Legal Briefing

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THE COURT OF JUSTICE RULES AGAINST AD HOC ARBITRATION AGREEMENTS THAT ARE IDENTICAL TO CLAUSES CONTAINED IN BILATERAL INVESTMENT TREATIES BETWEEN MEMBER STATES

The Court of Justice of the European Union (the **"CJEU"**) has again ruled on investment arbitration, this time in the *PL Holdings* case. In this new judgment, handed down on 26 October, the CJEU declared that European Union (**"EU"**) law prohibits a Member State from entering into an ad hoc arbitration agreement that is identical in content to an invalid arbitration clause contained in a bilateral investment treaty (**"BIT"**) between Member States. In the wake of the judgments in the *Achmea* and *Komstroy* cases, the decision in the *PL Holdings* case represents a further restriction on investment arbitration within the EU.

1. Facts and main proceedings

The *PL Holdings* case (Case C-109/20) relates to a dispute between the Luxembourg company PL Holdings and the Republic of Poland. The dispute originated in 2013, when Poland's Financial Supervision Authority suspended PL Holdings' voting rights attached to shares it held in a Polish bank, and forced it to sell the shares.

In disagreement with the decision taken by the Polish body, PL Holdings initiated arbitration proceedings against Poland before the Stockholm Chamber of Commerce. In order to do so, it relied on Article 9 of the BIT entered into in 1987 between Belgium and Luxembourg, on the one hand, and Poland, on the other.

The arbitral tribunal resolved the matter in two awards issued on 28 June and 28 September 2017. Firstly, it declared that it had jurisdiction to hear the dispute in question. Secondly, it ruled that Poland had breached its obligations under the BIT, and consequently ordered the state to pay damages to PL Holdings.

Poland sought annulment of the awards before the Stockholm Court of Appeal on the grounds that the arbitration proceedings were based on an invalid arbitration clause. This is because, in accordance with the *Achmea* case law (Case C-284/16), arbitration agreements contained within a BIT signed between Member States are contrary to EU law.

In this regard, the Stockholm Court of Appeal ruled that, while the *Achmea* judgment did render the arbitration agreement contained in Article 9 of the BIT null and void, this did not affect the validity of the awards rendered in the *PL Holdings* case. The Court of Appeal considered that the arbitration was not based on this article, but on an ad hoc arbitration agreement. Therefore, under Swedish law, both parties had concluded a separate arbitration agreement, but with identical content to that of Article 9 of the BIT, which stemmed from the investor's proposal for arbitration and the state's tacit acceptance of it, as it had not challenged the jurisdiction of the arbitral tribunal within the time limit established by Swedish law. As a result, the awards were not annulled.

Poland then filed an appeal before the Swedish Supreme Court, which stayed the proceedings and made a preliminary reference to the CJEU. In particular, the question raised was whether or not EU law allows a Member State to conclude an ad hoc arbitration agreement with an investor from another Member State which is identical in content to an arbitration clause contained in a BIT concluded between those two Member States, when such clause is invalid in accordance with the *Achmea* case law.

2. The CJEU's decision

The CJEU began its consideration by recalling that Article 9 of the BIT is invalid "*on the ground that it undermines the autonomy, effectiveness and uniform application of EU law*"; and that, therefore, arbitration proceedings cannot be brought under that arbitration clause. This clause, according to the CJEU, could lead an arbitral tribunal to decide on disputes concerning the application or interpretation of EU law, which would jeopardise the preservation of the particular nature and autonomy of EU law, as well as the principle of mutual trust between Member States.

This is exactly what was decided in the *Achmea* case, and was later reiterated in the *Komstroy* case (Case C-741/19), which extended the same logic to arbitrations within the EU, but arising from a multilateral investment treaty such as the Energy Charter Treaty (**"ECT"**), rather than from a BIT. The question in this case was whether the CJEU's case law concerning investment arbitration arising from a BIT (as in *Achmea*) and the ECT (as in *Komstroy*) can also be extended to those arising from an ad hoc arbitration agreement.

The CJEU considered that allowing a Member State to submit a dispute to arbitration on the basis of an ad hoc arbitration agreement which is identical to the clause of a BIT that is invalid would effectively circumvent the consequences of the *Achmea* case law. The raison d'être of this agreement would effectively be to replace such a clause, in order to maintain its effects, despite it being invalid.

Therefore, according to the CJEU, EU law prohibits a Member State from concluding an arbitration agreement with the same content as an invalid arbitration clause contained in a BIT between Member States. Based on the above, the CJEU concluded as follows:

(i) with regard to the Member States, that in addition to not undertaking to remove from the EU judicial system disputes which may concern the application and interpretation of EU law, where such a dispute is brought before an arbitral tribunal on the basis of an undertaking which is contrary to EU law, they are obliged to challenge, before that arbitral tribunal or before the court with jurisdiction, the validity of the ad hoc arbitration agreement; and

(ii) with regard to national courts, that they are obliged to set aside an arbitral award made on the basis of an arbitration clause or an ad hoc arbitration agreement which infringes the aforementioned case law.

3. Implications of the *PL Holdings* judgment

This CJEU judgment reveals a further limitation on the ability of EU Member States and investors to submit their disputes to arbitration. As explained above, the main consequence is that the case law

from the *Achmea* and *Komstroy* cases has been extended to arbitrations resulting from an agreement that is identical in content to an arbitration clause contained in a BIT between Member States.

Moreover, the CJEU (contrary to PL Holdings' request) has chosen not to limit the temporal effects of this decision, so it applies retroactively, and even to arbitration proceedings that were initiated in good faith, on the basis of ad hoc arbitration agreements concluded before the *Achmea* judgment. In this respect, it should be noted that, in *PL Holdings*, the contested awards predated this judgment.

However, this new CJEU judgment does not deny the validity of any ad hoc arbitration agreement entered into by a Member State for different types of contracts, but rather only those concluded in circumstances such as those in the *PL Holdings* case:

> "*Moreover, as regards the alleged serious difficulties, it should be noted that, as regards, first, the alleged impact that the present judgment might have on the arbitration agreements concluded by the Member States for various types of contract, the interpretation of EU law provided in the present judgment refers only to ad hoc arbitration agreements concluded in circumstances such as those at issue in the main proceedings and summarised, in particular, in paragraph 65 above*."

Lastly, the CJEU considers that any denial of due process rights that may be caused to investors by preventing them from resorting to arbitration must be corrected within the national judicial systems, with the cooperation of the CJEU if necessary, within the framework of its jurisdiction. This is likely to raise reasonable doubts for investors, given that, for example, in the *PL Holdings* case, the arbitral tribunal found that, prior to the commencement of the arbitration, the investor had been denied access to justice through Polish courts. This is especially true in situations such as the one that is occurring in Poland, where its courts have considered that they are not subject to the principle of the primacy of EU law, in accordance with the recent ruling of the Polish Constitutional Court of 7 October 2021.

This Legal Briefing was prepared by Fernando Bedoya, Ignacio Santabaya and Javier Tarjuelo, Partners and Associate of the Litigation and Arbitration practice respectively.

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For more information,
please contact:

Fernando Bedoya
Litigation and Arbitration Partner
fbedoya@perezllorca.com
T: + 34 91 423 20 75

Ignacio Santabaya
Litigation and Arbitration Partner
isantabaya@perezllorca.com
T: + 34 91 432 51 26