unenforceable with reference to the violation of EU state aid law.[82] However, it should not be ignored that the ICSID Convention creates a global system and the judgment creditor, as a matter of course, may seek enforcement outside the European Union, where the Commission's arguments may have less persuasive authority. This took place in *Micula*, in which, in April 2015, the ICSID award was converted into a judgment.[83] Currently, the appeal is pending before the US Court of Appeals for the Second Circuit.[84]

"TREATMENT" MATTERS AND REGULATORY AUTONOMY

Genuine expropriation claims against Central European countries have been relatively rare. Most cases have been primarily based on the BITs' "treatment" provisions. These cases centred around state intervention into the market (for example, price regulation), the fairness of national (administrative or judicial) procedures, public tenders or contractual disputes. While tribunals have been fairly deferential, they have not been reluctant to review national administrative and judicial procedures and civil law disputes.

An allegedly common feature of the Central European region is the state's strong market role,[85] which may appear in the form of intensive state intervention in the operation of the market and intrusive trade regulation. This allegedly intensive state intervention (although it does not qualify as direct or indirect expropriation) occasionally gave rise to claims on the basis of the BITs' "treatment" provisions.

In *AES Summit Generation Limited, AES-Tisza Erőmű Kft v Hungary*,[86] the dispute arose from Hungary's reintroducing regulated prices. AES Summit purchased AES-Tisza (at that time Tiszai Erőmű Részvénytársaság) in 1996 and agreed to complete a retrofit of the power plant's existing units and to construct a new power plant. MVM, Hungary's electricity monopoly, entered into power purchase contracts that set the price according to a contractual formula. After the prices charged by AES-Tisza to MVM entailed a general outcry, Hungary introduced regulated prices.

The claimants' expropriation claims were summarily rejected: although the regulated prices decreased profitability, they did not deprive the investment of its value.[87] The price regulation was also tested under the treatment standards (fair and equitable treatment, unreasonableness and discrimination). However, the tribunal was fairly deferential and rejected the claims. The claimants' reference to the frustration of legitimate expectations was rejected because Hungary made no specific promise not to regulate prices.[88] Interestingly, at the relevant time, Hungary was, in the form of MVM, the dominant buyer of electricity, and although the legislative act (decree) was of general application, it affected (also) the contractual relationship between MVM and AES-Tisza. As to due process, arbitrariness and transparency, the tribunal established that not all imperfections amount to a failure to provide fair and equitable treatment.[89] The tribunal concluded that Hungary's "process of introducing the Price Decrees, while sub-optional, did not fall outside the acceptable range of legislative and regulatory behavior."[90]

80 For a contrary view, see the European Commission's *amicus curiae* opinion in *Electrabel*, *supra* note 56 at paras 5.18–5.19.
81 See e.g. *Eureko*, *supra* note 26 at paras 175–96; *Micula*, *supra* note 1 at paras 316–317; *Electrabel*, *supra* note 56 at paras 4.89–4.110, 5.8–5.20.
82 Judgment, 26 January 2016, the Court of First Instance of Brussels (Tribunal de première instance francophone de Bruxelles – Juge des Saisies) Case No RG 15/7242/A.
83 See *Micula v Romania*, 2015 WL 5257013 (SDNY); *Micula v Romania*, 2015 WL 4643180 (SDNY).
84 Case No 15-3109.
85 For an analysis of the intensity of market competition and the intensity of state control over competition in Central Europe, see Beáta Farkas, "The Central and Eastern European Model of Capitalism" (2011) 23:1 Post-Communist Economies 15 at 17–19, online: <ssrn.com/abstract=1965290>.
86 Award, 29 June 2012, ICSID Case No ARB/07/22.
87 *Ibid* at paras 14.3.1–14.3.4.
88 *Ibid* at para 9.3.26.
89 *Ibid* at para 9.3.40.
90 *Ibid* at para 9.3.73.

The tribunal, using a fairly deferential standard, also dismissed the claim that Hungary impaired the investment by unreasonable and discriminatory measures.[91] The tribunal afforded Hungary a very wide margin of appreciation as to whether the measure served a legitimate end.[92] The tribunal accepted Hungary's argument that power plants (including AES-Tisza) were afforded excessively high profits under the power purchase agreements, entailing higher burdens for consumers.[93] Hence, regulation of the prices served a legitimate end[94] and was reasonable, proportionate and consistent with the public policy pursued;[95] it ensured the claimants a reasonable return[96] and was not discriminatory.[97]

In *Electrabel SA v Hungary*,[98] the tribunal considered that the claimant could not legitimately expect Hungary not to introduce regulated prices[99] and rejected the claimant's allegations that the introduction of price regulation was backed by populist politics: according to the tribunal, political rhetoric is part of the democratic process and does not overshadow rational policy considerations.[100]

