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The arbitration clause included in a Bilateral Investment Treaty concluded between two Members States is incompatible with EU law

On March 6, 2018, the Grand Chamber of the Court of Justice of the European Union issued a judgment stating that the UNCITRAL arbitration clause included in a Bilateral Investment Treaty that establishes a mechanism for settling disputes between an investor and an EU Member State is incompatible with EU law.

On March 16, 2018, the Grand Chamber of the Court of Justice of the European Union ("CJEU") issued a judgment in the Achmea case[1] in which it stated that EU law "*must be interpreted as precluding a provision in an international agreement concluded between Member States, such as Article 8 of the Agreement on encouragement and reciprocal protection of investments between the Kingdom of the Netherlands and the Czech and Slovak Federative Republic, under which an investor from one of those Member States may, in the event of a dispute concerning investments in the other Member State, bring proceedings against the latter Member State before an arbitral tribunal whose jurisdiction that Member State has undertaken to accept*"[2].

In 1991, the Netherlands and the former Czechoslovakia concluded a Bilateral Investment Treaty (BIT) stipulating that disputes between one Contracting State and an investor from the other Contracting State must be settled amicably or, in default, before an arbitral tribunal[3].

In 2004, Slovakia opened its health insurance market to private investors. Achmea, a Dutch group, set up a subsidiary in Slovakia to offer private health insurance services there. Shortly thereafter, Slovakia partly reversed the liberalization of its health insurance market and prohibited the distribution of profits generated by health insurance activities.

In 2008, Achmea, considering that this legislative change had caused it a loss, initiated arbitration proceedings against Slovakia on the basis of Article 8 under the BIT which provided for the application of the United Nations Commission on International Trade Law ("UNCITRAL") arbitration rules. Slovakia claimed that the arbitral tribunal lacked jurisdiction, arguing that Article 8 of the BIT was incompatible with EU law. The arbitral tribunal dismissed this objection.

On December 7, 2012, the arbitral tribunal ordered Slovakia to pay to Achmea 22.1 million euros in damages. Slovakia filed a motion to set aside the arbitral award but that motion was dismissed by the Higher Regional Court of Frankfurt am Main. Slovakia then decided to lodge an appeal before the German Federal Court of Justice.

1. The question referred to the CJEU for a preliminary ruling

The German Federal Court of Justice held that the BIT constituted an agreement between Member States and that, in the event of a conflict, EU law prevailed over the provisions of the BIT. Slovakia then claimed that the arbitration clause in the BIT was incompatible with Articles 18, 267 and 344 of the Treaty on the Functioning of the European Union (TFEU).

As the CJEU had not yet ruled on the compatibility of arbitration clauses included in BITs entered into between Member States with EU law, the German Federal Court of Justice decided, despites its initial reluctance, to refer this question to the CJEU for a preliminary ruling.

The European Commission as well as several Member States (including Italy, Spain, Hungary) submitted observations in support of Slovakia's arguments, while other Members States (including France, Germany, the Netherlands) contended that the clause at issue and, more generally, clauses of a similar kind commonly used in the 196 BITs currently in force within the EU were valid.

2. Reminder of the principles governing EU law

The CJEU first recalled the provisions set forth in Article 344 TFEU according to which "*the Member States undertake not to submit a dispute concerning the interpretation or application of the Treaties to any method of settlement other than those provided for in the Treaties*". By doing so, the CJEU stressed the autonomy of EU law, its primacy over national laws, and its direct effect.

The CJEU then formulated the general principle that "*EU law is thus based on the fundamental premiss that each Member State shares with all the other Member States, and recognises that they share with it, a set of common values on which the EU is founded*"[4].

According to the CJEU, "*it is precisely in that context that the Member States are obliged, by reason inter alia of the principle of sincere cooperation* […] *to ensure in their respective territories the application of and respect for EU law, and to take for those purposes any appropriate measure, whether general or particular, to ensure fulfilment of the obligations arising out of the Treaties or resulting from the acts of the institutions of the EU* […]"[5]. To this end, the CJEU insisted on the existence of a true judicial system which has as its keystone the preliminary ruling procedure provided for in Article 267 TFEU, which sets up a dialogue between courts and has the object of securing the uniform interpretation of EU law, its consistency, its full effect and its autonomy.

