

**IN THE MATTER OF AN ARBITRATION BEFORE THE INTERNATIONAL CENTRE FOR THE
SETTLEMENT OF INVESTMENT DISPUTES**

ICSID Case No. ARB/07/22

BETWEEN

AES SUMMIT GENERATION LIMITED

AES-TISZA ERÓMŰ KFT

Claimants

AND

THE REPUBLIC OF HUNGARY

Respondent

EXPERT OPINION OF PROFESSOR PIET EECKHOUT

THE LAW APPLICABLE TO THE DISPUTE UNDER THE ENERGY CHARTER TREATY 1994

30 October 2008

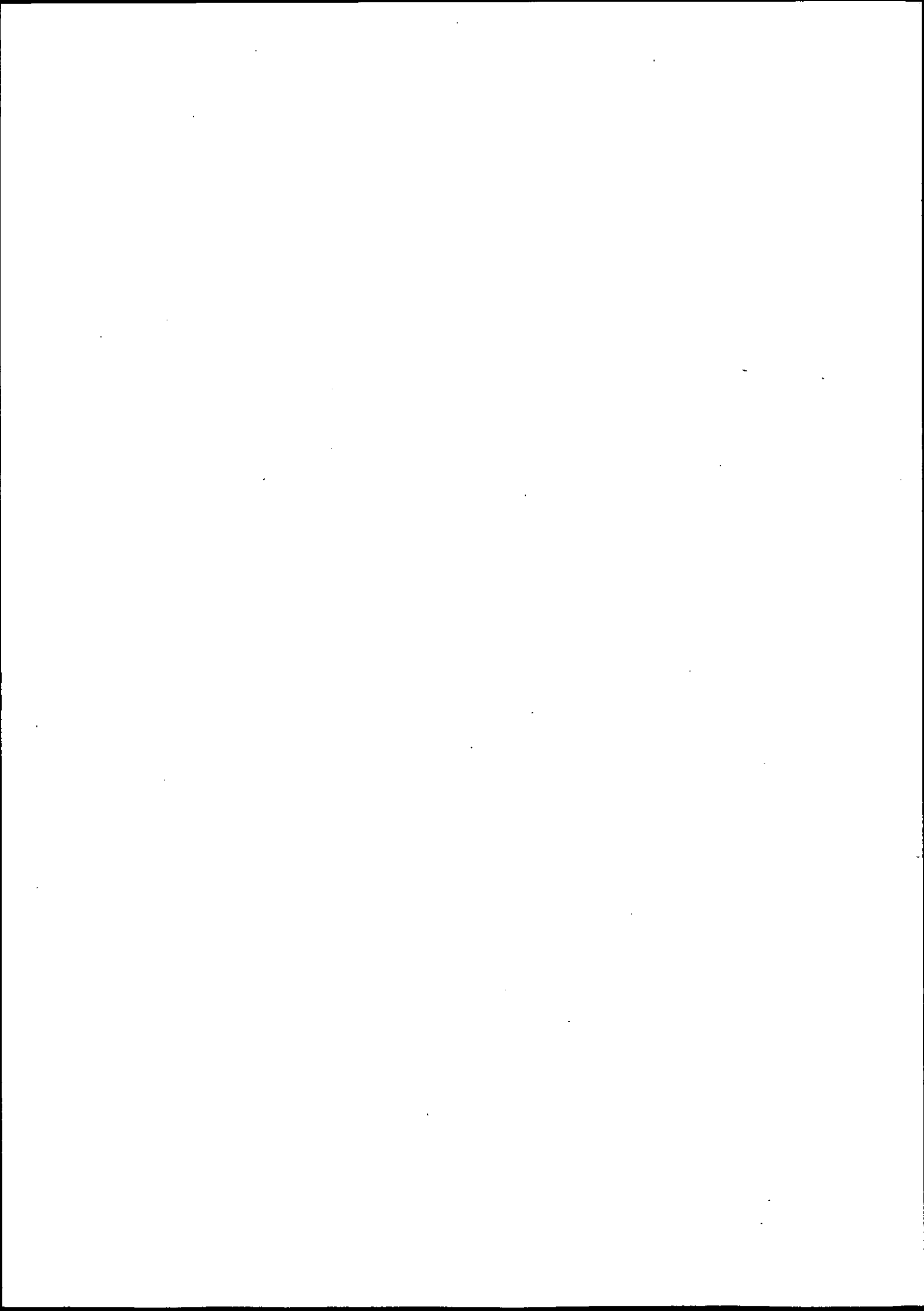
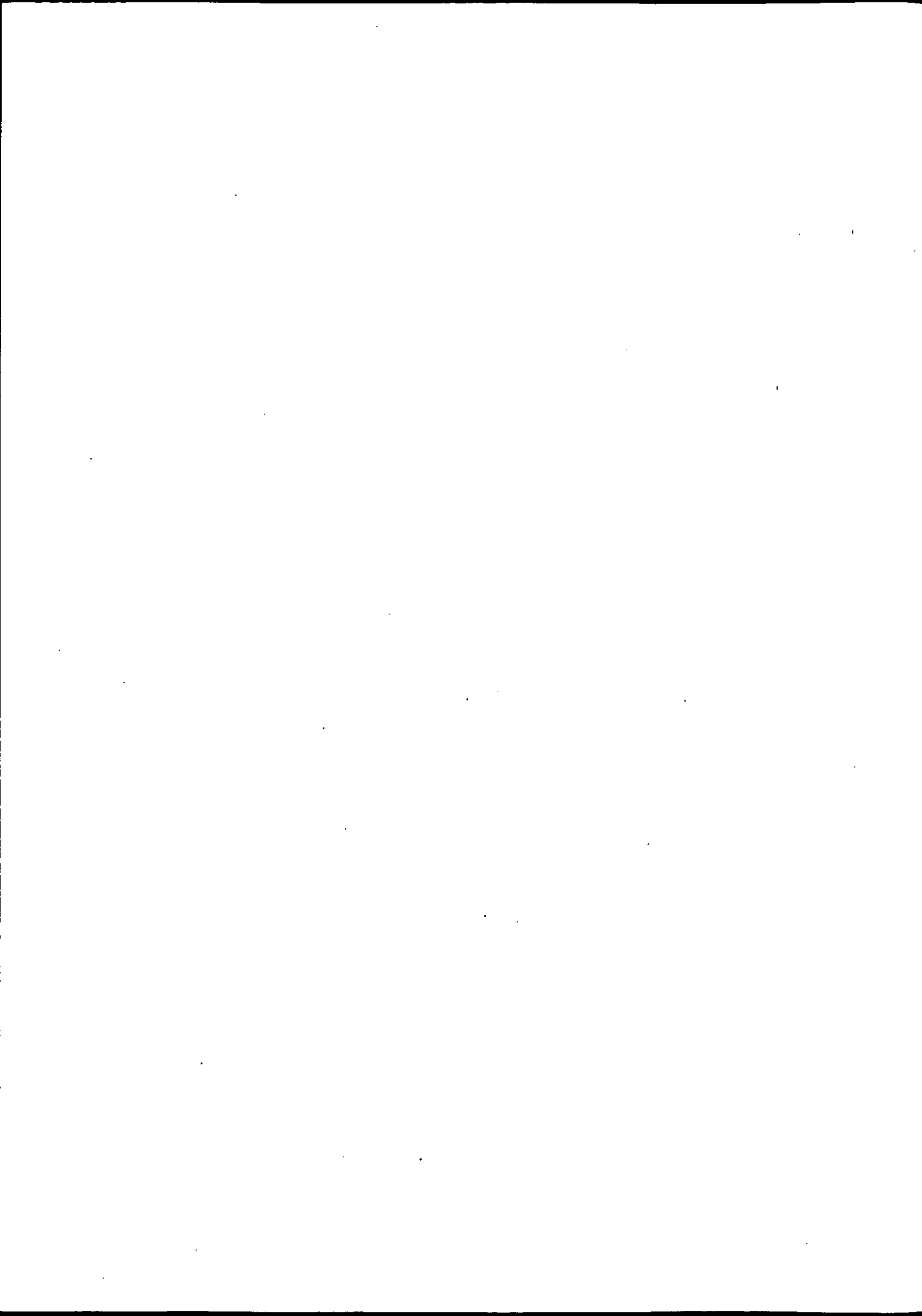


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1. INTRODUCTION¹

1. I, Professor Piet Eeckhout, have been requested by Allen & Overy LLP, acting on behalf of AES Summit Generation Ltd and AES –Tisza Erőmű KFT (together, **AES**), to submit this Expert Opinion on certain matters of international law and European Community law (**EC law**). The purpose of this Expert Opinion, which is independent and impartial and not intended to advocate the views of any of the Parties, is to assist the Arbitral Tribunal to resolve questions about the relevance, or lack thereof, of EC law, and about the legal relationship between EC law and the Energy Charter Treaty 1994 (the **ECT**) in the arbitration proceedings brought by AES against the Republic of Hungary (**Hungary**).
2. For the purpose of preparing my Opinion, I have been provided with copies of the written pleadings that have been filed by the Parties in this case, namely AES's Memorial dated 7 March 2008 and Hungary's Counter-Memorial dated 11 July 2008 (the **Counter-Memorial**), as well as Professor Slot's Expert Report dated 4 July 2008 (the **Slot Report**), along with accompanying exhibits. I have reviewed all of these documents in preparing this Expert Opinion.

1.1 Qualifications²

3. I am Professor of European Law and Director of the Centre of European Law at King's College, University of London. I have been teaching European Community and European Union law, as well as international economic law, for more than fifteen years. In addition to King's College, London, I have taught at the Universities of Ghent and Brussels and I teach at the College of Europe in Bruges. I have been Visiting Professor at various universities, including Georgetown Law Center, the University of Georgia, the European University Institute and the University of Amsterdam.

¹ Throughout this report I refer to various authorities. To avoid burdening the Tribunal with many volumes of unnecessary or repetitive reading, I have not reproduced as exhibits to my report, those authorities which are either easily accessible in the public domain or which are exhibited to the Claimants' Reply. To assist the Tribunal, I exhibit those documents which are not easily accessible and these are produced as Appendix 1 to this Report.

² Attached as Appendix 2 to this report is my Curriculum Vitae.

4. I worked for nearly five years in the chambers of Advocate General F.G. Jacobs at European Court of Justice (the ECJ), where I was involved in a number of well-known cases, particularly in the sphere of European Union (EU) external relations. I am an Associate Academic Member of Matrix Chambers, London. In that capacity I am a regular consultant to parties in litigation before the EU Courts (including in Case T-19/01 *Chiquita v Commission* [2005] ECR II-315, concerning damages for breach of WTO law; and Joined Cases C-402/05 P and C-415/05 P *Kadi and Al Barakaat v Council*, judgment of 3 September 2008, not yet reported, concerning EC implementation of UN Security Council Resolutions in the field of counter-terrorism).
5. I have published extensively in the fields of EC and EU law, as well as international economic law. I have particular expertise in EU external relations law, including the relationship between EC / EU and public international law. I am the author of one of the leading monographs on EU external relations law; I taught the General Course on this subject at the European University Institute's Summer Course (2005), and was General Rapporteur for this subject at the 2006 FIDE Conference (a biennial conference organised by the federation of associations for European law). I am joint-editor, with Professor Takis Tridimas, of the Yearbook of European Law, and I am a member of the editorial board of various European and international law journals.