In *United Utilities (Tallinn) BV v Estonia*,[101] the dispute resulted from the Estonian competition authority's refusal to approve the price hikes proposed by Tallinna Vesi (a water supply company operating in Tallinn). Tallinna Vesi and the city of Tallinn entered into a contract that determined the prices, connecting tariff hikes to the change in the consumer price index. The Public Water Supply and Sewerage Act (enacted subsequent to the conclusion of the contract) subjected tariff changes to the competition authority's approval and followed the "justified costs plus reasonable margin" test. Relying on this test, the competition authority disapproved the tariff hikes proposed by Tallinna Vesi, which commenced arbitration claiming compensation for the enterprise's losses. The case is pending before the ICSID.

A considerable part of the investor-state disputes launched against Central European countries concerns national legal proceedings, regulated tenders and civil law matters.

In *Nordzucker AG v Poland*,[102] the tribunal rejected the claimant's complaints, which were submitted because of Poland's rejection of extending privatization and of alienating further shares in a partially privatized enterprise. The dispute arose from Poland's decision to stop the privatization of the sugar industry. Poland allegedly stepped back from the sale of two state-owned Polish sugar plants during the privatization of the Polish sugar sector. The investor acquired sugar plants accounting for eight percent of the Polish sugar market. It argued that it had legitimate expectations to acquire further sugar plants. These further acquisitions would have increased the investor's market share to 20 percent. The arbitral tribunal rejected the claims, establishing that the claimant had no legitimate expectation to acquire further sugar plants, Poland negotiated in good faith and its decisions were not arbitrary.

In *Binder v Czech Republic*,[103] the tribunal was called upon to review the fairness of the investigations and procedures carried out by the Czech customs authorities. The claimant was the customs guarantor for the debts of a company, which failed to pay its customs debts, and this allegedly made the claimant's company bankrupt.

Dan Cake (Portugal) SA v Hungary[104] is one of the very rare cases where a state was condemned for a judicial error. The Hungarian bankruptcy court opened a bankruptcy proceeding against the claimant's subsidiary in Hungary, Danesita. With the help of its parent company, Danesita reached agreements with various creditors and requested that the court convene a "composition hearing" to enter into

91 *Ibid* at para 10.3.7.

92 *Ibid* at para 10.3.8: "[a] rational policy is taken by a state following a logical (good sense) explanation and with the aim of addressing a public interest matter."

93 *Ibid* at paras 10.3.20, 10.3.23–24, 10.3.31.

94 *Ibid* at para 10.3.34.

95 *Ibid* at para 10.3.36.

96 *Ibid* at paras 10.3.37, 10.3.44.

97 *Ibid* at paras 10.3.45, 10.3.47.

98 *Electrabel, supra* note 56.

99 *Ibid* at para 8.18.

100 *Ibid* at para 8.23.

101 *United Utilities*, *supra* note 26.

102 *Nordzucker v Poland*, Partial Award, 10 December 2008; Second Partial Award, 28 January 2009; Third Partial and Final Award, 23 November 2009 (UNCITRAL).

103 *Binder v Czech Republic*, Award on Jurisdiction, 6 June 2007 ; Final Award, 15 July 2011 (UNCITRAL).

104 Decision on Jurisdiction and Liability, ICSID Case No ARB/12/9.

a compromise with the creditors. However, the court rejected the request for a hearing.[105] Shortly thereafter, the sale of Danesita's factory was announced by the liquidator. The tribunal established that the rejection to convene a hearing amounted to a "flagrant violation" of Hungarian law;[106] and although "[i]t is impossible…to determine whether a composition agreement would have been reached if a composition hearing had been convened," this deprived the claimant of the fair and equitable treatment (in the form of denial of justice).[107]

In *Nykomb v Latvia*,[108] the investor's subsidiary, Windau, constructed a power plant and entered into a power purchase agreement with Latvenergo (the single buyer of electric power in Latvia). The price was regulated by Latvian law, which provided for a double tariff for a period of eight years as from the plant being put into operation. Subsequently, the law was amended and provided for a 0.75 tariff. After Latvenergo refused to pay the double tariff, Nykomb launched arbitral proceedings with reference to the ECT's treatment provisions (fair and equitable treatment, prohibition of arbitrary and discriminatory measures, etc.).

