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Over the past year, the European Commission (the Commission) has continued to take an interest in the relationship between bilateral investment treaties (BITs) and European Union (EU) law. During that time, there have been at least three notable developments. First, the European Court of Justice (ECJ) issued a judgment regarding the consistency of certain provisions in BITs entered into by Austria and Sweden with provisions of EU law.1 Second, the Commission has continued to take the position that intra-European BITs are unnecessary because of the protections embodied in the EC Treaty, a position that a number of member states have pushed back against. And finally, the Commission has submitted written comments in at least two investor-state arbitrations.

Notwithstanding the Commission’s signals of discomfort with investment treaties (and intra-EU treaties in particular) discussed below, investors from EU member states have continued seeking to enforce the protections they enjoy under those treaties, making them a popular means of dispute resolution. Therefore, it appears that EU investors consider such treaties as providing powerful leverage for investors injured by adverse government action.

### ECJ requiring member states to amend BITs

Prior to their accession to the EU in 1995, Austria and Sweden entered into a number of BITs with countries outside of the EU.2 These BITs include standard provisions guaranteeing investors the unconditional right to transfer capital in connection with an investment without undue delay, and in a freely convertible currency.3

In 2004, the Commission initiated infringement proceedings against Denmark, Austria, Finland and Sweden, alleging inconsistencies between the EC Treaty and certain provisions in their BITs with non-EU countries.4 The Commission alleged that, pursuant to article 307(2) of the EC Treaty, member states are required to eliminate (or revise) all international agreements that have been concluded before accession that are not compatible with the EC Treaty. While article 307(1) provides that EU law does not automatically prevail over an international agreement entered into by a member state, article 307(2) requires EU member states to eliminate any inconsistency.

The Commission raised concerns about BIT provisions that guarantee that investors can conduct international transfers freely and without interference or restriction. These principles are generally consistent with the EC Treaty, with a few notable exceptions. Specifically, the Commission alleged that certain guarantees found in those BITs conflict with powers reserved to the Council of the European Union (Council) under articles 57(2), 59, and 60(1) of the EC Treaty:

- article 57(2) empowers the Council to restrict capital movements to and from non-EU countries in certain sectors through the imposition of, among other things, performance requirements and ownership conditions;
- article 59 allows the Council, in exceptional circumstances, to impose safeguard measures for up to six months when movement of capital to or from third countries causes, or threatens to cause, ‘serious difficulties for the operation of the Economic and Monetary Union’; and
- article 60(1) allows the Council to restrict the transfer of capital based on common foreign and security policy. Article 60 provides the legal basis for EU sanctions against several countries and entities and is the legal mechanism by which the EU implements United Nations Security Council resolutions requiring the freezing of assets.

In defence, Austria and Sweden argued that until the Commission actually implemented measures that directly conflicted, there was no conflict between the BITs and the EC Treaty.5 Sweden also argued that, because articles 57(2), 59 and 60 may only be invoked in exceptional circumstances, the principle of rebus sic stantibus would operate to suspend the free transfer provisions if the Community were to adopt a measure pursuant to the EC Treaty.6

Additionally, Hungary and Finland – which intervened in both cases – argued that the Commission’s interpretation of article 307, which would allow the Commission to demand that a member state alter its laws even if the Commission had not yet exercised powers to enforce them, is contrary to distinctive treaty language that Finland had argued should address the Commission’s concerns. See opinion of Advocate General Sharpston of 10 September 2009 in Case C-118/07. The Commission closed its case against Denmark after Denmark notified the Commission that it had terminated the offending BIT. See EC: The EU Single Market, Website: Surveillance and Analysis of capital movements, available at http://ec.europa.eu/internal_market/capital_analysis/index_en.htm.


2 Specifically, the Commission alleged violations in the BITs that Austria has entered into with Korea, Cape Verde, the People’s Republic of China, Malaysia, the Russian Federation and Turkey. The Commission alleged violations in the BITs that Sweden has entered into with Argentina, Bolivia, Côte d’Ivoire, Egypt, Hong Kong, Indonesia, the People’s Republic of China, Madagascar, Malaysia, Pakistan, Peru, Senegal, Sri Lanka, Tunisia, Vietnam, Yemen and Yugoslavia.

3 The ECJ described these provisions as guaranteeing ‘the free transfer of funds in order to create, manage, or extend an investment; the freedom to repatriate the income from that investment; and the freedom to transfer the funds necessary to repay loans and the funds arising from the liquidation or assignment of that investment’. See Sweden judgment at paragraph 26.