1.2 Scope and structure of the expert opinion

6. The questions which Allen & Overy LLP put to me are as follows:
 - (1) What is the law applicable to the dispute;
 - (2) how, and in relation to what, is that law to be interpreted;
 - (3) what is the relevance, if any, of EC law and how does it relate to the ECT; and
 - (4) is there a 'circularity' problem should the Tribunal find in AES's favour?
7. In seeking to reply to those questions I have structured the Opinion as follows. In Section 2, I offer an executive summary of the main findings. The Opinion then turns to the question of applicable

law, in Section 3, which examines the relevant rules and principles. Section 4 examines, in greater depth, the question of how to interpret the provisions of the ECT. Section 5 considers in what way a potential conflict between the ECT and EC law should be resolved. It looks at such potential conflicts both from the perspective of the ECT itself, which is a treaty under international law, and from the perspective of EC law. Section 6 addresses, more in particular, the enforceability of an ICSID Arbitral Award in this case, in the light of EC law on the recovery of State aids. Both Sections 5 and 6 in substance analyse the alleged 'circularity' problem to which both the Counter-Memorial and Professor Slot's Opinion refer: as will be seen, such a circularity problem does not and will not arise, because in the matters which it regulates, the ECT prevails over EC law, and because EC law fundamentally respects international law, including the obligations of EU Member States under the ECT. Section 7 draws together my conclusions.

8. At the outset it is important to emphasize some crucial distinctions which pervade this Opinion. Public international law and EC law constitute different and distinct legal systems (as will be further analysed). The fundamental argument of this Opinion is that the Tribunal should apply international law, and not EC law, to this dispute. Where this Opinion discusses points of EC law, its purpose is strictly limited to *informing* the Tribunal of the position, under EC law, of the ECT, of Hungary's obligations under the ECT, and of the status and enforceability of the Tribunal's Arbitral Award. At no point is it suggested that the Tribunal should itself apply EC law.

2. EXECUTIVE SUMMARY

9. The law applicable to this dispute is, according to Article 26(6) ECT, the ECT itself and the applicable rules and principles of international law. EC law is not part of that applicable law. Hungary has suggested two avenues through which EC law could become legally relevant for the Tribunal. The first is that the ECT should be interpreted in the light of EC law. The second is that, if there were a conflict between the ECT and EC law, the latter would prevail. Neither of those positions is tenable.

10. The ECT should not be interpreted in accordance with EC law: Customary international law rules on the interpretation of treaties emphasize the ordinary meaning of the terms, in the light of their context, and their object and purpose. Preparatory work and the circumstances of a treaty's conclusion are only relevant where there is ambiguity, obscurity, manifest absurdity or unreasonableness. No such issues arise in relation to the interpretation of the ECT.
11. Even if it were necessary to take into account the ECT's origins, the conclusion could only be that the ECT is not a mere instrument of EC law or policy. Its membership extends beyond Europe, its terms are not based on and do not refer to EC law, and the sole intentions of the EC as a Contracting Party are not a basis for the ECT's interpretation. The ECT presents much closer links with GATT and WTO law than with EC law.
12. More particularly, the ECT should not be interpreted in the light of EC competition law. In sharp contrast with the EC Treaty, the ECT in no way addresses State aids or subsidies. Its competition provisions are targeted at private anti-competitive conduct, not governmental aids or subsidies. Therefore, no provisions of the ECT need to be interpreted in the light of EC State aid law. The judgment of the ECJ in *Eco Swiss* is irrelevant to the Tribunal's interpretative exercise: it does not concern ICSID arbitration; rather, it concerns EC law, not the ECT and private anti-competitive conduct, not State aids.
13. The EC and its Member States concluded the ECT as a "mixed agreement", and are each full Contracting Parties to the ECT, because they share competence in matters governed by the ECT. However, the internal division of competences between the EC and its Member States is irrelevant for the purpose of this dispute. The ECT was not "carved up" into an EC and a Member States part, nor did the EC and its Member States make a formal declaration of competences under international law. This means that the EC and its Member States are jointly liable for the full extent of their obligations under the ECT. For Hungary, this means that its accession to the EU in no way diminished its obligations under the ECT.

14. Furthermore, the absence of a so-called “disconnection clause” demonstrates that the EU Member States assumed international obligations, also in their *inter se* relations, when they concluded the ECT. In the field of investor protection those obligations are much further reaching than EC law, both in a procedural sense (the availability of international arbitration) and in a substantive sense (more extensive protection of an investment).
15. If there were a conflict between the ECT and EC law, it would have to be resolved in favour of the ECT. That is the position, both under international law and EC law.
16. Under international law, the first point is that the ECT contains no disconnection clause which would have the effect of rendering it inapplicable in relations between EC Member States. Second, the ECT itself regulates conflicts between its provisions on investor protection and other international treaties: the provisions more favourable to the Investor or Investment will apply. In the circumstances of the present case, the ECT provisions are clearly the more favourable. Third, there is no scope for applying the *lex posterior* principle, because the ECT itself expressly regulates potential conflicts. Nor would *lex posterior* yield a result, because it is not clear what that *lex* is for Hungary and the United Kingdom. Fourth, the ECT made no specific exception for EC law, as it did for the Svalbard Treaty.
17. Under EC law, the position is the same. EC law respects international law, in particular as it stems from treaties the EC has concluded. The ECT is such a treaty. The EC institutions are under a strict obligation to respect the ECT. A private party could rely on the direct effect of the ECT, as against an act of the EC institutions. Likewise, the EC institutions must respect the decisions of an ICSID Tribunal, issued pursuant to the ECT.
18. Furthermore, the EC Treaty, in Article 307, allows Hungary to derogate from EC law – including from EC State aid law – for the purpose of honouring its obligations under the ECT. Article 307 EC concerns obligations a Member State entered into pursuant to an international agreement concluded prior to accession to the EU. The ECT is such an agreement. It is irrelevant that the obligations in issue are owed to a private party, and not to a non-member State: Article 307 is simply declaratory of

the position under international law. Hungary's accession to the EU could not modify its obligations under the ECT.

19. Finally, an ICSID award is automatically enforceable. Even if it were to conflict with an EC State aid decision ordering the recovery of the aid, it is the latter decision which could not be enforced. Member States may rely on an absolute impossibility of recovery. Nor may recovery be ordered if it were in breach of general principles of EC law, which includes fundamental respect for the rules of international law.

20. The conclusion is that the 'circularity' issue does not arise.

3. APPLICABLE LAW

21. Pursuant to Article 26(6) ECT the Tribunal "*shall decide the issues in dispute in accordance with this Treaty and applicable rules and principles of international law*". This provision defines the applicable law before the Tribunal. That law consists of the ECT and applicable rules and principles of international law. It does not extend to the law of the European Union (the EU) or the law of the European Community (the EC).³ EC law constitutes a legal order of its own, distinct from public international law.⁴ It is, therefore, not applicable to this dispute. No party has suggested otherwise.

22. Hungary suggests two possible avenues through which EC law should become relevant to the Tribunal's legal analysis. The first is that the provisions of the ECT should be interpreted in light of EC law. The second is that, in the event of a conflict between the ECT and EC law, the latter should prevail. However, both those avenues are barred. In the following section I analyse the relevant international law rules concerning treaty interpretation, and apply them to the ECT. The conclusion I reach is that there is no basis for the claim that the ECT should be interpreted in light of EC law. In Section 5.2, I demonstrate that, if there were a conflict between the ECT and EC law, it would be the ECT which would prevail.

³ In what follows reference will mostly be made to EC law and to the EC Treaty, since most of the relevant legal provisions are found in the EC Treaty. Occasionally reference is made to the EU as an international organization, because the EU encompasses the EC, and EC policies are generally attributed to the EU.

4. INTERPRETATION OF THE ECT

4.1 Treaty interpretation

23. Articles 31 and 32 of the Vienna Convention on the Law of Treaties (the VCLT) are considered to codify the rules of customary international law concerning treaty interpretation. The starting point, according to those provisions, is “*the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose*” (Article 31(1)). Preparatory work and the circumstances of the treaty’s conclusion are only relevant as supplementary means of interpretation, where the interpretation in accordance with Article 31 leaves the treaty’s meaning ambiguous or obscure, or leads to a result which is manifestly absurd or unreasonable (Article 32).
24. I have seen the arguments developed in the Respondent’s Counter-Memorial⁵ as well as in the Expert Report of Professor Slot,⁶ in relation to the close link between the ECT, on the one hand, and EU law and policies in the energy sector, on the other. The Counter-Memorial suggests that the ECT was “*the brainchild of the European Union*”⁷ and that it has its “*origins as an instrument of broader EU policy*”.⁸ It cannot therefore be read “*as if it were entirely independent of critical EC laws and developments*”.⁹ Prof. Slot argues that “[t]he notion that the ECT should be interpreted as much as possible in harmony with EC law, rather than in conflict with it, also flows naturally from the history of the ECT itself”.¹⁰
25. The suggestion that the ECT should be interpreted in the light of EC law finds no basis in the relevant rules of treaty interpretation. As mentioned, preparatory work and the circumstances of a treaty’s conclusion are only relevant as supplementary means of interpretation. It first needs to be shown that the application of Article 31 leaves the treaty’s meaning ambiguous or obscure. I find no

⁴ ECJ, Case 26/62 *Van Gend en Loos* [1963] ECR I.

⁵ Counter-Memorial, paras. 306 to 314.

⁶ Slot Report, paras. 175 to 177.

⁷ Counter-Memorial, para. 307.

⁸ Counter-Memorial, para. 309.

⁹ Counter-Memorial, para 306.

¹⁰ Slot Report, para. 175.

indication that this is the case. In any event, neither Hungary nor Professor Slot point to any specific provisions of the ECT on investment and investor protection which they believe are ambiguous or obscure when interpreted according to their ordinary meaning, in their context and in the light of the ECT's object and purpose. Nor is there any indication that the application of Article 31 leads to a manifestly absurd or unreasonable result. Thus, it is not necessary to engage in the interpretation of the ECT in accordance with its history as Hungary suggests.

26. In any event, it is my opinion (a) that the ECT is not a mere extension and instrument of EU policies in matters of energy, and (b) that the norms of free competition, which are said to "*pervade the ECT*"¹¹ are irrelevant to this dispute because they address private anti-competitive conduct and not State aids or subsidies.

4.2 The ECT is not an EU instrument

27. The ECT is clearly not a mere extension and instrument of EU policies in matters of energy for the following five reasons.¹²
28. First, it may well be true that the EU considers the ECT to be an instrument of EU energy policy but that has no relevance in matters of interpretation of the ECT. The intentions of a single contracting party to a treaty, not expressed in the text of that treaty, are not relevant to its interpretation. There is no room under the VCLT provisions, to revert to the intentions of a single contracting party to a multilateral treaty.¹³

¹¹ Counter-Memorial, para. 310.

¹² Cf. Editor's Preface, in T.W. Wälde (ed.), *The Energy Charter Treaty – An East-West Gateway for Investment and Trade* (Kluwer Law International, 1996), page xix., produced as Exhibit PE-1, where Wälde points to a range of precedents for the ECT, including the Havana Charter, UN and World Bank instruments, and the GATT Uruguay Round agreements, whilst recognizing that the ECT was also much influenced by the EU's relative success in driving towards an internal market. See also J. Doré, *Negotiating the Energy Charter Treaty*, in Wälde, pages 137 to 153, produced as Exhibit PE-2, showing the important role played by the USA and others, next to the EC, in the negotiations.

