Slovak Republic v Achmea: See you in Court

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March 2018

On 6 March 2018, the Court of Justice of the European Union's (CJEU) judgment in *Slovak Republic v Achmea* (Case C-284/16) shook the world of investment arbitration to the core. The CJEU held that an arbitration clause in the Slovakia-Netherlands bilateral investment treaty (BIT) – and, essentially, all intra-EU BIT arbitration - was incompatible with EU law.

Much has been written already about the rights and wrongs of *Achmea*. However, if we accept (as we must) that it is the law, then it poses a crucial question: if not arbitration, then what? Gordon Nardell QC of 20 Essex Street and Richard Power of Clyde & Co. consider the solution.

Background

The Achmea, a Dutch insurance company, established a Slovakian subsidiary offering private sickness insurance. In 2006, Slovakia passed a law preventing private health insurers from distributing profits to shareholders.

Under Article 3(1) of the Netherlands-Slovakia BIT, each state undertakes to treat the other's investors fairly and equitably, and not to impair enjoyment of investments by unreasonable or discriminatory measures. Article 4 guarantees the free transfer of payments relating to an investment. Article 8 provides that, if a dispute under the BIT cannot be settled amicably, such a dispute will be determined by arbitration.

Achmea commenced arbitration proceedings, seated in Frankfurt, against Slovakia. In December 2012 the tribunal rendered an award which ordered Slovakia to pay Achmea compensation of €22.1m million. Slovakia applied to the Higher Regional Court in Frankfurt to set aside the award. That court rejected the application and Slovakia appealed to the German Federal Court of Justice. Slovakia argued that the tribunal lacked jurisdiction because the Netherlands-Slovakia BIT was contrary to the Treaty on the Functioning of the European Union (TFEU), which should take precedence over the BIT. The Federal Court of Justice referred the question of compatibility of the BIT with the TFEU to the CJEU.

The CJEU's judgment

In September 2017, Advocate General Wathelet delivered an opinion in which he advised that the arbitration clause did not violate the autonomy of EU law and was not discriminatory. In its judgment the CJEU framed the issue in the following way: "do Articles 267 and 344 TFEU preclude a provision in an international agreement

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between EU Member States under which an investor from one member state may bring proceedings against another Member State before an arbitral tribunal, whose jurisdiction that Member State has undertaken to accept?" Inevitably, the Court's answer would have wider significance than the Netherlands-Slovakia BIT.

However, the CJEU took the unusual step of departing from the Advocate General's opinion and held that the arbitration clause was incompatible with EU Law. Its reasoning was as follows:

- Article 8(6) of the BIT (similar to most arbitration clauses in BITs) provides that the arbitral tribunal shall take account of the law in force of the contracting party concerned, and international law principles. That would include EU law.

- Therefore, the tribunal may be called on to interpret and/or apply EU law, particularly provisions concerning freedom of establishment and free movement of capital which are closely related to the substantive BIT provisions.

- Article 19 Treaty on European Union (TEU) provides that it is for the national courts/tribunals of Member States and the CJEU to ensure the application of EU law in Member States. Key to this is the preliminary ruling procedure in Article 267 TFEU, which enables the courts of a Member State to refer questions on the interpretation and application of EU law to the CJEU, so as to ensure uniformity and consistency.

- An arbitral tribunal constituted under Article 8 of the Netherlands-Slovakia BIT is not a court or tribunal of a Member State within the meaning of Article 267 TFEU. Moreover, the award rendered by such a tribunal is subject to very limited judicial review, the extent of which is determined by national law depending on the seat (i.e. legal place) of the arbitration.

- Member States cannot enter into treaties which affect the allocation of powers created by the EU's constitutional Treaties, including the TFEU, so as to detract from the autonomy of the EU legal system. Art 344 TFEU in particular provides that Member States may not submit a dispute concerning the interpretation or application of the Treaties to any method of settlement other than those provided for in the Treaties.

- It follows that the arbitration agreement in Article 8 of the Netherlands-Slovakia BIT has an adverse effect on the autonomy of the EU legal order and is incompatible with EU law.

The CJEU recognised that it has previously held *commercial* arbitration agreements compatible with EU Law.[1] However, those agreements were distinguishable because they originate in the "freely expressed wishes of the parties", whereas BIT arbitrations derive from a treaty by which Member States agree to remove from the jurisdiction of their own courts a dispute which may concern the application or interpretation of EU law. That violates their obligations under Art 344 TFEU and Article 19(1) TEU.

