Legal update

Sun to set on intra-EU Bilateral Investment Treaties

June 12, 2020
Alternative dispute resolution

On May 5, 2020, 23 EU member states signed the Agreement for the termination of bilateral investment treaties between the member states of the European Union (the Termination Agreement). The Termination Agreement sounds the death knell for the vast majority of bilateral investment treaties between member states, or intra-EU BITs, deemed incompatible with EU law.

Achmea and the end of intra-EU BITs

On March 6, 2018, the Court of Justice of the European Union (CJEU) released its much-awaited decision in Achmea, in which it concluded that investor-state arbitration clauses contained in intra-EU BITs are incompatible with EU law. Following this decision, the Termination Agreement recognizes that such “illegal” arbitration clauses are “inapplicable”: they cannot form the basis of a member state’s consent to arbitration proceedings. The rationale appears to be that, since the parties to these BITs are governed by EU law and EU law states they do not have the capacity or competence to enter into intra-EU arbitration clauses, such clauses are void ab initio. This inapplicability or invalidity operates retroactively from the date on which the last of the parties to the intra-EU BIT became a member state. For example, the arbitration clause in the Germany-Croatia BIT will have been invalid since July 1, 2013, date on which Croatia officially joined the EU.

The entry into force of the Termination Agreement will lead to an abrupt and full termination of all intra-EU BITs between Belgium, Bulgaria, Croatia, Republic of Cyprus, Czech Republic, Denmark, Estonia, France, Germany, Greece, Hungary, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, and Spain. Pursuant to Articles 2 and 3 of the Termination Agreement, all sunset clauses are also terminated “and shall not produce legal effects.”

All new arbitrations are invalid

The Termination Agreements applies to all investor-state arbitration proceedings based on intra-EU BITs, under any set of rules, including ad hoc arbitrations. However, it does not cover arbitrations brought under the Energy Charter Treaty or ECT, which will be dealt with at a later stage.3

Any new arbitration commenced on or after March 7, 2018, under a listed BIT is devoid of legal basis. Contracting parties to the intra-EU BIT at issue must inform the arbitral tribunal that, pursuant to the Achmea judgment and the Termination Agreement, the arbitration clause contained in the BIT is contrary to EU law and thus “inapplicable.” Contracting parties must also, when parties to related judicial proceedings, request that the competent national court, including in any third country, set aside or annul the arbitral award, or refuse to recognize and enforce it.
Pending arbitrations get complicated

These include any arbitration initiated prior to March 6, 2018, which has yet to be concluded, no matter its stage on the date the Termination Agreement enters into force. As such, even if a proceeding concludes before the Termination Agreement comes into force, it will still be considered to be “pending.” Just as with new arbitrations, contracting parties must inform the arbitral tribunal of the illegality of the underlying arbitration clause and request that any domestic court, including in any third state, set aside or annul any resulting award, or refuse to enforce it.

Under the Termination Agreement’s transitional provisions, the investor may ask the member state to enter into a “structured dialogue” with a view to amicable settlement. There are two conditions: (i) the pending arbitration must have been suspended at the investor’s request; and (ii) if an award has been issued, the investor must undertake not to commence proceedings to have it recognized or enforced in a member state or third country (or suspend any such ongoing proceedings). The investor has six months from the date of termination of the BIT at issue to initiate this “dialogue.”

A settlement procedure may only be entered into if the CJEU or a national court has found that the state measure at issue in the pending arbitration violates EU law. If the CJEU, a national court, or the European Commission find that the impugned state measure does not violate EU law, no settlement procedure may be entered into, regardless of whether the impugned measure would violate the BIT.

Investors may choose to access the national courts to resolve a pending arbitration, even if national time limits have expired, on the following conditions: (i) the investor withdraws the pending arbitration or renounces the enforcement of an existing award; and (ii) any claims made will be limited to those based on national or EU law. The provisions of any relevant BIT may not form part of the applicable law in such proceedings.

Concluded arbitrations are (sort of) safe

The Termination Agreement does not apply to Concluded Arbitrations, defined as any arbitration proceeding that settled or in which an award was issued prior to March 6, 2018, as long as the award was executed prior to that date (and there are no pending review, set-aside, annulment or enforcement proceedings as of March 6, 2018).

Awards that have not yet been executed and are within an applicable limitation period to be executed are not addressed in the Termination Agreement. They will likely be treated as pending arbitrations.