¹³ Cf. WTO Appellate Body, *EC – Computer Equipment* (WT/DS62/AB/R, WT/DS67/AB/R and WT/DS68/AB/R, 5 June 1998), at para. 84: "*The purpose of treaty interpretation under Article 31 of the Vienna Convention is to ascertain the common intentions of the parties. These common intentions cannot be ascertained on the basis of the subjective and unilaterally determined "expectations" of one of the parties to a treaty.*"

29. Secondly, it is correct that the EC took the initiative to suggest the drawing up of the European Energy Charter, which led to the ECT. The EC is an important Contracting Party to the ECT. However, that does not mean that the ECT is a mere instrument of the EC (or, more broadly, the EU).¹⁴ Other multilateral agreements are also, at least in part, the result of EU or EC initiatives. For example, the EU was a key player in the negotiations establishing the World Trade Organization. That does not mean that the WTO is an instrument of the EU, let alone that WTO law must be read in harmony with EU or EC law.
30. Thirdly, the ECT's membership extends beyond Europe. A number of Asian countries, including Japan, are Contracting Parties to the ECT.¹⁵ The ECT therefore cannot be understood as relevant only to countries seeking to join the EU. In that sense, the ECT is, as a multilateral instrument, fundamentally different from, for example, the Europe Agreements, which prepared Central and Eastern European countries for accession to the EU.
31. Fourthly, the terms of the ECT in no way refer to any structural link with EC or EU law or policy. The terms "EC" or "EU" are absent from the text of the ECT. The only textual connection is the fact that the preamble of the ECT makes general references to the objectives and principles of the European Energy Charter; and the preamble to the latter provides that the Signatories are "[a]ssured of support from the European Community, particularly through completion of its internal energy market". No other provisions of the European Energy Charter refer to the EC.
32. Fifthly, the object and content of the ECT are substantially different from those of the EC Treaty. The ECT is not regional in character and does not aim at the kind of integration which the EU or the EC is pursuing.¹⁶ Nor does the ECT appear to contain any provisions which are inspired by EC law rules or principles. By contrast, the ECT contains numerous provisions which refer to, or are inspired by, the law of the GATT and of the WTO.¹⁷ Examples are:

¹⁴ The EU and the EC are, of course, distinct entities. It is the EC which is a signatory to the ECT.

¹⁵ In fact, of the 53 signatories of the ECT listed by the Energy Charter Secretariat as at 8 May 2007, 24 are non-EU countries.

¹⁶ See further H.-J. Schroth, *The Energy Charter Treaty in the Context of the Treaties of the European Union*, in Wälde, *supra*, pages 244 to 246, produced as **Exhibit PE-3**, pointing out that the ECT establishes no supranational structure.

¹⁷ Cf. C.S. Bamberger, *An Overview of the Energy Charter Treaty*, in Wälde, *supra*, at pages 3 to 8 and 17 to 18, produced as **Exhibit PE-4**.

- Article 4 on non-derogation from the WTO Agreement;
- Article 5 on trade-related investment measures;
- Article 7 on transit;
- Article 20 on transparency; and
- Article 24 on exceptions.

33. These references are natural, given that the ECT is a global treaty, open to accession by States and Regional Economic Integration Organizations, also beyond Europe. It is not hereby suggested that the ECT is a mere clone of the WTO. What is however striking is that the terms of the ECT have a much closer connection with WTO law than with EC law. It was expressly contemplated that the ECT would “*create an intermediary step towards WTO membership for those ECT countries that [were] not yet WTO members.*”¹⁸

34. Finally, it may be noted that the EC's policies in matters of energy are still of limited scope. The EC Treaty, in its current version, mentions “*measures in the [sphere] of energy*” as one of the Community's activities.¹⁹ However, in contrast with other Community policies, there is no separate Title in the EC Treaty devoted to energy, and the concept is only referred to in Article 154 on trans-European networks and in Article 175 EC on environmental protection. The lack of a fully-fledged EC policy on energy is often deplored in general discussions about the relevance of the EC for its citizens.²⁰

35. The conclusion I therefore reach is that the ECT is by no means a mere brainchild of the EU (or for that matter, the EC) nor a mere extension of EU or EC energy policies. Indeed, even if it was, which it clearly was not, that would not be a valid basis for interpreting the ECT in the light of EC law.

¹⁸ *The Energy Charter Treaty: A Reader's Guide*, published by the Energy Charter Secretariat and available from http://www.encharter.org/fileadmin/user_upload/document/ECT_Guide_ENG.pdf, page 10.

¹⁹ Article 3(1)(u) EC Treaty.

²⁰ Note that the Treaty of Lisbon would introduce a separate Title on Energy (Article 194 of the Consolidated Version of the Treaty on the Functioning of the Union). The fate of the Treaty of Lisbon is however uncertain after the negative referendum in Ireland.

4.3 No interpretation in light of EC competition law

36. As mentioned, Hungary suggests that “*norms of free competition pervade the ECT*”,²¹ and appears to regard those norms as relevant to the interpretative exercise in which the Tribunal must engage. It is not, however, very specific with regard to those norms. It simply refers²² to Article 6(1) ECT, according to which the Contracting Parties “*shall work to alleviate market distortions and barriers to competition in Economic Activity in the Energy Sector*”; and to Article 24(3)(c) which provides that “*the provisions of this Treaty ... shall not be construed to prevent any Contracting Party from taking any measure which it considers necessary ... for the maintenance of public order*”. These provisions call for a number of comments.
37. Article 6(1) ECT is a general provision, which must clearly be read in the light of the remainder of the Article, as well as of the preamble. Such a reading reveals that the ECT does not contain provisions directed at State aids or subsidies.²³ Article 6(2) speaks about laws concerning “*unilateral and concerted anti-competitive conduct*” and Article 6(5) further addresses “*anti-competitive conduct*”. The preamble to the ECT speaks of “*competition rules concerning mergers, monopolies, anti-competitive practices and abuse of a dominant position*”. These terms speak for themselves. They address various forms of *private* anti-competitive conduct, not governmental aids or subsidies. That is further confirmed by Annex T to the ECT. That Annex concerns transitional arrangements for a number of Contracting Parties who, at the time of their accession to the ECT, did not yet comply with Article 6(2) and (5), because they did not yet have the required legislation and institutions for enforcing a competition policy. The Annex specifies the existing laws of those Contracting Parties and their defects in the light of those ECT provisions. At no point is any reference made to missing legislation regarding governmental aids or subsidies. Moreover, as has been pointed out, the ECT does not promote a strict competition policy.²⁴

²¹ Counter-Memorial, para. 310.

²² Counter-Memorial, para. 311.

²³ See also K. Holmes, *Legal Implications of the Energy Charter Treaty Competition-Rules and Liberalization*, in Wälde, *supra*, pages 546 to 561, produced as Exhibit PE-5. The author analyses the ECT competition provisions and compares them to EC competition law, but makes no mention whatsoever of State aids or subsidies, or of the relevant EC Treaty provisions.

²⁴ H.-J. Schroth, *supra*, pages 243 to 244.

38. One also needs to bear in mind that the EC State aid regime is unique, in the sense that it involves a supranational organization monitoring and reviewing aids provided by its Member States. The Contracting Parties to the ECT who are not members of the EU are not subject to such a regime. Some of the non-EU Contracting Parties are subject to Article XVI GATT and the Agreement on Subsidies and Countervailing Measures, which are part of WTO law (obviously only insofar as ECT Contracting Parties are members of the WTO). However, although the ECT constantly refers to, and many of its terms are inspired by, WTO law, it makes no reference to WTO law on subsidies, and does not prohibit such subsidies in any way. Nor does it make WTO law on subsidies applicable between the Contracting Parties.
39. The Counter-Memorial also refers to Article 24(3)(c) ECT, and to the ECJ's judgment in the *Eco Swiss* case,²⁵ arguing that, in that judgment, the Court directly confirmed that EC competition law is part of the notion of public order. The *Eco Swiss* case arose pursuant to a reference to the ECJ from the Netherlands' Hoge Raad. Under Netherlands' law the ordinary courts have power to review arbitration awards for consistency with "public policy". The question was whether this notion of national public policy should be extended to EC competition law, *in particular* Article 85 EC (currently Article 81 EC) on agreements between undertakings which distort competition. The ECJ decided that this was indeed required, because "*Article 85 of the Treaty constitutes a fundamental provision which is essential for the accomplishment of the tasks entrusted to the Community and, in particular, for the functioning of the internal market*".²⁶
40. However, there are a number of differences between the ruling in *Eco Swiss* and the circumstances of the present case. The Court did not, in the English language version, employ the notion of "public order", but rather that of "public policy".²⁷ The latter concept appears broader than the former. Furthermore, the *Eco Swiss* case concerned a form of domestic arbitration where review of the arbitral award by the ordinary courts is provided for. It did not concern international arbitration of

²⁵ Counter-Memorial, para. 311.

²⁶ ECJ, Case C-126/97 *Eco Swiss v Benetton International* [1999] ECR I-3055, para. 36.

²⁷ However, in the French and Dutch versions of the judgment the Court does use the concept of "ordre public" and "openbare orde".

the ICSID kind, which is self-executing. Article 53(1) of the ICSID Convention provides that the award “shall not be subject to any appeal or other remedy except those provided for in this Convention.”

41. One should also note that *Eco Swiss* concerned private anti-competitive conduct, not State aid. There are no ECJ judgments extending the *Eco Swiss* ruling to the EC Treaty provisions on State aid. The ECJ’s ruling in *Eco Swiss* is clearly inspired by the concern that private companies should not be permitted to conclude anti-competitive contracts enforceable through arbitral awards, which are legally binding on the parties to such contracts. No such concern arises in the circumstances of this case. The ECT is obviously not a contract between Claimant and Hungary which has as its object to evade EC competition law. It is an international treaty between sovereign States, and has the EC itself as a contracting party. A last point to note is that the ECJ’s interpretation of what constitutes an issue of “public policy”, or even “public order”, is a matter of EC law, not international law. The notion of “public order” in Article 24(3)(c) must be interpreted under public international law, and that interpretation must obviously be a general one, which is common to all the ECT Contracting Parties, not just EU Member States.

42. The overall conclusion I reach is that, under international law, there is no basis for the suggestion that the ECT must be interpreted in harmony with EC law. In fact, as required by Article 31 of the VCLT, the ECT should be read on its own.

5. THE ECT PREVAILS OVER EC LAW IN MATTERS OF ENERGY

5.1 The ECT from the perspective of EC law

(a) The ECT is a “mixed agreement”

43. The ECT is, in EC law terminology, a “mixed agreement”, i.e. it was signed and concluded by both the EC and its Member States. It may be useful to describe here some of the main features and characteristics of mixed agreements, and to see what they mean for a treaty like the ECT.

(b) Features of a “mixed agreement”

44. The EC is an international legal person, and is capable of concluding international agreements to achieve its objectives. The EC Treaty provides for both express and implied powers to conclude agreements. An example of an express power is Article 133 EC, on the common commercial policy. That provision is the basis for the EC’s conclusion of international agreements in matters of trade. The ECJ has also accepted that, even when the EC Treaty does not expressly provide for the power to conclude an agreement, the EC can do so if the agreement is necessary to achieve its objectives or if the provisions of the agreement affect an EC act.²⁸ The conclusion of international agreements is regulated by Article 300 EC. It must further be noted that certain external EC powers are exclusive in nature, for example the EC’s powers under the EC Treaty provisions on the common commercial policy.²⁹ That means that international agreements coming within those powers can only be concluded by the EC, and not by the Member States. However, most EC external powers are “concurrent” or “shared” with those of the Member States. This means that, although the EC may conclude an agreement under such powers, it need not do so, and may leave international action to its Member States.
45. The EC is generally subject to the principle of conferred powers. According to Article 5 EC “[t]he Community shall act within the limits of the powers conferred upon it by this Treaty and of the objectives assigned to it therein”. In other words, the EC does not have full powers to act under international law in the way a sovereign State does. The legal justification for a mixed agreement is that the agreement cannot be concluded by the EC alone, because its competences do not cover the entire agreement. Participation by the Member States is required because of these limitations to the EC’s external powers. The ECT is such a mixed agreement, as the EC and its Member States considered that certain provisions of the ECT, such as those on investor protection, come within the powers of the Member States, and not those of the EC.

