

# The CJEU Finds Investor-State Arbitration Clause In The Energy Charter Treaty Inapplicable To Intra-EU Disputes

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In a September 2, 2021 judgment in *Republic of Moldova v. Komstroy LLC*, the Court of Justice of the European Union found that the investor-State arbitration clause in the Energy Charter Treaty is inapplicable to disputes between investors and States from the EU.<sup>1</sup>

In the wake of the landmark judgment of the Court of Justice of the European Union (“CJEU”) in *Slovak Republic v. Achmea BV* (“**Achmea Judgment**”)<sup>2</sup> and in line with the position of the European Commission and the majority of EU Member States,<sup>3</sup> the Court has ruled that the investor-State arbitration clause in Article 26 of the Energy Charter Treaty (“ECT”) is not applicable to disputes between an EU Member State and an investor of another EU Member State concerning an investment made by the latter in the first Member State (“**intra-EU disputes**”). The Court found that such arbitration clause, if interpreted as applying to intra-EU disputes, would adversely affect the autonomy and particular nature of EU law.<sup>4</sup>

The CJEU judgment in *Republic of Moldova v. Komstroy LLC* (“**Komstroy Judgment**”) is in stark contrast with a consistent line of investment treaty awards which have concluded that the ECT’s investor-State arbitration clause is applicable in intra-EU disputes.<sup>5</sup>

Rendered in the context of an arbitration between two non-EU parties, and regarding the ECT, a multilateral treaty whose contracting parties include the EU as well as both EU and non-EU Member States, the CJEU judgment has potentially far-reaching implications, including when it comes to the very future of investment arbitration under the ECT within the EU.

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## Background

### The Energy Charter Treaty

The ECT was concluded in December 1994, with the aim of providing a multilateral framework for energy cooperation, as well as stability and security in worldwide energy markets. There are currently 54 signatories to the ECT, including the European Union itself, as well as all EU Member States with the exception of Italy, which withdrew from the treaty in 2016.

The ECT is the most frequently invoked investment treaty, with over 140 investment arbitrations initiated under the ECT to date,<sup>6</sup> a majority of which initiated by EU investors and/or against EU Member States.<sup>7</sup>

### The *Achmea* Judgment And The Termination Agreement

As discussed in [our alert memorandum on the \*Achmea\* Judgment](#),<sup>8</sup> on March 6, 2018 the CJEU held that investor-State arbitration clauses in bilateral investment treaties between EU Member States (“intra-EU BITs”) are incompatible with EU law. The Court found that such clauses undermine the effective application and autonomy of EU law and therefore are contrary to the EU Treaties. Following the *Achmea* Judgment, in January 2019 all EU Member States adopted declarations in which they committed to terminate all their existing intra-EU BITs.<sup>9</sup> The majority of Member States further specified that the application of the ECT’s investor-State arbitration clause to intra-EU disputes would be incompatible with the EU Treaties.<sup>10</sup> Finland, Luxembourg, Malta, Slovenia, Sweden and Hungary declared separately that, in their view, the *Achmea* Judgment concerns only intra-EU BITs, not arbitration proceedings initiated under the ECT.<sup>11</sup>

On May 5, 2020, the vast majority of EU Member States<sup>12</sup> formalized their commitments to terminate all BITs in force between them, adopting the Agreement for the Termination of Bilateral Investment Treaties Between the Member States of the European Union (“Termination Agreement”).<sup>13</sup> As discussed in [our Alert Memorandum on the Termination Agreement](#),<sup>14</sup> these Member States reiterated that arbitration clauses in intra-EU BITs are incompatible with the EU Treaties and therefore cannot serve as a legal basis for the arbitration of intra-EU investor-State disputes.<sup>15</sup>

The Termination Agreement is expressly limited to intra-EU BITs and specifies that it does not apply to intra-EU arbitral proceedings on the basis of Article 26 of the ECT, which would be dealt with by the EU and its Member States “*at a later stage.*”<sup>16</sup>

### The *Komstroy* Arbitration And Request For Preliminary Ruling

The September 2, 2021 *Komstroy* Judgment follows a 2019 request for a preliminary ruling by the Paris Court of Appeal on the interpretation of the ECT.