[1] *Eco Swiss*, case no. C-126/97 and *Mostaza Claro*, case no. C-168/05

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How far does *Achmea* go?

The *Achmea* judgment now forms part of EU law. Consequently, any arbitral tribunal hearing a claim under an intra-EU BIT which has to take account of international law and/or the law of a contracting state – which most BIT arbitration clauses require – will have to take account of the judgment. This could result in a tribunal refusing jurisdiction. How likely is that?

Some have suggested that it depends on the arbitration agreement in question. For example, it has been argued that the arbitration clause in the Energy Charter Treaty (ECT) – a multilateral treaty protecting foreign investment in signatory states' energy markets – would not be affected by *Achmea*[2]. The argument runs that *Achmea* establishes the principle that EU Member States cannot derogate from the provisions of the Treaties which provide for the primacy of EU law and the necessity for it to be tested in the courts of Member States. The arbitration clause in Article 26 of the ECT is very similar to that in the Netherlands-Slovakia BIT. However, unlike that BIT, the EU *itself* is a party to the ECT, including Article 26. Consequently, it is argued, it must be implied that the EU itself has derogated from the provisions of the Treaties to the extent of claims under the ECT. Indeed, the Court pointed out in its judgment that it has previously ruled "not in principle incompatible with EU law" the Union *itself* becoming party to an international agreement establishing a decision-making body whose judgments are binding on EU institutions including the CJEU.[3]

However, this argument is not necessarily correct. In the context of the judgment as a whole, this passage seems to envisage an international agreement establishing a "court" in the usually understood sense of that term, not an autonomous arbitral tribunal. The true *ratio* of *Achmea* is that disputes involving the interpretation and application of EU law must be determined in *a court system* which enables a preliminary ruling referral pursuant to Article 267 TFEU, and arbitral tribunals lack that attribute. Moreover, in his opinion Advocate General Wathelet pointed out that an arbitration provision under a treaty to which the EU itself is party is *more*, not less, likely to offend Article 344 TFEU because the treaty provisions would become part of the EU legal order, hence any dispute regarding rights and obligations under the treaty would inevitably require the interpretation and application of EU law.[4]

Similarly, it has been suggested that arbitration under ICSID rules is not affected by *Achmea*, because the ICSID Convention requires contracting states to recognise ICSID awards directly and without any review, as they would for any final decision rendered by their own courts[5]. However, even AG Wathelet signalled – for precisely this reason – that he might well have reached a different view on compatibility with EU law had the BIT provided for ICSID arbitration.[6] And an ICSID tribunal is no more a court or tribunal of an EU Member State than an ad hoc/UNCITRAL or SCC tribunal constituted under the Netherlands-Slovakia BIT or a similar treaty. The EU is not a party to the Washington Convention[7].

In any event, if the tribunal decides that it does, in fact, have jurisdiction[8] (for example,

[2] See, for example, Power, Novenergia v. Kingdom of Spain, the ECT and the ECJ: Where to now for intra-EU ECT claims?
[3] Opinions 1/91 (EEA Agreement), 1/09 (unified patent litigation system) and 2/13 (EU accession to ECHR).
[4] Opinion, paras. 150, 163-167.
[5] Article 54 ICSID Convention.
[6] Opinion, paras, 252-253.
[7] Nor can it be: under Article 67 of the Convention only States can be contracting parties.
[8] In *RREEF Infrastructure (G.P.) Limited and RREEF Pan-European Infrastructure Two Lux S.à r.l. v. Kingdom of*

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because it will not be applying EU law in making its decision) and renders a substantive award in favour of the investor, it is likely that any attempt to enforce that award in an EU state would be resisted[9].

We are therefore left with the likelihood – or at any rate the real possibility - that EU law prohibits *any* intra-EU investment treaty claim (including an ECT claim) from being validly referred to *any* form of arbitration. So, investors face the conundrum: "If not arbitration, then where?" Indeed, can such a claim now be made anywhere? In other words, by barring investors from enforcing their treaty rights through arbitration, has the CJEU in reality extinguished the rights themselves? AG Wathelet thought that a BIT shorn of a right to refer a dispute to international arbitration would be "devoid of all practical effect"[10]

"Stranded" rights?