²⁸ ECJ, Opinion 1/03 re *Competence of the Community to conclude the new Lugano Convention on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters* [2006] ECR I-1145, paras. 115 to 133.

²⁹ ECJ, Opinion 1/75 re *Local Cost Standard* [1975] ECR 1355, 1363 to 1364.

46. When the EC and its Member States conclude a mixed agreement (which they do frequently), there are, in principle, a number of options open to them. They could "carve up" the agreement by allocating responsibility for one area to the EC and another to the Member States. They could thus expressly indicate which of the agreement's provisions bind the EC, and which bind the Member States. That option is, however, hardly ever used.
47. Another option is for both the EC and its Member States to conclude the entire agreement, but to add a "declaration of competences" of some kind, so as to indicate to the other contracting parties that competences are divided between the EC and its Member States. Examples of agreements for which such declarations have been made are the UN Convention on the Law of the Sea (UNCLOS), and the EC's participation in the Food and Agriculture Organization.³⁰ The legal effects of such a declaration will depend on its exact terms and on the relevant provisions of the agreement.
48. A third option is to remain silent as to the division of competences, and to give no official notice to the other contracting parties of where the boundaries of EC and Member State competences lie with respect to the agreement in question. In such cases, the only official indication of the scope of the EC's competences (and by implication those of the Member States) is to be found in the EC Council's decision to conclude the agreement, which needs to refer to the legal basis for such conclusion in the EC Treaty. But that Council decision is, of course, an internal act under EC law, not an international act. This third option is the most frequently used one, and it was followed with respect to the ECT. The EC and its Member States did not carve up the ECT between them, and they made no declaration of competences.

(c) International liability of the EC and Member States under the ECT

49. What are the consequences, under international law, of such joint participation by the EC and its Member States in a treaty such as the ECT, which is not carved up and for which no declaration of competences was made? What does this mean in terms of the international responsibility of the EC and its Member States?

50. There is, as yet, no clear case law of any international courts or tribunals on the responsibility of the EC and its Member States under either the ECT or under other mixed agreements with similar features (i.e. no “carving up” and no declaration of competences).³¹
51. However, the ECJ has made certain statements about international responsibility in the case of a mixed agreement where no declaration of competences was made, and where the agreement contains no indication of which obligations were entered into by which party (EC or Member States). Those statements are a useful indication of how the ECJ conceives of the position under international law. In *Parliament v Council*, regarding the Lomé IV Convention, Advocate General Jacobs stated that, under a mixed agreement, the EC and the Member States are jointly liable unless the provisions of the agreement point to the opposite conclusion.³² The Court confirmed this.³³ In *Hermès*, a case which concerned the WTO Agreement, the Court referred to the fact that the agreement was concluded by the EC and ratified by its Member States without any allocation between them of their respective obligations towards the other Contracting Parties.³⁴ Implicitly, therefore, the Court again assumed that the EC and its Member States are jointly liable.
52. The majority of academic literature also adopts this approach of joint liability,³⁵ and so does the Special Rapporteur to the International Law Commission on Responsibility of International Organizations, Professor Gaja.³⁶

³⁰ See, respectively, Annex IX to UNCLOS and Article II FAO Constitution as well as Rule XLI of the FAO General Rules.

³¹ As regards the WTO, see P. Eeckhout, *The EU and its Member States in the WTO – Issues of Responsibility*, in L. Bartels and F. Ortino (eds), *Regional Trade Agreements and the WTO Legal System* (Oxford University Press 2006), pages 449 to 464, produced as **Exhibit PE-6**.

³² ECJ, Case C-316/91 *Parliament v Council* [1994] ECR I-625, para. 69 of the Opinion of Mr Advocate General Jacobs.

³³ *Idem*, para. 29 of the Judgment of the ECJ.

³⁴ ECJ, Case C-53/96 *Hermès International v FHT* [1998] ECR I-3603, para 24; see also the Opinion of Advocate General Tesauo, paras. 14 and 20; ECJ, Joined Cases C-300/98 and 392/98 *Parfums Christian Dior v Tuk Consultancy* [2000] ECR I-11307, para. 33.

³⁵ See e.g. E. Stein, *External Relations of the European Community; Structure and Process*, in *Collected Courses of the Academy of European Law*, Volume I, Book 1, (Dordrecht: Nijhoff, 1991), page 162, produced as **Exhibit PE-7**; G. Gaja, *The European Community's Rights and Obligations under Mixed Agreements*, in D. O'Keefe and H.G. Schermers (eds), *Mixed Agreements* (Deventer: Kluwer, 1983), page 137, produced as **Exhibit PE-8**; and C. Tomuschat, *Liability for Mixed Agreements*, in O'Keefe and Schermers, *ibid.*, page 130, produced as **Exhibit PE-9**.

³⁶ ILC, Second report on responsibility of international organizations by Mr. Giorgio Gaja, Special Rapporteur, 56th session, UN Doc. A/CN.4/541, pages 4 to 5: “In case of an infringement of a mixed agreement that does not distinguish between the respective obligations of the EC and its member States — either directly, or by referring to their respective competencies — responsibility would be joint towards the non-member State party to the agreement.”

53. Joint liability is further confirmed by the Transparency Statement which the EC made in accordance with Article 26(3)(b)(ii) of the ECT: “*The European Communities and their Member States have both concluded the Energy Charter Treaty and are thus internationally responsible for the fulfilment of the obligations contained therein, in accordance with their respective competence*”.³⁷
54. The conclusion is that the EC and its Member States are jointly liable for the fulfilment of all the obligations entered into under the ECT. There are a number of consequences which flow from this finding. One is that the ECT creates international law obligations, also between the EC Member States, in their *inter se* relations. This is further confirmed by the absence of a so-called “disconnection clause”, which would have the object of ensuring that no such *inter se* obligations are created.³⁸ A further consequence is that Hungary’s accession to the EU in no way modified its obligations under the ECT. When Hungary concluded the ECT it undertook to guarantee investor protection to investors from other Contracting Parties, including the United Kingdom where the Claimant is based. That international undertaking was in no sense modified by Hungary’s accession to the EU which, from Hungary’s perspective, turned the ECT into a mixed agreement. Hungary continues to be fully liable at the international level.

(d) Non-applicability of the EC's internal division of competences

55. It must further be stressed that the question of where competence lies as between the EC and its Member States in matters of investment promotion and protection is a question of “internal” EC law, not a question of international law and is, therefore, irrelevant here. Even if it were established that in such matters the Member States have transferred certain, or even all powers to the EC (by accession to the EU), their international responsibility under the ECT would remain intact and complete.

³⁷ Energy Charter Secretariat, Transparency Document: Policies, Practices and Conditions of Contracting Parties Listed in Annex ID not Allowing an Investor to Resubmit the same Dispute to International Arbitration at a Later Stage As Provided by Contracting Parties, 3 April 2008, page 4, available at <http://www.encharter.org/fileadmin/user_upload/document/Annex_ID.pdf>.

³⁸ For more detail, see Section 5.2(a) below.

56. However, the EC and its Member States generally share powers in matters of investment promotion and protection, and the EC's powers in this field are limited. Although this is a question of EC law with which the Tribunal in no way needs to concern itself, it may be useful, for the purpose of information and completeness, to indicate briefly how these powers are shared. Such an analysis also highlights the unique contribution which the ECT makes to investor protection, offering both procedural and substantive guarantees which are not present in "internal" EC law.
57. Indeed, one of the central purposes of the ECT is to offer investor protection, which is "*arguably the most extensive around*",³⁹ whereas EC internal market law does not cover all aspects of investment promotion and protection. As shown below, there are procedural thresholds in EC law, not present in the ECT and, even should these be surmounted, EC law does not provide remedies to compensate a party for loss suffered in the way the ECT does.
58. The EC Council and Commission decision to conclude the ECT gives only a limited indication concerning the division of competences between the EC and its Member States. It states that "*Article 73c(2) [now Article 57(2)] of the Treaty establishing the European Community must be used as a legal basis for this Decision, since the Energy Charter Treaty imposes certain obligations on the European Communities regarding the movement of capital and payments between the Communities and third country contracting parties to the Energy Charter Treaty*". It further indicates that the ECT "*could affect legislative acts based on Article 235 [now Article 308] of the Treaty*".⁴⁰ It is, in any event, clear from those considerations that the EC institutions considered that the EC's powers in relation to the ECT were of limited scope.
59. From the perspective of EC law, a distinction must be made between the "external" and "internal" dimensions of investment promotion and protection. By "external" dimension I mean investment promotion and protection inside the EU for investors based outside the EU, and vice versa. The EC

³⁹ T.W. Wälde, and K. Hobér, *The First Energy Charter Treaty Award*, *Transnational Dispute Management*, Vol. 1, Issue 4 (October 2004), page 3.

⁴⁰ See the preamble of Council and Commission Decision 98/181/EC of 23 September 1997 on the conclusion, by the European Communities, of the Energy Charter Treaty and the Energy Charter Protocol on energy efficiency and related environmental aspects, *Official Journal of the EC* (1998) L 69, at 1.

Treaty has some impact on such investment by virtue of the provisions on free movement of capital. Under Article 56(1) “*all restrictions on the movement of capital between Member States and between Member States and third countries shall be prohibited.*” In terms of legislative competence, Article 57(2) provides that “*the Council may ... adopt measures on the movement of capital to or from third countries involving direct investment – including investment in real estate – establishment, the provision of financial services or the admission of securities to capital markets*”. So far, the Council has not made use of those powers for the purpose of adopting EC legislation.⁴¹ There is little doubt that an international agreement could be concluded pursuant to Article 57(2). The Council and the Commission indeed based their Decision to conclude the ECT on Article 57(2). However, it is equally obvious that these powers do not cover all aspects of investment promotion and protection. That is clearly also the opinion of the Member States as drafters of the EU’s founding treaties: the Treaty of Lisbon, designed to amend the EC and EU Treaties, specifically extends the EC’s competences under the common commercial policy to “foreign direct investment”. Such express extension of the EC’s powers would of course not be required if foreign direct investment were already part of the EC’s powers.⁴² The Treaty of Lisbon is not yet in force and whether it ever will be is uncertain after the referendum in Ireland.

60. The “internal” dimension of investment promotion and protection – in other words investment between Member States – is of course to some extent covered by EC internal market law. The right of establishment and the free movement of capital apply to such investment. There is legislative competence for the EC to adopt measures to facilitate free movement, under, for example, Articles 44, 47, and 95 EC. However, none of those provisions provide for an exclusive EC competence.⁴³ In other words, powers are shared with the Member States. Applied to the ECT, this means that the Member States had the power, at the time of the conclusion of the ECT, to enter into mutual

⁴¹ ECJ, Case C-205/06 *Commission v Austria* and Case C-249/06 *Commission v Sweden*, para. 3 of the Opinion of Advocate General Maduro.

⁴² See also C. Tietje, *The Applicability of the Energy Charter Treaty in ICSID Arbitration of EU Nationals vs. EU Member States*, 78 *Beiträge zum Internationalen Wirtschaftsrecht* (2008), at page 14, produced as **Exhibit PE-10**.

⁴³ This is confirmed by the Treaty of Lisbon, see Article 4(2) of the Treaty on the Functioning of the Union.

obligations between them as regards investment promotion and protection.⁴⁴ For the purposes of this case, this means that Hungary and the United Kingdom had full authority to enter into the ECT and to undertake the obligations set out therein with respect to the protection of investors from the State of the other party.