4 A decision in the case against Finland has not yet been issued by the ECJ. In a recent development, an advocate general of the ECJ filed an opinion in the case arguing that Finland’s BITs are defective in the same manner as Sweden’s and Austria’s BITs, notwithstanding certain
available under the Treaty, and in an area in which no legislation
had been enacted, would give the Commission ‘an unlimited scope
which would be open to challenge from the perspective both of
legal certainty and of the distribution of powers between the com-

munity and member states.’ 7 Hungary also questioned the potential
implications of any ECJ judgment for the more than 1,000 BITs
entered into by EU member states with third countries, many of
which include similar free transfer provisions. 8

The ECJ rejected Austria and Sweden’s defences, and held that
[j]in order to ensure the effectiveness of [the EC Treaty] provisions,
measures restricting the free movement of capital must be capa-
ble, where adopted by the Council, of being applied immediately
with regard to the States to which they relate. 9 The ECJ further
reasoned that ‘the periods of time necessarily involved in any inter-
national negotiations which would be required in order to reopen
discussion of the agreements at issue is inherently incompatible
with the practical effectiveness of those measures.’ 10 The ECJ also
determined that there was no mechanism, either within the BITs or
under international law generally that would allow for the immedi-
ate suspension of the free transfer provision. 11

Importantly, the ECJ explicitly held that its findings were ‘not
limited to the Member State which is the defendant in the present
case.’ 12 This appears to be a suggestion by the ECJ that the more
than 1,000 EU member state BITs noted by Hungary may also be
deed to be in violation of the EC Treaty, to the extent that they
contain similar free transfer provisions.

The ECJ decisions require Austria and Sweden to take all appro-
riate steps to eliminate the incompatibilities between their BITs and
the EC Treaty. 13 While the ECJ does not prescribe specific actions
that must be taken, the decision mentions the possibility of amending
BITs to include a ‘provision allowing the Member State concerned to
exercise its rights and to fulfill its obligations as a member of the Com-

unity’. 4 Obviously, deletion of the free transfer provisions from the
offending BITs – or termination of the BITs in their entirety – would
also bring them into compliance. The Swedish Ministry of Foreign
Affairs confirmed recently that it is in discussions with its treaty part-
ners to amend the capital transfer provisions of its BITs. 15

However, until those BITs are terminated or amended, invest-
ments made under those treaties will continue to enjoy the full
range of legal protections afforded by the BIT. Many of the affected
BITs include long transition periods (up to 15 years) during which
the protections afforded by the BIT shall continue even after termi-
nation of the BIT. Thus, unilateral termination would not eliminate
the inconsistency identified by the ECJ, at least not in the foresee-
able future. The preferred course of action would be to seek an
agreement with the treaty partner to amend the text and eliminate
the inconsistencies.

Interestingly, the Commission did not extend its claim to challenge
any investment treaties that contain similar free transfer provisions but
to which both EU member states and the EU itself are signatories.
Thus, it will be interesting to see what the impact of the ECJ judg-
ments will be, for example, on the Energy Charter Treaty (ECT).

7 Sweden judgment at paragraph 19.
8 Sweden judgment at paragraph 22.
9 Sweden judgment at paragraph 37; Austria judgment at paragraph 36.
10 Sweden judgment at paragraph 40; Austria judgment at paragraph 39.
11 Sweden judgment at paragraph 36; Austria judgment at paragraph 36.
12 Sweden judgment at paragraph 43; Austria judgment at paragraph 43.
13 Sweden judgment at paragraph 35; Austria judgment at paragraph 34.
14 Sweden judgment at paragraph 36; Austria judgment at paragraph 37.
15 “Advocate General Renders Opinion on Finland’s Investment Treaties
with Non-EU countries; Sweden Begins Compliance with Earlier ECJ

EC efforts to terminate intra-EU BITs
The ECJ’s decision did not, however, directly address another sim-
mering issue – the existence of BITs between EU member states. It is
estimated that there are nearly 200 such BITs currently in force
between pairs of EU member states, many of which pre-date at
least one state’s EU accession. A number of these BITs have been
invoked by investors in recent years.

In 2006, Commission officials submitted an informal note to the
Economic and Financial Committee of the Council (EFC) regarding
the continued existence of intra-EU BITs. In that note, the Com-
mision suggested that ‘[s]tates appear to enter no need for agree-
ments of this kind in the single market and their legal character after
accession is not entirely clear. It would appear that most of their content
is superseded by Community law upon accession of the respective
Member State.’ 16 Commission officials also warned that ‘investors
could try to practice forum shopping by submitting claims to BIT
arbitration instead of – or in addition to – national courts. This could
lead to BIT arbitration taking place without relevant questions of EC law
being submitted to the ECJ, with unequal treatment of investors among
member states a possible outcome.’ 17

Last year, after receiving comments from member states regard-
ing the Commission’s proposal, the EFC prepared a letter to the
president of the Council of the European Union in which it noted
that ‘[m]ost member states did not share the Commission’s concern
regarding arbitration risks and discriminatory treatment of investors
and a clear majority of member states preferred to maintain the
existing agreements’. 18

In the few recent cases where the issue has been raised, arbitral
tribunals have determined that intra-EU BITs were not implicitly
terminated when those countries acceded to the EU. For exam-
ple, a tribunal recently ruled against the Czech Republic’s defence
that when it acceded to the EU, all of its BITs with other EU
member states were implicitly terminated. 19 A separate tribunal has
reportedly reached a similar conclusion. 20 The Czech Republic has
appealed at least one of these decisions to local courts. 21

