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Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@law360.com

Why Investors Are Worried About Intra-EU BITs

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Tomas Varga

On June 18, 2015, the European Commission initiated infringement proceedings against five member states of the European Union for intra-EU bilateral investment treaties' (BITs) incompatibility with EU law. The infringement proceedings exert further pressure on these states (Austria, the Netherlands, Romania, Slovakia and Sweden) to terminate their intra-EU BITs. Neither the states concerned, nor the existing or potential investors likely to be affected by these proceedings are particularly content about this recent development.

The Argument Over Intra-EU BITs

The commission has long argued that intra-EU BITs are outdated and no longer necessary because the same protection is now afforded to investors pursuant to various EU rules in the single market, including those on cross-border investments (in particular the freedom of establishment and the free movement of capital). The commission has also been arguing that intra-EU BITs are often incompatible with EU law. Perhaps the clearest example of the commission's "dislike" for intra-EU BITs was when it issued a suspension injunction against Romania in Ioan Micula, Viorel Micula and others v. Romania (ICSID Case No ARB/05/20). In Micula, Romania lost an investment treaty arbitration and was required to pay a substantial sum to the claimants. The commission's formal conclusion in its action against Romania was that any payment by Romania in accordance with the terms of the award in that case would infringe EU rules on state aid. Accordingly, the commission directed Romania not to satisfy the award and to recover any sums already paid. The claimants in Micula brought an action against the commission later that year arguing that the commission's decision failed to acknowledge Romania's obligations under international law to execute the ICSID award without delay and that Romania's international law obligations took primacy over EU law. The outcome of the case is currently pending.

Uncertainty for Investors

The commission's action in the Micula case and its recent proceedings against the five member states raise various issues. One in particular is that of legal certainty afforded to existing and potential investors. As the current proceedings only affect Austria, the Netherlands, Romania, Slovakia and Sweden, the issue of legal certainty is of particular relevance to the nationals of, and entities in, those states. For example, what mechanism, if any, can and should an existing investor use to bring a claim against one of the member states in question? It is clear that the commission can (and has successfully done so in the past) force a state that is a party to such an intra-EU BIT not to execute an award to which it is subject. An investor that has already obtained such an award in its favour can challenge the commission's decision (and the Micula brothers have done just that) hoping that the General Court — the court of first instance where the commission's decisions can be challenged — would overturn the commission's decision. An investor that is yet to initiate an arbitration proceeding is however in a slightly different position because it now already knows that there is a risk that it may end up paying hundreds of thousands of dollars in legal fees and disbursements to obtain an award whose enforceability may be questionable. Another option is therefore to start proceedings in a national court. Potential investors 20 years ago, when some of these BITs entered into force, knew they had the option to bring a claim in a national court (that is if the local legislation provides for a cause of action and a particular relief sought), but this is probably not what those investors hoped for. Even a fairly unsophisticated investor understands the advantages of arbitration when a sovereign state is concerned.

One advantage is that of added impartiality and practicality. Whereas in traditional court proceedings an investor would have no power over the appointment of a judge presiding over the case, in investment treaty arbitration (as is the case generally in any other international arbitration) the claimant has a degree of influence over the appointment of the members of the arbitral tribunal. This advantage may be particularly relevant in those cases where there is a fear that the appointed judge may lack relevant expertise or when one is concerned that the state organs may want to influence the judge's decision in the case. After all, not every state has a strong tradition of the doctrine of separation of powers. Another advantage is that of applicable law. It is usual for the arbitral tribunals in BIT arbitrations to apply the substantive provisions of the BIT itself and other sources of international law rather than national law, even where the governing law clause in a BIT refers to national law (Emilio Agustin Maffezini v. The Kingdom of Spain (ICSID Case No ARB/97/7). This can be very important in those cases where the national law is not well developed or where the investor hopes to take advantage of a particular provision in a BIT which cannot be found in the relevant national legislation.

Another issue that potential investors now have to face is that of their reliance on the "promises" given by a member state in an intra-EU BIT when they already know or at least suspect that the commission is likely to challenge any such award rendered under an intra-EU BIT, considering it incompatible with EU laws. Although this is a commercial rather than a legal issue as the investors' rights to bring arbitral proceedings under the existing intra-EU BITs are not affected by the commission's recent proceedings, it is nevertheless an important one. Even though different classes of investors may have different considerations when entering or exiting a particular country-specific market, investing in a country that has been put under elevated pressure by both the investors on one side and the commission on the other is something that should be carefully considered. It is yet to be seen how the countries in question will respond to the commission's letters of formal notice. Member states are expected to reply to the commission within two months of receiving such letters.

Lastly, it is important to observe that even if the notice of termination of a particular intra-EU BIT was to be served by any of the above countries, thus disposing of the need for the commission to continue with its proceedings, the intra-EU BITs often include a provision which provides for continuous protection of any investments made prior to the date when such notice of termination became effective. In such a scenario the relevant provisions of the BIT remain in force for several more years from the date the intra-EU BIT was terminated. This would in effect mean that uncertainty can continue for many more years after the day the BIT is terminated because the rights afforded under that BIT would continue in parallel with the threat of a potential suspension from the commission if an award is incompatible with EU laws.

Conclusion

It is unclear how the infringement proceedings may affect intra-EU BIT claims currently being pursued by investors — but it is clear that they add further uncertainty for both investors and member states. It has been suggested that the investors presently relying on intra-EU BITs as a form of protection for their investment in the EU might want to consider restructuring such investments. This can be done by changing the seat of the holding company from an EU country to a non-EU country which still has an appropriate BIT with the EU country the investor hopes to bring proceedings against. Although restructuring one's holdings to take advantage of another BIT is not novel in the world of investment treaty arbitration, it is often not straightforward and may not always work; especially as different BITs may afford different types of protection. Finally, it is also unclear whether any alternative to arbitration under intra-EU BITs will follow. Although the EU commissioner for financial services has recently suggested that some form of "investment mediation" will be established, this is unlikely to be accomplished any time soon. However, it is important to note that there are likely to be fewer obstacles to the successful enforcement of an arbitral award than to a negotiated mediation settlement.

—By Tomas Varga, Faegre Baker Daniels

Tomas Varga is a trainee solicitor in Faegre Baker's London office.

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