61. It must furthermore be noted that EC internal market law does not provide for the type of investor protection embodied in the ECT. This is first of all the case from a procedural perspective. EC law does not make provision for the kind of direct international arbitration proceedings for which the ECT provides, and which were instituted in this case. It is possible for a private investor to claim damages from a Member State for breach of internal market rules, for example on free movement of capital or freedom of establishment. However, such claims need to be brought before the ordinary courts of the Member State in question. Moreover, they will only be successful where the investor can prove a “*sufficiently serious*” breach of the relevant EC rules.⁴⁵ This condition constitutes a high threshold, not easily met. The Member State must have engaged in wrongful behaviour which does not merely constitute a breach of EC law. There must be a substantial measure of gravity and seriousness to the breach in issue. It is clear, by contrast, that the ECT provisions on investor protection do not impose such a threshold. In other words, a Member State may be complying with EC law whilst violating its obligations under the ECT.
62. From a substantive perspective, it must be noted that EC internal market rules are particularly focused on ensuring access to the market of another Member State,⁴⁶ and much less on protecting an investment in another Member State, throughout that investment’s life. Those rules do not, for example, extend to issues of expropriation in the way the ECT does.

⁴⁴ Tietje, *supra*, page 15: “...the EU Member States conducted themselves and continue to conduct themselves with complete state sovereignty with regard to the ratification of ECT Part III and V [Investment Promotion and Protection and Dispute Settlement respectively]. On these grounds alone, there is no possibility for an exclusion of the applicability of Part III and V ECT in the inter se relationship of EU Member States.”

⁴⁵ ECJ, Joined Cases C-46/93 and 48/93 *Brasserie du Pêcheur and Factortame* [1996] ECR I-1029.

⁴⁶ See e.g. C. Barnard, *The Substantive Law of the EU* (2nd ed., Oxford University Press 2007) page 19.

63. The conclusion as regards competence is that the EC Member States had the power under EC law, at the time of the conclusion of the ECT, to enter into obligations regarding investment promotion and protection, such as those for which the ECT provides. However, it bears repeating that this is an issue which the Tribunal need not decide.⁴⁷ It is a question of internal EC law which has no relevance in these proceedings. As the EC and its Member States did not carve up the ECT or make a declaration of competences, they may each incur international responsibility for breach of any of its provisions.

(e) Conclusion

64. The conclusion is that both the EC and its Member States are bound, under international law, by all the provisions of the ECT. They may each incur international responsibility for breach of their obligations. The "internal" division of competences between the EC and its Member States cannot be relied upon to deny responsibility. The EC Member States entered into obligations *inter se* regarding investor protection when they concluded the ECT. Hungary's accession to the EU therefore in no sense modified its obligations under the ECT.

5.2 Conflict resolution rules within the ECT

65. Notwithstanding the clear conclusion that no conflict exists between the ECT and EC law as (i) the ECT prevails as a matter of international law, and (ii) EC law expressly respects that to be the case, I have been asked to examine how a potential conflict between the ECT and EC law would be approached. There are two perspectives to that issue. One is the public international law perspective, the other the EC law perspective. As international law and EC law constitute different and distinct legal orders,⁴⁸ they could in theory deal with such a conflict in different ways. However,

⁴⁷ See also ECJ, Ruling 1/78 re Convention on the Physical Protection of Nuclear Materials, Facilities and Transports [1978] ECR 2151, para. 35: "It is further important to state ... that it is not necessary to set out and determine, as regards other parties to the convention, the division of powers in this respect between the Community and the Member States, particularly as it may change in the course of time. It is sufficient to state to the other contracting parties that the matter gives rise to a division of powers within the Community, it being understood that the exact nature of that division is a domestic question in which third parties have no need to intervene."

⁴⁸ ECJ, Joined Cases C-402/05 P and C-415/05 P *Kadi and Al Barakat v Council and Commission*, judgment of 3 September 2008, not yet reported, paras. 285 and 288.

as will be shown, that is not the case. EC law fundamentally respects international law, and therefore provides for instruments to avoid conflicts with it. In what follows, I examine the position under international law. Section 5.3 turns to the relevant EC law rules and principles.

(a) No disconnection clause

66. It must be noted that mixed agreements such as the ECT often contain a so-called “disconnection clause”. Such a clause aims to ensure that the agreement does not apply in an intra-EC context, where it could conflict with EC law. By introducing a disconnection clause in a mixed agreement, the EC and its Member States effectively declare that, in the relations between Member States and in “internal” EC matters, the agreement does not apply. It is now a widespread practice of the EC, in existence for over 20 years, to include such disconnection clauses in mixed agreements.⁴⁹

67. As the ECT does not contain such a disconnection clause, its provisions bind the EC Member States, including in their *inter se* relations.⁵⁰ That is particularly the case for the ECT’s provisions on investment promotion and protection, at issue in this case. There is no indication whatsoever in the ECT that those provisions do not apply in an intra-EC context, where an investor from one Member State seeks the protection of his investment in another Member State.

68. Absent such a disconnection clause, the ECT protects cross-border, intra-EC investments in exactly the same way that it protects an investment by an investor of a third country made in a Member State. This effect must be taken to have been intended by the EC and its Member States, when one considers that disconnection clauses are a long used instrument of the EC and yet none was used here.

(b) Applicable law

⁴⁹ See further M. Smrkolj, *The Use of the “Disconnection Clause” in International Treaties: What does it tell us about the EC/EU as an Actor in the Sphere of Public International Law*, SSRN Paper, see <<http://ssrn.com/abstract=1133002>>. An example of such a clause, discussed in the ECJ’s case-law, can be found in the Lugano Convention, a convention which aims to extend the EC’s regime of jurisdiction and recognition of judgments to the EFTA countries, see Opinion 1/03, *supra*, para. 130.

⁵⁰ Tietje, *supra*, pages. 9 to 11.

69. As analysed above,⁵¹ the law to be applied to this dispute is that of the ECT and principles of international law. This results from the express choice of law clause in the ECT, which operates to exclude EC law. Pursuant to Article 26(6) ECT the Tribunal “*shall decide the issues in dispute in accordance with this Treaty and applicable rules and principles of international law*”. This provision defines the applicable law before the Tribunal. That law consists of the ECT and applicable rules and principles of international law. It does not include EC law.⁵²
70. In its Counter-Memorial Hungary does not argue that there is a genuine conflict between the ECT and EC law. Nor does it argue that, if there were a conflict, it would need to be resolved, by the Tribunal, in favour of EC law. Hungary only makes a passing reference, in a footnote,⁵³ to Article 30 VCLT which deals with successive treaties. Hungary’s argument is that the ECT should be interpreted in the light of EC law, and that therefore no conflict arises.
71. Under international law, there is a presumption against conflict,⁵⁴ and Hungary therefore has the burden of showing that there is such a conflict, and that it would need to be resolved in favour of one or the other norm (in this case in favour of EC law). As mentioned Hungary does not make that argument, and indeed it seems very clear that the Tribunal can only apply the ECT, not EC law, and that the ECT prevails over EC law in the context of this arbitration.

(c) Conflicts to be resolved in favour of the Investor

72. It is true that treaty law provides for some rules on conflicts. The starting point is that the parties to treaties may themselves regulate potential conflicts, by inserting so-called conflict clauses.⁵⁵ That is precisely what happened in the case of the ECT: it regulates its relationship with both earlier and later treaties, at least insofar as investment promotion and protection, and dispute resolution are

⁵¹ Section 3 of this Report.

⁵² Tietje, *supra*, page 7.

⁵³ Counter-Memorial, footnote 532.

⁵⁴ J. Pauwelyn, *Conflict of Norms in Public International Law* (Cambridge University Press 2003), page 240, produced as Exhibit PE-11.

⁵⁵ Pauwelyn, *supra*, page 328.

concerned, which are the provisions of the ECT relevant to this dispute. It may be worth quoting the relevant provision of the ECT in full:

“ARTICLE 16
RELATION TO OTHER AGREEMENTS

Where two or more Contracting Parties have entered into a prior international agreement, or enter into a subsequent international agreement, whose terms in either case concern the subject matter of Part III or V of this Treaty,

(1) nothing in Part III or V of this Treaty shall be construed to derogate from any provision of such terms of the other agreement or from any right to dispute resolution with respect thereto under that agreement; and

(2) nothing in such terms of the other agreement shall be construed to derogate from any provision of Part III or V of this Treaty or from any right to dispute resolution with respect thereto under this Treaty,

where any such provision is more favourable to the Investor or Investment.”

73. Part III ECT concerns Investment Promotion and Protection; Part V concerns Dispute Settlement.
74. The clear effect of this provision is as follows. Article 16 gives precedence to any provisions, in either the ECT or in an earlier or later agreement between the Contracting Parties, which are more favourable to the Investor or the Investment. If the Tribunal were to decide that Hungary has breached the ECT provisions on investment promotion and protection, that would clearly be more favourable to the Claimants than any provisions of the the EC Treaty which Hungary may rely upon to justify its actions. In other words, in the circumstances of this case the only applicable legal principles are those of the ECT, which takes precedence over the EC Treaty.⁵⁶
75. In terms of treaty law, Hungary refers in a footnote to Article 30 VCLT, on successive treaties.⁵⁷ That provision embodies the *lex posterior* principle. However, this rule of customary international law does not apply, because there is an express conflict clause. The parties to the ECT have “contracted out” of the *lex posterior* principle by providing that the ECT provisions on investment

⁵⁶ Tietje, *supra*, at pages 11 to 12.

promotion and protection prevail over later treaties, where they are more favourable to the Investor or the Investment. Furthermore, even if Article 30 were considered to apply, it would not yield a clear result. This is for the simple reason that it is unclear which treaty is earlier and which later: for the United Kingdom (the State from which the investment was made) the EC Treaty is the earlier treaty, for Hungary it is the ECT.

76. It must again be noted that nothing in the terms of Hungary's accession to the EU suggests that such accession constitutes an *inter se* modification, between the old and new EU Member States, of the provisions of the ECT. At the occasion of that accession, the Member States have not attempted to modify the effect of the ECT between them.⁵⁸

77. It is a principle of international law that parties to an international agreement should avoid conflicts of norms through interpretation, as much as possible.⁵⁹ That principle also binds the EC institutions. In the present case, which is governed by the express conflict clause of Article 16 ECT, it is therefore for the EC and Hungary to avoid a conflict with the ECT by applying EC law in the light of Hungary's investment protection obligations under the ECT. The European Commission, in particular, clearly had room for manoeuvre in the circumstances of this case. One would have expected the aid (if aid there is) to be characterized as "existing" rather than "new" aid. Indeed, Hungary notified the aid to MVM as existing aid under the interim procedures provided for by the Accession Treaty, but it was apparently the Commission which insisted that that notification be withdrawn, and Hungary agreed to this.⁶⁰ This action on the part of Hungary had the effect of subjecting the aid to the disciplines on new aid. Existing aid cannot be made the subject of a recovery decision. If the Commission had completed the notification of the aid to MVM, it would have been required to grant the existing aid label and it could simply have kept the aid under review,

⁵⁷ Counter-Memorial, footnote 532.

⁵⁸ Act concerning the conditions of accession of the Czech Republic, the Republic of Estonia, the Republic of Cyprus, the Republic of Latvia, the Republic of Lithuania, the Republic of Hungary, the Republic of Malta, the Republic of Poland, the Republic of Slovenia and the Slovak Republic and the adjustments to the Treaties on which the European Union is founded, (2003) EU Official Journal L 236, page 33.