3. The three-step reasoning of the CJEU

In order to find that the mechanism introduced by Article 8 of the BIT had an adverse effect on the autonomy of EU law as it "***is such as to call into question not only the principle of mutual trust between the Member States but also the preservation of the particular nature of the law established by the Treaties, ensured by the preliminary ruling procedure provided for in Article 267 TFEU, and is not therefore compatible with the principle of sincere cooperation***"[6], the CJEU adopted a three-step reasoning.

- *May the arbitral tribunal be called on to interpret or to apply EU law?*

The CJEU insisted on the arbitral tribunal's duty to take into account, interpret and apply the law in force within the concerned States, i.e. EU law in the present matter, in particular the provisions concerning fundamental freedoms, including freedom of establishment and free movement of capital.

- *Can the arbitral tribunal be regarded as a court or tribunal within the meaning of Article 267 TFEU?*

The CJEU recalled that the courts or tribunals set up by Members States must, as per Article 267 TFEU, subject their decisions to mechanisms capable of ensuring the full effectiveness of the rules of the EU and allow for the referral of questions for a preliminary ruling in order to guarantee the unity of EU law.

The CJEU considered, in particular, that "*the arbitral tribunal is not part of the judicial system of the Netherlands or Slovakia. Indeed, it is precisely the exceptional nature of the tribunal's jurisdiction compared with that of the courts of those two Member States that is one of the principal reasons for the existence of Article 8 of the BIT*"[7].

The CJEU thus held that "*that characteristic of the arbitral tribunal at issue in the main proceedings means that it cannot in any event be classified as a court or tribunal 'of a Member State' within the meaning of Article 267 TFEU*"[8].

- *Is the decision of the arbitral tribunal subject to review by a court of a Member State?*

Lastly, the CJEU examined the potential existence of a judicial review by a court of a Member State so as to ensure that the questions of EU law which the arbitral tribunal may have to address could be submitted to the CJEU by means of a reference for a preliminary ruling.

In this respect, the CJEU noted that the decision of the arbitral tribunal was final and that judicial review could only be exercised to the extent that national law so permits. The CJEU specified that the only possibility offered by German law in this respect was the filing of a motion to set aside, which could be implemented in a very limited number of cases only.

As a result, the CJEU found that the established mechanism for settling disputes did not ensure that the dispute would be adjudicated in such manner as to guarantee the full effectiveness of EU law.

4. Concerns about the scope of the CJEU's judgment

The reasoning of the CJEU leaves many questions unanswered, in particular as regards what consequences it will have and how it will be taken into account by national courts.

Indeed, while it is conceivable that the arbitral tribunals will decline jurisdiction to hear disputes initiated by European investors against a Member State, national courts – whose assistance would be required in the framework of arbitration proceeding conducted in the European Union or asked to rule on a request for the recognition and enforcement of arbitral awards handed down in relation to an Intra-EU BIT – would have the obligation to take this judgment into account.

On the other hand, even though the CJEU has been careful to specify that its reasoning does not apply to commercial arbitration proceedings which originate in the freely expressed wishes of the parties, the scope of its judgment for arbitration proceedings conducted outside the EU or under the auspices of the International Centre for Settlement of Investment Disputes (ICSID) remains uncertain.

As such, its actual scope should be put into perspective.

[1] CJEU, Slowakische Republik vs. Achmea BV, C-284/16.

[2] CJEU, Slowakische Republik vs Achmea BV, C-284/16, § 62.

[3] In 1993, Slovakia succeeded to Czechoslovakia's rights under this BIT.

[4] CJEU, Slowakische Republik vs Achmea BV, C-284/16, § 34.

[5] CJEU, Slowakische Republik vs Achmea BV, C-284/16, § 34.

[6] CJEU, Slowakische Republik vs Achmea BV, C-284/16, § 60.

[7] CJEU, Slowakische Republik vs Achmea BV, C-284/16, § 45.

[8] CJEU, Slowakische Republik vs Achmea BV, C-284/16, § 46