European Commission commences proceedings against holdout states

Austria, Ireland, Sweden, Finland, and the UK have not signed the Termination Agreement. It appears that Austria and Sweden are terminating their BITs bilaterally, while Ireland terminated its only intra-EU BIT (with the Czech Republic) in 2011. On May 14, the European Commission began infringement proceedings against both Finland and the UK “for failing to effectively remove intra-EU Bilateral Investment Treaties (BITs) from their legal orders.” Both states have been given 4 months to comply.

Although the UK left the European Union on January 31, 2020, EU law continues to apply in the UK during the 11-month transition period under the withdrawal agreement. That said, the effects of the Commission’s infringement proceedings are unlikely to have any teeth, given that the time between the Commission’s compliance deadline (September) and the UK’s full exit from the EU (January 2021) is only a matter of months. From a political perspective, it seems impractical for the UK to agree to terminate any existing BITs with EU member states that it wishes to maintain in the future, when such treaties will cease to be “intra-EU.”

What do we do now?

The Termination Agreement, which will come into force 30 days after the second ratification is deposited, leaves us with far more questions than answers. For example, what will arbitral tribunals do with it? To date, tribunals have consistently rejected arguments relating to state consent and the future impossibility of enforcement on the basis of the
However, the Termination Agreement may be deemed a new “fact” in pending or new arbitrations, justifying new or belated jurisdictional objections by the members states involved or the European Commission.\(^2\) Tribunals will also have to grapple with the apparent retroactive effect of the Termination Agreement on the validity of arbitration clauses, which runs afoul of the basic principle of the non-retroactivity of treaties.

Investors will need to be particularly mindful of the hard line being adopted by the contracting states and the European Commission – evidenced by the recent infringement proceedings – and of the immediate impacts on their rights.

First, the Termination Agreement explicitly – and repeatedly – states that sunset clauses are also terminated. This means that there will be no transition or “sunset” period once the Termination Agreement comes into force, despite any provisions to the contrary in the individual BITs at issue.

Second, under the Termination Agreement, investors may pursue remedies before EU national courts, but they can only invoke breaches of EU or national law. Any claims based on investment protections granted under the BIT or on national law. Any claims based on investment protections granted under the BIT or on international law will likely be rejected. Investors choosing to litigate rather than arbitrate their disputes will need to tailor their claims accordingly.

Most importantly, investors need to keep in mind that even if they clear the first hurdles and obtain an award against a contracting state, it may become increasingly difficult, not to say impossible, to enforce such an award. While third states are unlikely to react positively to being asked not to recognize or enforce otherwise valid arbitral awards (in breach of their own obligations under the New York and ICSID Conventions), the problem of actually collecting from EU member states will remain thorny. As we have seen through the Micula saga, the European Commission will aggressively pursue any member state it sees complying with an “incompatible” award and may even extend sanctions to the investors themselves.\(^6\) If the only assets against which an award could be enforced are located in the territory of an EU member state, any victory before the arbitral tribunal may thus prove to be theoretical at best.

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Footnotes


2. Under the framework of the New York Convention, the argument against recognition or enforcement of any ensuing award would be that, pursuant to Article V(1)(a), the parties to the arbitration agreement were, under the law applicable to them, under some incapacity when they entered into the agreement.


4. This would apply if the European Commission adopts a decision which has become definitive in which it finds that the impugned measure does not violate EU law.


6. The first known instance of a tribunal member declining jurisdiction on the basis of an intra-EU objection is found in the dissenting reasons of Marcelo Kohen dated February 7, 2020 in the decision on jurisdiction for the Adamakopoulos et al. v. Cyprus matter: https://www.italaw.com/sites/default/files/case-documents/italaw11284.pdf

7. For example, in the Micula v. Romania (II), the tribunal allowed Romania to file a new jurisdictional objection, a year after it had filed its Rejoinder, on the basis of the CJEU's Achmea decision, as this constituted a new “fact”. Ioan Micula, Viorel Micula and others v. Romania [II], ICSID Case No. ARB/14/29, at paras. 259 ff: https://www.italaw.com/sites/default/files/case-documents/italaw11284.pdf
In *Micula and Others v. Romania*, ICSID ARB/05/20, issued in December 2013, Romania was ordered to pay a sum equal to EUR 178 million. In a decision dated March 30, 2015, the European Commission concluded that to comply with this award would constitute a violation of EU law against illegal state aid. Romania was ordered not to pay out any amounts to the claimants and to recover any amounts previously disbursed. The claimants were deemed jointly liable to repay any so-called illegal state aid received from Romania.

On June 18, 2019, the General Court of the European Union held that the European Commission’s decision of March 2015 was invalid and annulled. The European Commission has since appealed to the CJEU, where the case remains pending.

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