⁵⁹ Pauwelyn, *supra*, page 244.

⁶⁰ Exhibit R-76: Letter from the Ministry of Finance to AES-Tisza dated 25 April 2005.

effectively allowing the PPAs to be honoured until their expiry. Such an application of EC State aid law would have shown much greater respect for the Claimants' rights under the ECT. As things stand, it would appear that the Commission completely disregarded the ECT, notwithstanding the fact that the EC is bound by its provisions.

(d) No specific exception made in relation to EC law

78. As shown above, the ECT contains its own conflict clause, which confirms that its provisions on investment protection prevail over other agreements, when those provisions are more favourable to the Investor or the Investment. The ECT therefore does not instruct the Tribunal to lessen, in any way, the scope or effects of its investment protection provisions, with a view to avoiding conflict with another agreement, such as the EC Treaty. Any potential conflict must be resolved in favour of the ECT.

79. This is further corroborated by the fact that the ECT Contracting Parties have provided for a conflict rule, in relation to another treaty, i.e. the treaty concerning Spitsbergen of 1920 (the Svalbard Treaty). Decision 1 with Respect to the ECT (Annex 2 to the Final Act of the European Energy Charter Conference) provides that "*in the event of a conflict between the treaty concerning Spitsbergen ... and the ECT, the treaty of Spitsbergen shall prevail to the extent of the conflict...*". No such provision exists regarding conflicts between the ECT and the EC Treaty.

(e) Conclusion

80. The conclusion is that, if there were a conflict between the ECT and EC law, it would in any event need to be resolved in favour of the ECT. In other words, the Tribunal must simply apply the provisions of the ECT, and must disregard any potential conflict with EC law.

5.3 Conflict resolution rules in EC law

81. It must again be emphasized that EC law is irrelevant for the interpretation of the ECT. The ECT must be read on its own purely under international law. However, in light of Hungary's argument

cautioning against an interpretation of the ECT which may produce a conflict with EC law, it may simply be helpful to inform the Tribunal about the relevant EC law rules and principles – which expressly confirm respect for international law and contain mechanisms to avoid or resolve conflict.

82. The main conclusions one reaches when applying the general rules and principles, outlined below, are:

- The EC institutions are bound by the ECT, which has primacy over EC acts;
- The ECT would most likely be recognized as having direct effect in EC law, as it confers rights on private parties;
- Such parties can invoke the ECT before the EU courts in actions challenging the legality of an EC act; and
- An award by an Arbitral Tribunal under the ECT provides an authoritative interpretation of the obligations of the Contracting Parties, binding on the EU courts.

(a) Primacy of international law over EC law

83. The ECJ consistently emphasizes that the EC must respect international law in the exercise of its powers.⁶¹ In *Poulsen and Diva Navigation* the ECJ held that a measure adopted by virtue of those powers “*must be interpreted, and its scope limited, in the light of the relevant rules of international law*”.⁶² These principles were recently recalled in the very significant judgment in *Kadi and Al-Barakaat v Council*, on counter-terrorism listings emanating from the UN Security Council.⁶³

84. Article 300(7) EC provides that international agreements concluded by the EC “*shall be binding on the institutions of the Community and on Member States*”. The ECT is of course such an agreement.

⁶¹ E.g. ECJ, Case C-286/90 *Poulsen and Diva Navigation* [1992] ECR I-6019, para. 9; ECJ, Case C-162/96 *Racke v Hauptzollamt Mainz* [1998] ECR I-3655, para. 45.

⁶² *Poulsen and Diva Navigation*, para. 9.

⁶³ *Kadi, supra*, para. 291.

In *Haegeman v Belgium* the ECJ stated that the provisions of a treaty, “*from the coming into force thereof, form an integral part of Community law*”.⁶⁴

85. It is therefore clear under EC law that the EC institutions are bound by the provisions of an international treaty concluded by the EC, and that all acts of those institutions should comply with such treaties.
86. A private party can rely on a treaty concluded by the EC when challenging an EC act before a Community or domestic court, provided the treaty has so-called “direct effect”.⁶⁵ Most international treaties or agreements concluded by the EC have been recognised to produce such direct effect. In a very recent judgment, *Intertanko and Others v Secretary of State*, the ECJ emphasized that direct effect depends on whether the treaty establishes “*rules intended to apply directly and immediately to individuals and to confer upon them rights or freedoms capable of being relied upon against States*”.⁶⁶
87. It is of course clear that this approach would be directly relevant for the ECT, if it were being examined under EC law, for it cannot be denied that its provisions, in particular those concerning investment promotion and protection, *do* apply directly and immediately to individuals and confer upon them rights capable of being relied upon against States. In other words, although the ECJ has not yet had the opportunity to address the question whether the ECT has direct effect, the conclusion that it does, appears indisputable.⁶⁷ This means that private parties are capable of challenging the validity or legality of EC acts on the basis of a breach of the ECT, either before a court of a Member State, or in a direct action before the EU Courts. It would thus be open to the Claimant in this case

⁶⁴ ECJ, Case 181/73 *Haegeman v Belgium* [1974] ECR 449, para. 5.

⁶⁵ See for an in-depth analysis P. Eeckhout, *External Relations of the European Union – Legal and Constitutional Foundations* (OUP 2004), Chapter 9, produced as Exhibit PE-12.

⁶⁶ ECJ, Case C-308/06 *Intertanko and Others v Secretary of State*, judgment of 3 June 2008, not yet reported, para. 64.

⁶⁷ Compare with T.W. Wälde, *International Investment under the 1994 Energy Charter Treaty*, in Wälde, *supra*, produced as Exhibit PE-13 who argues at page 310 that Part III of the ECT is most likely to have direct effect, and should have such effect, its provisions being hard obligations by virtue of intent, policy and formulation.

to bring an action for annulment against the European Commission's State aid decision, on the ground that the decision is in breach of the EC's obligations under the ECT.⁶⁸

88. Of course, the Tribunal is not being asked to decide whether or not the PPAs contained State aid. Rather, the question before the Tribunal is whether Hungary's amendments to its legislation and subsequent introduction of the Price Decrees breached the investor protection obligations under the ECT. An action for annulment would, at most, be complementary to the present dispute and does *not* constitute an alternative. The annulment or otherwise of the Commission's State aid decision is a different dispute from the present one. Any determination of whether the Commission's decision on State aid should be annulled as violating the obligations of the EC under the ECT, and the determination of whether Hungary's decision to enact the Price Decrees was in violation of the ECT, are entirely separate disputes.

(b) Some examples

89. It may be useful to give some examples of cases in which the EU courts were happy to review acts of the EC institutions on the ground of breach of international law, thus confirming the primacy of international law over EC law.

90. In *Opel Austria* the EU Court of First Instance (CFI) annulled an EC Council decision to impose tariffs on products imported from Austria (a non-member State at the time). The decision had been adopted just a few days prior to the entry into force of the European Economic Area (EEA) Agreement, and that agreement clearly prohibited the imposition of the tariffs. However, the CFI could not directly apply the EEA Agreement because the legality of the contested decision had to be assessed on the basis of the law as it stood at the time of its adoption – when the EEA Agreement had not yet entered into force. The CFI nevertheless found a way to uphold international law. It referred to the international law principle of good faith, according to which, pending the entry into force of an agreement, the signatories cannot adopt measures which would defeat its object and

⁶⁸ For the sake of completeness, it is clear in EC law that a company which has been granted State aid in breach of the EC Treaty can bring an action for annulment before the EU Court of First Instance against the relevant European Commission decision, see ECJ, Case 730/79

purpose. It stated that the principle was a rule of customary international law, codified in Article 18 VCLT, and binding on the EC. The CFI further stated that the principle of good faith was the corollary in international law of the principle of protection of legitimate expectations, which forms part of the EC legal order. Traders such as Opel Austria could rely on good faith and legitimate expectations, and the CFI struck down the Council decision as being in breach of those principles, combined with the provisions of the EEA Agreement.⁶⁹

91. In *Racke* the ECJ reviewed an EC Council decision to suspend a Cooperation Agreement with Yugoslavia as a reaction to the war which broke out in that country in the early 1990s. The suspension affected Racke's imports of wines. The company argued that the suspension had been adopted in breach of customary international law, the Cooperation Agreement itself not providing for suspension. The Council defended its action on the basis of the customary international law principle of a fundamental change in circumstances (*rebus sic stantibus*). In the end the ECJ accepted that defence, on the facts of the case, but what must be noted is that the ECJ established that a private party could rely on customary international law – again in combination with the provisions of an agreement concluded by the EC – to challenge the legality of an EC act.⁷⁰

(c) Respect for international judicial decisions

92. EC law and principles concerning respect for international law do not merely apply to customary international law and treaty law. The ECJ has also made statements concerning respect for international judicial decisions. In Opinion 1/91, a ruling concerning the first version of the EEA Agreement, the Court stated the following:⁷¹

“Where ... an international agreement provides for its own system of courts, including a court with jurisdiction to settle disputes between the Contracting Parties to the agreement, and, as a result, to interpret its provisions, the decisions of that court will be binding on the Community institutions, including the Court of Justice. ...

Philip Morris v Commission [1994] ECR 2671, para. 5

⁶⁹ CFI, Case T-115/94 *Opel Austria v Council* [1997] ECR II-39.

⁷⁰ *Racke*, *supra*.

⁷¹ ECJ, Opinion 1/91 re the EEA Agreement [1991] ECR I-6079, paras. 39 to 40.

An international agreement providing for such a system of courts is in principle compatible with Community law. The Community's competence in the field of international relations and its capacity to conclude international agreements necessarily entails the power to submit to the decisions of a court which is created or designated by such an agreement as regards the interpretation and application of its provisions."

93. There are no reasons why these statements should not cover the position of the Tribunal in this case, which has jurisdiction under the ECT to settle disputes between an investor and a Contracting Party. It is true that, as regards the WTO, the ECJ denies that parties can rely on decisions by the WTO Dispute Settlement Body, or on WTO Panel or Appellate Body reports.⁷² However, as the ECJ very recently clarified, this simply follows from the lack of direct effect of WTO law in general.⁷³ As was mentioned, under the criteria employed by the ECJ, the direct effect of the ECT, by contrast, appears undeniable.

94. The overall conclusion is, again, that the EC institutions are bound by the ECT's provisions and by the award of an Arbitral Tribunal pursuant to the ECT.

(d) The specific conflict resolution provision of Article 307 EC

(i) Article 307 EC permits derogations from even primary law

95. Derogations from even primary EC law, such as the rules on State aid, are permitted by Article 307 EC, where such derogations are in pursuance of obligations under international law, which the Member States are required to honour, such as the obligations under the ECT.

⁷² ECJ, Case C-377/02 *Van Parys* [2005] ECR I-1465.

⁷³ ECJ, Joined Cases C-120/06 P and C-121/06 P *FIAMM v Council*, judgment of 9 September 2008, not yet reported, paras. 128 to 129: "A DSB decision ... cannot in principle be fundamentally distinguished from the substantive rules which convey such obligations and by reference to which such a review is carried out, at least when it is a question of determining whether or not an infringement of those rules or that decision can be relied upon before the Community courts for the purpose of reviewing the legality of the conduct of the Community institutions. A recommendation or a ruling of the DSB finding that the substantive rules contained in the WTO agreements have not been complied with is, whatever the precise legal effects attaching to such a recommendation or ruling, no more capable than those rules of conferring upon individuals a right to rely thereon before the Community courts for the purpose of having the legality of the conduct of the Community institutions reviewed".