The tribunal established that Windau had both a statutory and a contractual right to the double tariff (i.e., the power purchase contract not only referred to the tariff set by the law but also incorporated these tariffs, creating an independent contractual basis). While the statutory right was revoked by Latvia, Latvenergo could have (and should have) honoured its contractual obligation to pay the double tariff. Although this facet of the case appeared to be a genuine contractual dispute, the tribunal condemned Latvia, attributing Latvenergo's breach of contract to the Latvian state.[109] The tribunal established that, for a period of eight years, Latvenergo was obliged to pay a double tariff, and the failure to pay a double tariff was attributable to Latvia.[110] It was also established that the non-payment was discriminatory, as Latvenergo did pay a double tariff to two other Latvian power plants.

In *Vigotop Ltd v Hungary*,[111] the claimant envisaged constructing a casino (King City), and, for this purpose, concluded a concession agreement with Hungary. The annex of this agreement listed numerous locations and provided that the casino could be constructed at any of them. Before the publication of the call for tenders, the claimant concluded a land swap agreement to acquire title over a plot near Sukoró (one of the plots subsequently listed in the tender). The claimant's project company was announced as the tender's winner.[112] Two hours after the concession contract was signed, the ministry of finance issued a press release stating that negotiations would be started as to the Sukoró land swap "with the aim of restoration of the original — pre-land-swap condition."[113] In the end, the Hungarian court established that the acquisition of the Sukoró site was illegal and ordered the restoration of the initial status.[114] Although the claimant could have chosen any of the plots listed in the concession agreement's annex (which listed 133 locations),[115] it insisted on constructing the casino on the Sukoró site and secured no other site for the purpose of the concession contract. As a corollary, Hungary terminated the

105 *Ibid* at para 54.

106 *Ibid* at para 142: "It also results from the above analysis of the decision that it was rendered in flagrant violation of the Bankruptcy Act and that it purported to condition the mandatory convening of the hearing upon several requirements, all of which were unnecessary; two of which were in direct violation of Dan Cake's creditor rights; and at least one of which was impossible to satisfy within a reasonable time."

107 *Ibid* at paras 142, 146.

108 Arbitral Award, 16 December 2003, Arbitration Institute of the SCC.

109 See *ibid* at 26: "[A]s may be derived from the court decisions in the Latelektro-Gulbene case, the price clauses in the purchase contracts are not merely references to Latvian laws and regulations at any time, but these clauses are deemed by the highest legal authority, the Latvian Supreme Court, to be legally binding contractual obligations under Latvian law"; see also *ibid* at 29–31.

110 For an analysis of the attribution of the acts of state-owned enterprises to the state see Michael Feit, "Responsibility of the state under international law for the breach of contract committed by a state-owned entity" (2010) 28 BJIL 142.

111 Award, 1 October 2014, ICSID Case No ARB/11/22 [*Vigotop*].

112 *Ibid* at para 127.

113 *Ibid* at para 154.

114 *Ibid* at para 198. Under Hungarian law, state-owned arable can be alienated only through a public tender; however, this requirement does not apply if the state wishes to acquire a land "for the purposes of public utility infrastructure projects or for some other reason of public interest" — in this case, a land swap is possible. Blum, in order to secure a proper site for the casino for the purposes of the concession contract, wanted to acquire the Sukoró site. He had three plots in Albertirsa. It was established that the bypass section of the M4 motorway (which was under contract at that time) touched two of these properties. The MNV (Hungarian national asset management corporation) concluded a land swap contract with Blum, in which the latter transferred title over the three properties and paid a certain amount of money to the MNV, while the MNV transferred title over the Sukoró plot. However, the Hungarian Supreme Court (Kúria) established, in November 2012, that the land swap agreement was null and void, since it violated section 13(4) of *Act CXVI of 2001 on National Land Fund*: it was justified neither by "the purposes of public utility infrastructure projects" nor by "some other reason of public interest." The construction of the M4 motorway concerned only two of the three plots, and, even as to the latter, the interference of the M4 motorway was minimal.

115 *Ibid* at para 145.

concession agreement and demanded the payment of a penalty as stipulated in the contract. The legal dispute concerning the termination was pending at the time of the ICSID proceeding.