Some EU member states have announced their intention to
terminate their BITs with other EU member states. Leading that
effort is the Czech Republic, which in 2005 announced its inten-
tion to terminate all of its BITs with other EU member states. 22
Italy and the Czech Republic have already terminated their BIT. 23
Denmark is in the process of terminating its BIT with the Czech
Republic. 24 And recently Slovenia and Malta announced their

16 ‘EU Members Review Intra-European BITs in Light of Potential Overlap
17 ‘EU member states Reject the Call to Terminate Intra-EU Bilateral
18 ‘EU member states Reject the Call to Terminate Intra-EU Bilateral
19 Eastern Sugar BV (Netherlands) v The Czech Republic. SCC No.
pdf.
20 “Czech Republic Quietly Pursues Challenge to Jurisdictional Ruling in
21 “Czech Republic Quietly Pursues Challenge to Jurisdictional Ruling in
22 “Czech Republic pursues shake-up of its bilateral investment treaties,”
23 ‘Italy, Slovenia and Malta concur with Czech Republic on lack of
necessity for intra-EU BITs; Italy-Czech treaty has been terminated,’
24 ‘Denmark and Czech Republic working to terminate investment treaty;
not all EU member-states agree with the Czech view that intra-EU
traties are unnecessary,’ Investment Arbitration Reporter, 17 July 2009.
agreement with the Czech position, and their intent to unwind their own BITs.\textsuperscript{25} Italy also has indicated that it intends to terminate a number of other intra-EU BITs.\textsuperscript{26}

However, not all EU member states concur with the Czech Republic’s approach including, according to public reports, Belgium, Germany, the Netherlands and the United Kingdom.\textsuperscript{27} Notably, many of the disputes brought against the Czech Republic in recent years have arisen under BITs with some of those countries.

**Commission intervention as amicus**

Recently, the Commission petitioned two arbitral tribunals, both hearing disputes related to power generation in Hungary, to allow it to submit non-party written submissions.\textsuperscript{28} In both disputes the tribunals allowed the Commission to make those submissions.

Both arbitrations turn on Hungarian government requirements that the Hungarian purchaser of electricity make changes to long-term contracts (known as power purchase agreements) that were entered into before Hungary acceded to the EU. The Hungarian government is defending itself in part on the ground that it was allegedly obliged to make the changes as a matter of EU law, as the Commission had determined that the agreements were illegal under EU law because they ‘constitute[d] unlawful and incompat-


tible state aid to the power generators’,\textsuperscript{29} and because they unduly restricted competition by preventing new entrants.

In November 2008, the tribunal in *AES Summit Generation Limited et al v Hungary* granted the request of the Commission to file a third-party submission under ICSID Arbitration Rule 37(2).\textsuperscript{30} However, the tribunal limited the Commission to discussing EU law and its relevance to the dispute.\textsuperscript{31} The tribunal in *Electrotel SA v Republic of Hungary* has also permitted the Commission to file a non-party submission.\textsuperscript{32}

While the submissions themselves are not public, it is generally understood that the Commission intervened to defend Hungary’s actions as being required by EU law. Press reports indicate that the Commission also sought to challenge the jurisdiction of the tribunal, because some aspects of the dispute, and the underlying contract from which the dispute arose, were subject to EU law, and thus within the jurisdiction of the Commission.

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EU BITs remain powerful tools for the investors that invoke them against harmful actions by host state authorities. Investors should continue to monitor the Commission’s interest in intra-EU BITs, and BITs entered into by member states with third countries.

\textsuperscript{25} ‘Italy, Slovenia and Malta concur with Czech Republic on lack of necessity for intra-EU BITs; Italy-Czech treaty has been terminated.’ Investment Arbitration Reporter, 6 August 2009.

\textsuperscript{26} ‘Italy, Slovenia and Malta concur with Czech Republic on lack of necessity for intra-EU BITs; Italy-Czech treaty has been terminated.’ Investment Arbitration Reporter, 6 August 2009.

\textsuperscript{27} See ‘Italy, Slovenia and Malta concur with Czech Republic on lack of necessity for intra-EU BITs; Italy-Czech treaty has been terminated.’ International Arbitration Reporter, 6 August 2009; and ‘Denmark and Czech Republic working to terminate investment treaty; not all EU member-states agree with Czech view that intra-EU treaties are unnecessary.’ Investment Arbitration Reporter, 17 July 2009.

\textsuperscript{28} *AES Summit Generation Limited and AES-Tisza Erőmű Kft v Republic of Hungary* (ICSID Case No. ARB/07/22); and *Electrotel SA v Republic of Hungary* (ICSID Case No. ARB/07/19).

\textsuperscript{29} ‘European Commission seeks to intervene as amicus curiae in ICSID arbitrations to argue that long-term power purchase agreements between Hungary and foreign investors are contrary to European Community Law,’ Investment Treaty News, 17 September 2008.


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