In October 2013, the *Energoalians v. Moldova* ECT tribunal had issued a US\$49 million arbitral award in favor of the Ukrainian company.<sup>17</sup> The Republic of Moldova then initiated set aside proceedings against the award in front of the Paris Court of Appeals, arguing that the tribunal lacked jurisdiction *ratione materiae* over the claimant’s rights under a contract for electricity supply. After October 2014, Ukrainian company Komstroy LLC (“**Komstroy**”) acted as the successor in law to Energoalians in the proceedings.<sup>18</sup>

The Paris Court specifically requested a preliminary ruling from the CJEU on the interpretation of the notion of “investment” in Articles 1(6) and 26(1) ECT. The European Commission and several EU Member States intervened in the proceedings, asking the CJEU to also rule on the applicability of its findings in the *Achmea* Judgment to the ECT. Komstroy, as well as the Council of the European Union, Hungary, Finland and Sweden, argued that the CJEU did not have jurisdiction to answer the questions put before it, as the underlying dispute did not involve EU law, since the parties to that dispute are external to the EU.<sup>19</sup>

In March 2021, Advocate General Szpunar opined that the Court’s findings in *Achmea* applied in the context of the ECT, *i.e.* that the investor-State arbitration clause in Article 26 ECT is incompatible with EU law,<sup>20</sup> and therefore that it cannot apply within the EU legal order.

### The *Komstroy* Judgment

#### The ECT Forms Part Of The EU Legal Order

In its September 2, 2021 ruling, the CJEU upheld its jurisdiction over the interpretation of international agreements of the EU and/or its Member States. The Court found that the ECT, being an international

treaty to which the EU is a party, forms an integral part of the legal order of the European Union.<sup>21</sup> The Court further noted that the European Union has exclusive or shared competence over matters of foreign investment, thus confirming that it has jurisdiction to interpret the notion of “investment” in the ECT.<sup>22</sup>

As to the fact that the underlying dispute only involved non-EU parties, the CJEU held that, where a provision of an international treaty can apply to both situations falling within the scope of EU law and outside of that scope, it is “*clearly in the interest of the European Union*” to ensure that that provision will be interpreted uniformly in all circumstances.<sup>23</sup> Moreover, the Court stressed that the parties to the underlying arbitration chose Paris as the seat of the arbitration, thus accepting that French law, together with EU law, would be applicable.<sup>24</sup>

### **Intra-EU Arbitration Under Article 26 ECT Is Incompatible With EU Law**

Turning to the questions referred to it by the Paris Court of Appeal, the CJEU noted that, in order to interpret Article 26 of the ECT, it first had to determine which disputes may be brought to arbitration pursuant to that provision.<sup>25</sup> In this context, the CJEU reiterated and applied its key findings from the *Achmea* Judgment to the ECT.<sup>26</sup>

The Court stressed the importance of the autonomy of EU law and the role of the EU judicial system to ensure consistency and uniformity in the interpretation of EU law. The ECT itself being an act of EU law, an arbitral tribunal established under the ECT “*is required to interpret, and even apply, EU law.*”<sup>27</sup> An arbitral tribunal constituted under Article 26 ECT, however, is not part of the judicial system of an EU Member State and therefore may not make a reference to the Court for a preliminary ruling.<sup>28</sup> Moreover, judicial review by EU Member State courts of an award rendered by an ECT arbitral tribunal is limited in scope.<sup>29</sup> The Court concluded that allowing a dispute between an investor of an EU Member State and another EU Member State to be submitted to arbitration pursuant to Article 26 ECT could therefore undermine the autonomy and full effectiveness of EU law. The CJEU stressed that investment arbitration under the ECT, unlike

commercial arbitration, effectively removes disputes which may concern the application or interpretation of EU law from the EU judicial system.<sup>30</sup>

The Court concluded that the investor-State arbitration clause in Article 26(2)(c) ECT is not applicable to intra-EU disputes.