96. Article 307 EC is a crucial provision for the purpose of resolving conflicts between a Member State's obligations under EC law and its obligations under an earlier international agreement. The first and second paragraphs provide:

“The rights and obligations arising from agreements concluded before 1 January 1958 or, for acceding States, before the date of their accession, between one or more Member States on the one hand, and one or more third countries on the other, shall not be affected by the provisions of this Treaty.

To the extent that such agreements are not compatible with this Treaty, the Member State or States concerned shall take all appropriate steps to eliminate the incompatibilities established. Member States shall, where necessary, assist each other to this end and shall, where appropriate, adopt a common attitude.”

97. The ECJ has clarified that the first paragraph concerns the obligations of a Member State towards third countries – and thus, conversely, the rights of third countries – under an agreement predating the Member State's accession to the EU.⁷⁴ There is of course no doubt that Hungary concluded the ECT prior to its EU accession. The ECT is therefore a treaty which comes within the terms of Article 307 EC.

98. As in fact Advocate General Mischo observed in *Commission v Portugal*,⁷⁵ the first paragraph of Article 307 is merely declaratory of the position under general international law. *Pacta sunt servanda* is binding on the Community and its Member States. To the Advocate General's knowledge, no-one has yet seriously defended the idea that, by creating a regional international organization, States could, without recourse to any other procedure, release themselves from the obligation to fulfil earlier commitments to non-member countries.

99. The legal effects of Article 307 EC, first paragraph, were recently recalled and re-examined in *Kadi and Al Barakaat*.⁷⁶ The facts and legal issues of that case are rather specific, and have no connection with the ECT and the issues arising in the present proceedings. The case concerned UN Security

⁷⁴ ECJ, Case 10/61 *Commission v Italy* [1962] ECR I.

⁷⁵ ECJ, Joined Cases C-62/98 and C-84/98 *Commission v Portugal* [2000] ECR I-5171, paras. 56 and 57 of the Opinion of Mr Advocate General Mischo.

⁷⁶ *Kadi, supra*, paras. 301 to 304.

Council resolutions imposing financial sanctions (freezing measures) on persons suspected of supporting Al-Qaeda. Those resolutions were implemented by the EU through EC regulations freezing the assets of those persons. In challenges to the regulations the CFI had reasoned that no review on the grounds of a violation of fundamental rights was permissible, in light of the UN origins of the measures. The CFI had inter alia referred to Article 307 EC to establish this jurisdictional immunity; the UN Charter, which provides that Security Council resolutions are binding, is obviously an agreement also coming within the terms of Article 307 EC. The ECJ on appeal rejected that reasoning. As regards Article 307 it stated the following:⁷⁷

“301 Admittedly, the Court has previously recognised that Article 234 of the EC Treaty (now, after amendment, Article 307 EC) could, if the conditions for application have been satisfied, allow derogations even from primary law, for example from Article 113 of the EC Treaty on the common commercial policy (see, to that effect, *Centro-Com*, paragraphs 56 to 61).

302 It is true also that Article 297 EC implicitly permits obstacles to the operation of the common market when they are caused by measures taken by a Member State to carry out the international obligations it has accepted for the purpose of maintaining international peace and security.

303 Those provisions cannot, however, be understood to authorise any derogation from the principles of liberty, democracy and respect for human rights and fundamental freedoms enshrined in Article 6(1) EU as a foundation of the Union.

304 Article 307 EC may in no circumstances permit any challenge to the principles that form part of the very foundations of the Community legal order, one of which is the protection of fundamental rights, including the review by the Community judicature of the lawfulness of Community measures as regards their consistency with those fundamental rights.”

100. What is important, for the purposes of the present case, is paragraph 301, where the ECJ recalls and confirms that Article 307 allows derogations, even from primary law (i.e. from the EC Treaty itself). The precedent to which it refers, *Centro-Com*, was a case concerning the common commercial policy.⁷⁸ It is true that in *Kadi and Al Barakaat* the ECJ imposes limits on the scope of Article 307: it cannot be understood to authorise any derogation from the principles of liberty, democracy and respect for human rights and fundamental freedoms which are a foundation of the EU. However, it

⁷⁷ *Kadi, supra.*

⁷⁸ ECJ, Case C-124/95 *Centro-Com v HM Treasury* [1997] ECR I-81.

is equally clear that this limitation does not apply to the EC Treaty provisions on State aid. Those provisions are no more a “foundation” of the EU than the EC Treaty provisions on the common commercial policy. The EC Treaty State aid provisions are, admittedly, of vital importance for a proper functioning of the EU internal market. But so is the common commercial policy. *Kadi and Al Barakaat*, by contrast, was a highly exceptional case, in which the very foundations and core values of the EU, in terms of respect for fundamental rights, were in issue.

101. The conclusion is clearly that Article 307 EC permits derogations from the EC Treaty provisions on State aid. This means that, in so far as the ECT imposes obligations on Hungary towards ECT Contracting Parties which are not EU Member States, Article 307 EC allows Hungary to honour those obligations, irrespective of its obligations under EC State aid law.

(ii) Position of private parties

102. However, the obligations of Hungary in issue in the present case are not obligations owed to a non-Member State. They are obligations owed to a private investor. It needs to be recognized that the question whether a Member State can refer to its obligations towards a private party under an agreement coming within the scope of Article 307 EC has not yet been raised before the EU courts. In my opinion, however, that question ought to receive a positive reply. A Member State should be in a position to invoke Article 307 EC, also where the agreement in issue imposes obligations on that Member State towards a private party – particularly in circumstances such as those of the present case. There are a number of arguments in support of that opinion.

103. First, as described above, EC law fundamentally respects international law. Article 307 EC is no more than a declaratory expression of that respect. Since, as argued above, the rights of private investors under the ECT were not in any sense modified by Hungary’s accession to the EU, EC law cannot be interpreted as overriding these rights under international law.

104. Second, the International Court of Justice (ICJ) has recognized that international agreements may confer rights on a private party, which States must respect. In the *LaGrand* case the ICJ found that

certain provisions of the Vienna Convention on Consular Relations conferred rights on individuals. It based itself purely on the text of the relevant provisions (which refer expressly to the “rights” of detained persons), the clarity of which admitted of no doubt.⁷⁹ Likewise, it is indisputable that the ECT confers rights on investors under international law.

105. Third, the EC is itself a Contracting Party to the ECT and, therefore, needs to recognise and respect the ECT’s provisions on investment promotion and protection.
106. Fourth, there are statements in the ECJ’s case-law which appear to confirm that Article 307 EC also protects rights of private parties. *Attorney General v Burgoa* concerned Irish criminal proceedings against the master of Spanish fishing-vessels which had, without authority, fished within Irish fishery limits. At the time Spain was not yet a member of the EEC. In those proceedings the accused attempted to rely on the London Fisheries Convention of 1964, an agreement concluded by Ireland prior to its accession to the (then) EEC. The Irish court referred several questions to the ECJ, one of which was whether Article 234 EEC (now Article 307 EC) maintained or upheld rights of the beneficiaries of treaties to which that article applied, which national courts of the Member States had to uphold. In other words, *Burgoa* was attempting to rely directly on Article 234 EEC as a provision which confers direct effect on the agreements within its scope. It was not seeking to rely on Article 234 EEC as against any incompatible EEC act. The ECJ stated the following:⁸⁰

“Since the purpose of the first paragraph of Article 234 is to remove any obstacle to the performance of agreements previously concluded with non-member countries which the accession of a Member State to the Community may present, *it cannot have the effect of altering the nature of the rights which may flow from such agreements.* From that it follows that that provision does not have the effect of conferring upon individuals who rely upon an agreement concluded prior to the entry into force of the Treaty or, as the case may be, the accession of the Member State concerned, rights which the national courts of the Member States must uphold. *Nor does it adversely affect the rights which individuals may derive from such an agreement.*”

107. The highlighted passages suggest that the ECJ would be ready to recognize individual rights which agreements coming within the scope of Article 307 EC protect.

⁷⁹ ICJ, *LaGrand (Germany v. United States of America)*, Judgment, I. C. J. Reports 2001, page 466, para. 77.

(iii) Article 307 and intra-Community situations

108. Prof. Slot argues in his Expert Opinion that Article 307 EC does not apply in intra-Community situations.⁸¹ However, the case-law to which he refers does not speak to the kind of issues which arise in the circumstances of the present case.
109. Ever since *Commission v Italy*⁸² the ECJ has indeed held that Article 307 EC does not protect any rights and obligations between Member States, because accession to the EU modifies those rights and obligations. In *Commission v Austria*, to which Prof. Slot refers, the ECJ indeed recalled that “whilst Article 307 EC allows Member States to honour obligations owed to non-member States under international agreements preceding the Treaty, it does not authorise them to exercise rights under such agreements in intra-Community relations”.⁸³ However, the facts of that case were fundamentally different from the present case. The Commission brought proceedings against Austria because it discriminated against nationals from other Member States as regards recognition of secondary education diplomas and access to higher education in Austria. One of Austria’s defences was simply to argue that it was *entitled* to impose the relevant conditions under a Council of Europe convention. In other words, Austria was arguing that it had *rights* protected by Article 307 EC.
110. This is fundamentally different from the present case, which concerns Hungary’s *obligations* towards a private investor. The principle that a Member State may not rely on any rights conferred by an Article 307 agreement logically follows from the rationale of Article 307, which as stated above is simply to embody *pacta sunt servanda*. By concluding the EC Treaty, a Member State cannot modify obligations owed to a third country under an earlier agreement. However, a Member State may very well relinquish rights under such an agreement, for to relinquish such rights constitutes no breach of *pacta sunt servanda*. International law does not require a State to exercise

⁸⁰ ECJ, Case 812/79 *Attorney General v Burgoa* [1980] ECR 2787, para. 10 (emphasis added).

⁸¹ Slot Report, para. 180.

⁸² *Commission v Italy*, *supra*.

⁸³ ECJ, Case C-147/03 *Commission v Austria* [2005] ECR I-5969, para. 73.

its rights under a treaty. It is therefore entirely coherent for the ECJ to hold that a Member State cannot justify a violation of EC law on international law grounds where it is merely seeking to exercise rights under an earlier agreement. In the circumstances of this case, Prof. Slot is suggesting that Hungary could not rely on Article 307 to honour its *obligations* to EU investors. This would, of course, constitute a breach of *pacta sunt servada*.

(iv) Obligations under the second paragraph of Article 307 EC

111. The second paragraph of Article 307 EC requires that the Member States take all appropriate steps to eliminate any incompatibilities between an earlier agreement and EC law. It is a natural counterpart of the rule in the first paragraph. As long as a Member State is bound by the agreement, it must honour its provisions, even if incompatible with EC law. However, such incompatibility must be avoided as much as possible, so that EC law may produce its intended effect. Member States must therefore work to remove this incompatibility, for example by re-negotiating or even terminating the agreement.⁸⁴
112. From an EC law perspective, these obligations under the second paragraph are important.⁸⁵ However, they are irrelevant for the Arbitral Tribunal in this case, essentially for two reasons.
113. First, the ECT was not only concluded by Hungary, but also by the EC itself. There is no indication that the EC is seeking to take any action to amend the provisions of the ECT in the light of possible incompatibilities with EC law. On the contrary, the EC is bound by and must comply with, the ECT. Therefore, Hungary, on its own, can hardly be expected to take any such action at this stage. Mixed agreements are governed by a duty of cooperation between the EC and its Member States.⁸⁶ Important decisions affecting the life of a mixed agreement, such as re-negotiation or denunciation, require concerted action at EC level. To the best of my knowledge, no such action has been taken or even suggested.

⁸⁴ ECJ, Case C-62/98 *Commission v Portugal* [2000] ECR I-5171 and Case C-84/98 *Commission v Portugal* [2000] ECR I-5215.