The starting point is that nothing in the *Achmea* judgment suggests that the CJEU intended to invalidate the substantive rights and obligations arising from an intra-EU investment treaty. On the contrary, the CJEU's reasoning presupposes the existence of those rights and obligations, and in particular their complex relationship with rights and obligations under the EU Treaties. It is the interaction between the two regimes – and hence the need to determine questions of EU law when adjudicating on investment claims – that generates the incompatibility between arbitration and Article 344 TFEU. The CJEU has recognised, in other words, that the rights and duties under the investment treaty have been validly created by Member States acting within their (former) competence in the field of trade and investment – a competence defined by EU law itself[11].

It is fundamentally unlikely that EU law, with its rich rule of law tradition and insistence on effective remedies (reflected in Article 47 of the Charter of Fundamental Rights and in cases such as *Marshall*[12]) would intentionally create a category of *damnum absque injuria* – a wrong without a remedy. Rather, in situations where existing rules provide no explicit route for enforcing EU rights against the authorities of a Member State, the CJEU has invariably insisted on recognising – or more accurately, creating – the necessary jurisdiction in the national courts. In *Factortame* the CJEU held that the EU principle of effectiveness conferred on UK courts the previously unknown (and constitutionally heretical) power to disapply provisions of primary legislation incompatible with the Treaties[13]. The CJEU and English courts went on to award damages against the UK Government for the loss caused to the Spanish undertakings whose rights the national legislation had infringed[14].

Spain, ICSID Case No. ARB/13/30, the tribunal observed that if it was ever determined that ECT and EU law were inconsistent, "the unqualified obligation in public international law of any arbitration tribunal constituted under the ECT would be to apply the former. This would be the case even were this to be the source of possible detriment to EU law. EU law does not and cannot 'trump' public international law."

[9] Article V(2) of the New York Convention enables the national courts of contracting states to refuse to register and enforce a foreign arbitral award on the grounds that the dispute was not capable of settlement by arbitration and/or enforcement would be contrary to public policy.

[10] Opinion para. 207 (and see para. 76).

[11] The current scope of this competence, and its relationship with the exclusive competence of the Union, was analysed in CJEU *Opinion 2/15 on the Free Trade Agreement between the EU and the Republic of Singapore*, 16 May 2017.

[12] C-271/91 *Marshall v. Southampton & SW Hampshire Health Authority* [1993] ECR I-4367.

[13] C-213/89 *R v. Secretary of State for Transport, ex p. Factortame* [1990] ECR I-2433.

[14] Joined cases C-46/93 and C-48/93 *Brasserie du Pêcheur v. Germany* and *R v. Secretary of State for Transport, ex p. Factortame (No. 3)* [1996] ECR I-1029; *R v. Secretary of State for Transport, ex p. Factortame (No. 5)* [2000] 1 AC 524, HL.

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Do national courts have jurisdiction?

It seems entirely consistent with these developments that an EU investor deprived by the *Achmea* judgment of the benefit of *arbitral* protection of BIT rights against a Member State should be entitled instead to seek *judicial* protection by claiming damages in a national court. But that immediately raises two questions. First, are rights created on the level of international law by an intra-EU BIT – as opposed to rights created by the EU Treaty regime itself – justiciable in a national court at all? And if so, which national court has jurisdiction to entertain a claim – the court of the investor's home State, or of the host State?

The second question is the more straightforward. It would be a jurisprudential quantum-leap, even by EU standards, for a national court in one State (the investor's home State) to claim jurisdiction to determine the legality of conduct attributable to another State (the host State). True, EU law recognises the principle of extraterritorial jurisdiction of national courts over activity occurring within another Member State, in the fields of both civil and criminal law. But there is a world of difference between jurisdiction over *private entities* located in another Member State's territory, and jurisdiction over *the State itself*. That is reflected in, for example, the EU regime for cooperation in civil justice, which carefully excludes claims of a sovereign nature from the rules on allocation of jurisdiction and mutual recognition of judgments[15].

So, the focus is necessarily on the question whether the courts of a Member State have jurisdiction to entertain an investment treaty claim by an intra-EU investor against *that* State, in substitution for the arbitral mechanism made inaccessible by *Achmea*.