Turning to the meaning of the term “investment” in the ECT, the CJEU found that *Komstroy’s* alleged investment – a claim arising from a contract for the sale of electricity - could not qualify as an investment under Article 1(6) ECT, as this contractual claim was not connected to an economic activity in the energy sector or to another investment, but arose from a purely commercial contract.<sup>31</sup>

### **Impact For Investors And EU Member States**

The CJEU’s *Komstroy* Judgment is limited to assessing the compatibility of ECT investor-State arbitrations in intra-EU disputes with EU law. It does not concern the substantive investment protections accorded under the ECT. The ECT also remains in force and continues to bind its Contracting Parties, including EU Member States and the EU.

The *Komstroy* Judgment can however be expected to impact investor-State arbitration under the ECT in various ways. Arbitral tribunals constituted under the ECT to resolve intra-EU disputes may face renewed objections to their jurisdiction from EU Member States on grounds of an incompatibility with EU law. EU Member States may also invoke the *Komstroy* Judgment in national courts to resist the recognition and enforcement of ECT intra-EU arbitral awards, and/or to ask for such awards be set aside, including before ICSID *ad hoc* annulment committees.

It remains to be seen whether arbitral tribunals and domestic courts will hold different views on the consequences of the *Komstroy* Judgment on intra-EU arbitration, similar to their diverging views regarding the CJEU’s *Achmea* Judgment. To date, no arbitral tribunal established under an intra-EU BIT has indeed denied jurisdiction based on an incompatibility with EU law in line with the *Achmea* Judgment.<sup>32</sup> At the same time, German courts have followed the *Achmea* Judgment, for example by setting aside the *Achmea*

Award,<sup>33</sup> or finding that the arbitration clause in the Austria-Croatia BIT underlying the *Raiffeisen v. Croatia* arbitration was invalid and thus that the arbitral proceedings were inadmissible, based on an incompatibility with EU law.<sup>34</sup>

Prior to the *Komstroy* Judgment, ECT arbitral tribunals have routinely held that investor-State arbitration under Article 26 ECT is not incompatible with EU law,<sup>35</sup> and tribunals may continue to hold the same position despite the *Komstroy* Judgment. By contrast, EU domestic courts ruling on applications to set aside non-ICSID ECT intra-EU awards may be more deferential to the CJEU's Judgment.<sup>36</sup>

Given the uncertainties surrounding the future of ECT intra-EU arbitration and the enforceability of awards rendered in such arbitrations within and outside the EU, investors may attempt to seat investor-State arbitrations outside the EU or wish to restructure their investments through vehicles incorporated in ECT Member States that are not part of the EU.

### Impact On The Future Of ECT Arbitration

The *Komstroy* Judgment can be expected to also add momentum to the ongoing efforts to modernize the ECT that are driven by the European Commission and EU Member States. The Commission's May 2020 modernization proposal for the ECT indicates that it seeks, *inter alia*, to harmonize the investment provisions of the ECT with the investment agreements

recently entered into by the EU and its Member States and to reform the ECT's investor-State dispute settlement mechanism.<sup>37</sup> The European Commission has also indicated that a withdrawal from the ECT would be an option, should the EU's core objectives for a modernized ECT not be reached within a reasonable timeframe.<sup>38</sup> In December 2020, Belgium announced that it will submit a request to the CJEU to opine on the compatibility with EU law of the arbitration provision in the draft modernized ECT.<sup>39</sup>

Following the *Komstroy* Judgment, it is likely that the discussions around resorting to arbitration to solve ECT investor-State disputes will intensify.

### Conclusion

While answering the long-debated question of the compatibility of ECT investor-State arbitration with EU law, the *Komstroy* Judgment has created additional uncertainties for investment treaty arbitration in the European Union and the ECT.