The matter's pivotal legal question was whether Hungary's termination of the concession contract came under the scope of the applicable BIT. Namely, Hungary's termination of the contract was a private act, giving rise to a purely contractual dispute.[116] However, the tribunal did not shy away from adjudicating the commercial dispute. It examined whether Hungary had public policy reasons (contrary to purely contractual ones) to terminate the contract, whether the termination had a contractual basis and whether it was legitimate (i.e., whether Hungary acted in good faith). Although Hungary was afforded some deference, the tribunal's analysis suggests that it was willing to scrutinize the private law issues in parallel to and independently of any national court judgment.[117] Finally, the tribunal found that Hungary had a solid contractual ground to terminate the concession agreement and exercised its right in good faith. The claimant failed to secure a suitable plot for the purpose of the concession contract.[118]

SUMMARY AND CONCLUSIONS

Central European member states follow a relatively uniform approach to ISA. All of them entered into numerous standard BITs with various EU and non-EU countries, and, with the exception of Poland, all of them are parties to the ICSID Convention. This uniformity suggests that BITs and ISA have had no alternative in the region. Although Hungary recently introduced a set of anti-arbitration provisions, which also concerned investor-state disputes, it later felt compelled to revoke these due to economic considerations. Hungary's attempt to defy the settled pattern of investor-state dispute resolution demonstrates how difficult (or even impossible) it is to square unilateralism with the current framework of international economic relations.

The accession of Central European countries to the European Union brought to light the problem of intra-EU BITs. While investment tribunals have consistently followed the approach that EU law does not overrule intra-EU BITs, the European Commission launched infringement proceedings with the aim of uprooting bilateral investment protection from European "domestic" matters. As investment arbitration is a global regime, the Commission's approach may be feasible only if it is reflected outside the European Union as well, especially in the judicial practice of recognition and enforcement. However, as the ICSID Convention does not allow for public policy review, it is expected that European regionalism, without specific action, may not triumph over investment arbitration's globalism.

Although intra-EU BITs may at first glance appear to be only a technical issue, in fact they go to the heart of European integration. It is submitted that the cause of the controversy is the lack of an effective EU mechanism for the protection of human rights, including the right to property. While the effective protection of investments is at the core of BITs, this is not reproduced in EU law, at least not on the level guaranteed in BITs. Taking this into account, it is difficult to argue that, as a matter of practice, the subject matters of BITs and EU law considerably overlap. It is submitted that the problem of intra-EU BITs could be satisfactorily solved only as part of the European Union's general human rights question.

Most of the claims submitted against Central European member states have centred around "treatment" issues. Genuine expropriation claims have been rare. Most matters have involved state intervention into the competitive process, fair trial (due process) grievances and contractual disputes. While tribunals have been fairly deferential, they have been consistently willing to engage in reviewing the above measures.

The arbitral practice may suggest that the arbitral tribunals' extraordinarily wide powers are not necessarily backed by an ossified decisional practice. Arguably, the extremely high stakes involved in investment arbitration would call for a consistent and predictable system based on transparency and institutional legitimacy, while the contradictory decisional practice of arbitral tribunals may undermine the system's reputation. For instance, as regards member states' liability for acts mandated by EU law,

116 *Ibid* at para 312.
117 *Ibid* at paras 328–31.
118 *Ibid* at para 634.

in *Electrabel SA v Hungary*, the tribunal essentially accepted the "defense of superior orders,"[119] while in *EDF International SA v Hungary*, which was based on the same state aid saga, this defence was rejected.

As to whether the jurisdiction of investment arbitration extends to purely contractual claims, Central European experiences show a similar inconsistency. It has been a long-standing, settled practice in investment arbitration that "[a] treaty cause of action is not the same as a contractual cause of action; it requires a clear showing of conduct which is in the circumstances contrary to the relevant treaty standard,"[120] and it is "the exercise of its sovereign authority (*puissance publique*)" and not contractual rights that is subject to the jurisdiction of investment arbitration.[121] On the other hand, the *Vigotop* tribunal had no scruples about scrutinizing whether Hungary's use of its contractual rights was justified by the contract or not. While such contradictions are inherent in schemes based on ad hoc bodies and proceedings, they may obviously undermine the system's credibility and legitimacy.

119 *Electrabel, supra* note 56 at para 4.169.

120 *Compañia de Aguas del Aconquija SA v Argentina*, Decision on Annulment, 3 July 2002, ICSID Case No ARB/97/3 at para 113.

121 *Salini v Jordan*, Award, 31 January 2006, ICSID Case No ARB/02/13 at para 155: "Only the State, in the exercise of its sovereign authority (puissance publique), and not as a contracting party, has assumed obligations under the bilateral agreement…. In other words, an investment protection treaty cannot be used to compensate an investor deceived by the financial results of the operation undertaken, unless he proves that his deception was a consequence of the behaviour of the receiving State acting in breach of the obligations which it had assumed under the treaty." See also *Siemens AG v Argentina*, Award, 6 February 2007, ICSID Case No ARB/02/8 at para 253: "What all these decisions have in common is that for the State to incur international responsibility it must act as such, it must use its public authority. The actions of the State have to be based on its "superior governmental power." It is not a matter of being disappointed in the performance of the State in the execution of a contract but rather of interference in the contract execution through governmental action."

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