This question is particularly acute for the EU's common law jurisdictions, including the UK and Ireland, that operate a 'dualist' approach to international law. Under the 'monist' systems of most EU States, international treaties ratified by the State become part of the domestic legal order. The EU itself follows this tradition: by Article 216(2) TFEU an international agreement to which the EU is party is binding on both the Union and Member States[16]. But in a 'dualist' system, a BIT – like any other treaty – confers no rights justiciable in a domestic court unless and until it is given effect by national legislation. The *Miller* case in the English courts is a recent reminder of the potency of this principle: the government could not lawfully terminate the UK's membership of the EU without legislative approval because that would have impermissible domestic consequences, namely to denude of all practical effect the European Communities Act 1972 by which the EU Treaty regime had been made part of national law[17].

The question is probably easiest to answer in relation to the ECT. Article 26 expressly contemplates that an investor may refer a dispute to the national courts of the host State[18]. Because the EU itself is party to the ECT, this provision would appear to bind Member States as a matter of EU law (see above) and therefore forms part of domestic

[15] Article 1(1) of the Brussels I Recast Regulation (No. 1215/2012) provides that the Regulation "shall not extend, in particular, to revenue, customs or administrative matters or to the liability of the State for acts and omissions in the exercise of State authority (*acta iure imperii*)."

[16] An agreement between the EU and one or more non-EU entities has an intermediate status between the EU Treaties and secondary legislation: see Joined Cases C-402/05 and C-415/05 *Kadi and Al Barakaat* [2008] ECR ECR I–6351.

[17] *R. (Miller) v. Secretary of State for Exiting the* EU [2017] UKSC 5, [2017] 2 WLR 583; and see Nardell and Leary, *Won't you stay another day?*.

[18] Article 26(2): "If such disputes [ie "disputes between a Contracting Party and an Investor of another Contracting Party relating to an Investment of the latter in the Area of the former"] cannot be settled… within a period of three

law in the same way as other rules derived from EU law. That sidesteps the 'dualist' problem.

But there are also good reasons to conclude that, quite apart from the special case of the ECT, the principle of effectiveness itself is likely to require the national court, in the wake of *Achmea*, to accept jurisdiction over an intra-EU claim under *any* investment treaty. That would necessitate extension of the principle from rights generated by the Treaties (where, as we have seen, there has been no difficulty in recognising novel forms of jurisdiction against Member State authorities) to rights arising under 'ordinary' international agreements between EU States. But the point of the *Achmea* judgment is that EU law *requires* that those rights, because of their interaction with rights under the EU regime proper, be ventilated in a court forming part of the EU judicial framework. The need for jurisdiction to vest in such a court is inherent in the removal of jurisdiction from the arbitral mechanism in the first place. The court must accept jurisdiction for the high-level reason that doing so is necessary to preserve the autonomy of the EU legal order, while also preserving rights and duties which, as noted above, have been validly conferred on investors by the contracting Member States acting within the scope of their competence.

Focusing for a moment on the position in England and Wales, this is ironically a situation in which English law's pragmatic streak is likely to reinforce the position in high theory. The High Court – as a court of unlimited jurisdiction[19] – has ample power to offer a forum for a dispute when an intended non-judicial mechanism is no longer available. The context may be contractual: where the parties have created a private decision-making machinery which for some reason cannot be operated, the court will step in to take the necessary decision itself. It does so to enable the wider agreement between the parties to take effect rather than be defeated by the technical problem: see *Sudbrook Trading Estate Ltd.* v. *Eggleton*[20]. The same approach has been adopted where a mechanism established by statute has lapsed. In *Swanhill Developments plc v. BWB*[21] a claim was made under an old Canal Act which established a body of commissioners to assess compensation. The commissioners were long defunct, but Lord Woolf MR said:

> "...it is accepted that the appropriate body to exercise what would otherwise be the powers of the commissioners in these circumstances is the High Court. The High Court can, by granting declarations, make any appropriate decision which is needed in the absence of the commissioners. That seems to me to be a happy resolution of what could otherwise be a purely technical problem"[22].

Echoes of the New York Convention's acceptance of judicial intervention where an arbitration agreement is "null and void, inoperative or incapable of being performed"[23] will not be lost on arbitration practitioners. In this situation the court, by accepting jurisdiction, would not be inventing new legal rights against the UK State in defiance of the dualist principle. It would simply be offering a

months…the Investor party to the dispute may choose to submit it for resolution:
(a) to the courts or administrative tribunals of the Contracting Party to the dispute…". The question whether arbitration under paragraphs (3) to (6) remains an option where a dispute has been submitted to the national court depends on whether the State in question has adopted the "fork in the road" provision, Annex ID.