From a practical perspective, it remains to be seen how domestic courts, arbitral tribunals, foreign investors and EU Member States will handle the legacy of the *Komstroy* judgment.

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CLEARY GOTTlieb

<sup>1</sup> *Republic of Moldova v. Komstroy LLC, successor in law to the company Energoaliants*, Court of Justice of the European Union, Judgment, Case C-741/19 (Sept. 2, 2021) ("**Komstroy Judgment**"), ¶ 66.

<sup>2</sup> *Slowakische Republik (Slovak Republic) v. Achmea BV*, Court of Justice of the European Union, Judgment, Case C-284/16 (Mar. 6, 2018) ("**Achmea Judgment**").

<sup>3</sup> See Declaration of the Representatives of the Governments of the Member States on the Legal Consequences of the Judgment of the Court of Justice in *Achmea* and on Investment Protection in the European Union (Jan. 15, 2019) ("**January 15, 2019 Declaration**") (available [here](#)).

<sup>4</sup> *Komstroy* Judgment, ¶ 65.

<sup>5</sup> See, e.g., *Masdar Solar & Wind Cooperatief U.A. v. Kingdom of Spain*, ICSID Case No ARB/14/1, Award (May 16, 2018); *Antin Infrastructure Services*

*Luxembourg S.a.r.l v. Kingdom of Spain and Antin Energia Termosolar B. V. v. Kingdom of Spain*, ICSID Case No. ARB, 13/2, Award (June 15, 2018); *Vattenfall AB and others v. Republic of Germany*, ICSID Case No. ARB/12/12, Decision on the Achmea Issue (Aug. 31, 2018); *Stadtwerke Munchen GmbH and others v. Kingdom of Spain*, ICSID Case No. ARB/15/1, Award (Dec. 2, 2019); *Mathias Kruck and others v. Kingdom of Spain*, ICSID Case No. ARB/15/23, Decision on Jurisdiction and Admissibility (Apr. 19, 2021).

<sup>6</sup> International Energy Charter, List of all Investment Dispute Settlement Cases (last updated Aug. 3, 2021) (available [here](#)).

<sup>7</sup> International Energy Charter, Statistics of ECT Cases (last updated Aug. 3, 2021) (available [here](#)).

<sup>8</sup> *European Court of Justice: Investor-State Arbitration Under Intra-EU Bilateral Investment Treaties Is*