[19] *M. v. Home Office* [1992] QB 270, Lord Donaldson MR at 299A.
[20] [1982] 3 All ER 1, HL, Lord Fraser at 11e.
[21] [1998] JPL 153.
[22] At 161.
[23] Article II.3.

platform for a dispute where the State has signed up to binding determination in principle, but where the original mechanism for achieving that has become ineffective as a result of another system whose binding decisions the State has likewise signed up to. In that capacity the court could still make any necessary preliminary reference to the CJEU in the usual way, thus satisfying the *Achmea* requirements. Indeed, an early reference may well be necessary on the very question whether the national court possesses, and should exercise, a jurisdiction of this kind.

Does the CJEU have jurisdiction?

The final question in the jurisdictional jigsaw is this: has *Achmea* opened up the possibility that an investor might bypass national courts entirely and bring a claim directly before the judicial institutions of the EU itself? There is a certain poetic attraction in the proposition that the body which has imposed the barrier to arbitration should now 'own' the problem it has created. But the difficulty in that route is that the jurisdiction the Treaties confer on the General Court and Court of Justice against Member States and Union Institutions is precisely defined.

The Commission can seise the CJEU in infraction proceedings against a Member State under Article 258 TFEU. But, as AG Wathelet pointed out,[24] there is no direct route for a private party to take any comparable step. A claim by an individual against a Member State can only reach the CJEU on a preliminary reference from a national court.

Meanwhile, under Article 340 TFEU, a party with sufficient standing may bring an action for damages in the Union courts against a Union institution. In the case of the ECT, the EU is itself party to the investor protection provisions along with the Member States. One can see that if a breach of those provisions by a Member State results purely from its observing an act of a Union institution that is subsequently found unlawful, the Union might be jointly liable with the State – for example, where a decision of the Commission that a benefit peremptorily withdrawn from an investor constituted unlawful State aid is overturned by the General Court. Indeed, the EU institutions are currently examining certain cases where there seems at least some possibility of fixing the Union with liability on this basis[25]. But outside that category of case, it is not easy to see how an alleged breach by a Member State resulting from decision-making purely within the scope of its own domestic competence can be imputed to the Union so as to generate liability under Article 340.

Conclusion

Whatever criticism might be levelled at *Achmea*, it cannot be ignored, not least in light of the difficulties in enforcing in the EU an award rendered by an arbitral tribunal constituted in breach of the judgment. The judgment gives obvious impetus for establishing the standing international investment court proposed by the EU, possibly initially as an EU institution hearing intra-EU claims. However, that would require a new multilateral convention and

[24] Opinion para, 205.

[25] In the long-running *Micula v. Romania* saga, the English High Court ([2017] EWHC 31 (Comm)) has stayed enforcement of contested ICSID award ARB/05/20, pending the decision of the General Court on the investors' action (case T-694/15) to annul the Commission's State aid decision that lay behind Romania's non-compliance with the award. The EU is not party to the underlying Sweden-Romania BIT. However, similar developments are now unfolding in the ECT case of *Eiser Infrastructure Ltd. v. Spain* where the Commission has intervened to block payment of ICSID award ARB/13/36. If that decision is successfully challenged, the question of concurrent Union liability under the ECT may well be tested.

corresponding EU legislation, and establishing such a court would take years[26].

In the meantime, the question of where to enforce the rights bestowed on investors via numerous inter-EU BITs and multilateral treaties remains, and requires urgent attention. This is particularly true for the UK, at least pending expiry of the likely Brexit transitional arrangements in December 2020. As explained in this article, there are good grounds for believing that the national courts of the host State are should now step into the breach created by the CJEU. But with the Commission distracted by Brexit, it remains to be seen how investors will take their cases forward. *Achmea* has ultimately posed more questions than it has answered.

If you require advice on any of the topics discussed in this report from Gordon, or any member of 20 Essex Street please contact: clerks@20essexst.com

[26] On 20 March 2018 the Council adopted negotiating directives enabling the Commission to move forward with a convention establishing a new court: http://www.consilium.europa.eu/en/press/press-releases/2018/03/20/multilateral-investment-court-council-gives-mandate-to-the-commission-to-open-negotiations/.