- Incompatible With EU Law*, Cleary Gottlieb Alert Memo (Mar. 9, 2018) (available [here](#)).
- <sup>9</sup> See January 15, 2019 Declaration (available [here](#)).
- <sup>10</sup> January 15, 2019 Declaration, p. 2.
- <sup>11</sup> See Declaration of the Representatives of the Governments of the Member States (Finland, Luxembourg, Malta, Slovenia and Sweden) On The Enforcement Of The Judgment Of The Court Of Justice In *Achmea* And On Investment Protection In The European Union (Jan. 16, 2019) (available [here](#)), p. 3.
- Declaration of the Representative of the Government of Hungary on the Legal Consequences of the Judgment of the Court of Justice in *Achmea* and on Investment Protection in the European Union (Jan. 16, 2019) (available [here](#)), ¶ 8.
- <sup>12</sup> Austria, Finland, Ireland and Sweden abstained.
- <sup>13</sup> Agreement for the Termination of Bilateral Investment Treaties Between the Member States of the European Union, signed on May 5, 2020 (“**Termination Agreement**”) (available [here](#)).
- <sup>14</sup> *Most EU Member States Agree To Terminate Their Intra-EU Bilateral Investment Treaties*, Cleary Gottlieb Alert Memo (May 7, 2020) (available [here](#)).
- <sup>15</sup> Termination Agreement, Article 4(1).
- <sup>16</sup> Termination Agreement, Preamble, ¶ 10.
- <sup>17</sup> *Energoalians TOB v. Republic of Moldova*, UNCITRAL, Award (Oct. 23, 2013).
- <sup>18</sup> *Komstroy* Judgment, ¶ 16.
- <sup>19</sup> *Komstroy* Judgment, ¶ 21.
- <sup>20</sup> *Republic of Moldova v. Komstroy LLC, successor in law to the company Energoalians*, Court of Justice of the European Union, Case C-741/19, Opinion of Advocate General Szpunar (Mar. 3, 2021).
- <sup>21</sup> *Komstroy* Judgment, ¶ 23.
- <sup>22</sup> *Komstroy* Judgment, ¶¶ 25-27.
- <sup>23</sup> *Komstroy* Judgment, ¶ 29.
- <sup>24</sup> *Komstroy* Judgment, ¶¶ 32-34.
- <sup>25</sup> *Komstroy* Judgment, ¶ 40.
- <sup>26</sup> See *Most EU Member States Agree To Terminate Their Intra-EU Bilateral Investment Treaties*, Cleary Gottlieb Alert Memo (May 7, 2020) (available [here](#)).
- <sup>27</sup> *Komstroy* Judgment, ¶ 50.
- <sup>28</sup> *Komstroy* Judgment, ¶ 53.
- <sup>29</sup> *Komstroy* Judgment, ¶¶ 55-57.
- <sup>30</sup> *Komstroy* Judgment, ¶¶ 59-62.
- <sup>31</sup> *Komstroy* Judgment, ¶¶ 72-80.
- <sup>32</sup> See, e.g., *UP (formerly Le Chèque Déjeuner) and C.D Holding Internationale v. Hungary*, ICSID Case No. ARB/13/35, Award (Oct. 9, 2018); *Theodoros Adamakopoulos and others v. Republic of Cyprus*, ICSID Case No. ARB/15/49, Decision on Jurisdiction (Feb. 7, 2020); *GPF GP S.à.r.l v. Republic of Poland*, SCC Case No. V2014/168, Final Award (Apr. 29, 2020); *Strabag SE, Raiffeisen Centrobank AG and Syrena Immobilien Holding AG v. Republic of Poland*, ICSID Case No. ADHOC/15/1, Partial Award on Jurisdiction (Mar. 4, 2020); *Addiko Bank AG and Addiko Bank d.d. v. Republic of Croatia*, ICSID Case No. ARB/17/37, Decision on Croatia’s Jurisdictional Objection Related to the Alleged Incompatibility of the BIT with the EU Acquis (June 12, 2020). See, however, *Theodoros Adamakopoulos and others v. Republic of Cyprus*, ICSID Case No. ARB/15/49, Statement of Dissent of Professor Marcelo G. Kohen (Feb. 3, 2020).
- <sup>33</sup> See German Federal Court of Justice, Decision, Case I ZB 2/15 (*Achmea B.V. v. Slovak Republic*) (Oct. 31, 2018).
- <sup>34</sup> See Higher Regional Court of Frankfurt, Decision, Case 26 SchH 2/20 (*Raiffeisen v. Croatia (II)*) (Feb. 11, 2021).
- <sup>35</sup> See above, note 5.
- <sup>36</sup> The Swedish Svea Court of Appeal, in a pending preliminary reference procedure, separately requested the Court to review the compatibility of ECT intra-EU arbitrations with EU law. See, Svea Court of Appeal, Case T 3229-19 (*Greentech and Novenergia v Italy*), Decision (Feb. 11, 2021).
- <sup>37</sup> See EU text proposal for the modernization of the Energy Charter Treaty (May 2020) (available [here](#)).
- <sup>38</sup> Answer to the European Parliament by Executive Vice-President Dombrovskis on behalf of the European Commission (Dec. 2, 2020) (available [here](#)).
- <sup>39</sup> Federal Ministry of Foreign Affairs of the Kingdom of Belgium, *Belgium requests an opinion on the intra-European application of the arbitration provisions of the future modernised Energy Charter Treaty* (Dec. 3, 2020) (available [here](#)).