⁸⁵ See e.g. Opinion Advocate General Maduro, *supra*, which deals with bilateral investment treaties.

⁸⁶ *Ruling 1/78, supra*.

114. Second, even if Hungary were considered to be under an obligation to remove a potential incompatibility between the application of the ECT and the application of EC State aid law, as long as no action has been taken, the first paragraph of Article 307 EC simply applies. In other words, for as long as there is incompatibility, the international obligation prevails over EC law.⁸⁷
115. The conclusion from the above analysis is that Article 307 EC permits Hungary to give precedence to its international law obligations under the ECT, including its obligations towards private investors, even if they are from an EU Member State. Article 307 thus reflects the position under international law: Hungary's obligations under the ECT were not modified by its accession to the EU. As long as the ECT is in force, confers the rights that it does, and is not amended or terminated, those rights need to be honoured under international law. EC law is incapable of modifying that position, and, moreover, respects it.
116. Not only does EC law confirm the primacy of international law, including treaty obligations, over acts of the EC institutions. It further allows Member States to honour their obligations pursuant to an agreement concluded prior to their accession to the EC. For Hungary, the ECT constitutes such an agreement. In the circumstances of this case, Article 307 EC resolves potential conflicts between the EC Treaty and the ECT by allowing Hungary to derogate from its obligations under the EC Treaty.

6. ENFORCEABILITY OF ECT ARBITRAL DECISIONS AND RECOVERY OF STATE AID

117. Next to the above rules and principles concerning the relationship between EC law and international law, EC law may be considered to provide still further instruments to avoid – or at least manage – a possible conflict with the ECT. Those instruments can be found in EC State aid law itself, in particular in the form of rules and principles regarding the recovery of incompatible aid. Thus, Hungary would be in a position to argue that it need not give effect to a Commission decision to recover the alleged aid.

⁸⁷ Eeckhout, *supra*, pages 338 to 339.

118. First, Article 14(1) of Regulation 659/1999, the basic regulation concerning State aid, provides that the Commission may not order recovery if this would be contrary to a general principle of EC law. One of those principles is that of the protection of legitimate expectations. It is arguable that that principle is in issue here. In that respect, reference can again be made to the *Opel Austria* case, in which the CFI combined respect for international law (the principle of good faith in treaty law) with the legitimate expectations of a company, affected by a Council decision contrary to that good faith principle.⁸⁸ Likewise, if in this case the Tribunal decides that the investor had a legitimate expectation that its investment should be protected – in other words that the PPA would be honoured – then the Commission ought not demand recovery.
119. Second, EC law recognizes that a Member State may rely on an absolute impossibility to recover an incompatible aid.⁸⁹ In other words that it was “*absolutely impossible for it [the Member State] to implement the decision properly...*”⁹⁰ Although there are as yet no examples in the case law of a Member State successfully relying on this principle, it is arguable that a Member State’s international obligations could give rise to such an absolute impossibility. Moreover, the case law also provides that “*a Member State which, in giving effect to a Commission decision on State aid, encounters unforeseen and unforeseeable difficulties, whether of a political, legal or practical kind, ... must submit those problems to the Commission for consideration, together with proposals for suitable amendments to the decision in question*”.⁹¹ This statement recognizes that there is scope for amendment of a State aid decision, including in the light of legal difficulties, which could of course include difficulties under international law.
120. There should be no question as to the enforceability of an award of the Tribunal on grounds of State aid as such would be contrary to the general principles of EC law and the recovery of the aid would be “absolutely impossible” due to the principles of international law which, as explained above, are accorded primacy over those of EC law. Moreover, the award of the Tribunal would be

⁸⁸ See Section 5.3(b) above.

⁸⁹ See lastly ECJ, Case C-441/06 *Commission v France* [2007] ECR I-8887, para. 27.

⁹⁰ ECJ, Case C-348/93 *Commission of the European Communities v Italian Republic* [1995] ECR I-00673.

⁹¹ *Commission v France*, para. 28 (emphasis added).

automatically enforceable and binding upon the parties to the Arbitration, in accordance with Article 53(1) ICSID. It will be recognized automatically by Hungary as a Contracting State to ICSID under Article 54(1).

121. Finally, it is surprising that Professor Slot does not in his report address the decision of the ECJ in *Asteris*. The ECJ expressly states that damages are of a fundamentally different legal nature from State aid. An ICSID award in favour of AES, ordering Hungary to pay compensation, would not, therefore, constitute State aid. In *Asteris* the ECJ stated that "*State aid, that is to say measures of the public authorities favouring certain undertakings or certain products, is fundamentally different in its legal nature from damages which the competent national authorities may be ordered to pay to individuals in compensation for the damage they have caused to those individuals.*"⁹² This statement related to an action in damages which had been brought before the Greek courts. There is no reason why it should not extend to an ICSID award; all the more so since such an award emanates from an international instance, not from a court of a Member State, which forms part of that Member State's authorities for the purposes of State aid law. Clearly, the EC Treaty provisions regarding State aid are not addressed to ICSID Tribunals and do not bind them. Thus, Hungary would be required to satisfy any award of this Tribunal and could not rely on the Commission's State aid decision to claim that the award is not binding upon it. As shown above, this is the position at international law and *Asteris* confirms this to be the case from an EC law perspective.

7. CONCLUSION

122. The conclusions I reach on the questions put to me are as follows:

- (1) The law applicable to this dispute consists of the ECT and relevant rules and principles of international law. It does not encompass EC law. The two avenues through which Hungary suggests EC law may become relevant to this dispute are barred and Hungary's position is untenable.

⁹² Joined cases 106 to 120/88 *Asteris AE and Others v. Hellenic Republic and European Economic Community* [1988] ECR 5515

- (2) The ECT is to be interpreted in accordance with its ordinary meaning, in the light of its context and its object and purpose. There is no room under the Vienna Convention to interpret a treaty by reference to the intentions of a single contracting party. Thus there is no scope for interpreting the ECT in the light of EC law generally, or EC competition law in particular, no matter how the EC alone views the ECT.
- (3) EC law is irrelevant for the Tribunal's legal analysis, as is the internal division of competences between the EC and Member States, since both are bound under international law to apply the ECT and its provisions for investor protection and promotion.
- (4) There is no circularity problem should the Tribunal decide in AES's favour. EC law itself confirms the primacy of international law rules and, moreover, the ECT's conflict resolution rules resolve any potential conflict between its provisions and those of other international agreements in favour of those provisions that are more favourable to the Investor. The more favourable provisions are clearly those of the ECT. An award of this Tribunal would be fully enforceable, and EC law would not constitute an obstacle to its enforceability.



Professor Piet Eeckhout

30 October 2008

APPENDIX 1

EXHIBITS

Tab number	Exhibit	Exhibit number
2	The editor's preface to <i>The Energy Charter Treaty - An East-West Gateway for Investment and Trade</i> , ed. Thomas W. Wälde	PE-1
3	J Dore, <i>Negotiating the Energy Charter Treaty</i> , in <i>The Energy Charter Treaty - An East-West Gateway for Investment and Trade</i> , ed. Thomas W. Wälde	PE-2
4	H.J. Schroth, <i>The Energy Charter Treaty in the Context of the Treaties of the European Union</i> , in <i>The Energy Charter Treaty - An East-West Gateway for Investment and Trade</i> , ed. Thomas W. Wälde	PE-3
5	C.S. Bamberger, <i>An Overview of the Energy Charter Treaty</i> , in <i>The Energy Charter Treaty - An East-West Gateway for Investment and Trade</i> , ed. Thomas W. Wälde	PE-4
6	K. Holmes, <i>Legal Implications of the Energy Charter Treaty Competition Rules and Liberalization</i> , in <i>The Energy Charter Treaty - An East-West Gateway for Investment and Trade</i> , ed. Thomas W. Wälde	PE-5
7	P. Eeckhout, <i>The EU and its Member States in the WTO – Issues of Responsibility</i> , in <i>Regional Trade Agreements and the WTO Legal System</i> , eds. L. Bartels and F Ortino (2006 Oxford University Press)	PE-6
8	E. Stein, <i>External Relations of the European Community; Structure and Process</i> , in <i>Collected Courses of the Academy of European Law</i> , Vol. 1, Book 1	PE-7
9	G. Gaja, <i>The European Community's Rights and Obligations under Mixed Agreements</i> , in <i>Mixed Agreements</i> , eds. D. O'Keefe and H.G. Schermers	PE-8
10	C. Tomuschat, <i>Liability for Mixed Agreements</i> , in <i>Mixed Agreements</i> , eds. D. O'Keefe and H.G. Schermers	PE-9
11	C. Tietje, <i>The Applicability of the Energy Charter Treaty in ICSID Arbitration of EU Nationals vs. EU Member States</i> , 78 <i>Beiträge zum Internationalen Wirtschaftsrecht</i> (2008)	PE-10
12	J. Pauwelyn, <i>Conflict of Norms in Public International Law</i> , pages 237 to 249, and 327 to 331	PE-11
13	P. Eeckhout, <i>External Relations of the European Union: Legal and Constitutional Foundations</i> , (2004, Oxford University Press), Chapter	PE-12

T.W. Wälde, *International Investment under the 1994 Energy Charter Treaty*, in *The Energy Charter Treaty - An East-West Gateway for Investment and Trade*, ed. Thomas W. Wälde

APPENDIX 2

CURRICULUM VITAE

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Studies

1980-1985, at the University of Ghent, law degree («licentiaat rechten»), *magna cum laude*

1985-1986, at the University of Ghent, European law degree («licentiaat Europees recht», a master's degree), *magna cum laude*

1993, University of Ghent, PhD, dissertation on «The External Dimension of Completing the European Community's Internal Market in Services and Goods - A Legal Analysis», *summa cum laude*

Professional Career

1986 - 1990: university assistant of Prof. Dr. Marc Maresceau, European Institute, University of Ghent

1990 - 1993: research fellow with Prof. Maresceau in the framework of a research project, funded by the Belgian Fund for Joint Basic Research (FKFO), concerning the legal framework of trade relations between the European Community and Eastern Europe

1993 - 1998: Professor in EC law at the University of Ghent

1994 - 1998: legal secretary of Advocate General Francis G. Jacobs, European Court of Justice
Significant cases worked on:

- Case C-7/93 *Beune* [1994] ECR I-4471 (sex equality)
- Opinion 1/94 *re Agreement establishing World Trade Organisation* [1994] ECR I-5267
- Case C-284/94 *Spain v Council* [1995] ECR I-1985 (IP legislation)
- Case C-70/94 *Fritz Werner v Germany* [1995] ECR I-3189 (export controls)
- Case C-83/94 *Peter Leifer* [1995] ECR I-3231 (export controls)
- Case C-25/94 *Commission v Council* [1996] ECR I-1469 (membership FAO)
- Opinion 2/94 *re Accession to the ECHR* [1996] ECR I-1759
- Case C-84/95 *Bosphorus Hava Yollari* [1996] ECR I-3953 (economic sanctions)
- Case C-124/95 *Centro-Com* [1997] ECR I-81 (economic sanctions)
- Case C-177/95 *Ebony Maritime* [1997] ECR I-1111 (economic sanctions)
- Case C-338/95 *Wiener* [1997] ECR I-6495 (preliminary rulings)
- Case C-162/96 *Racke* [1998] ECR I-3655 (customary international law)
- Case C-274/96 *Bickel and Franz* [1998] ECR I-7637 (citizenship and non-discrimination)

CURRENT POSITIONS

Professor of European Law and Director, Centre of European Law, King's College London, teaching several courses on EU law and international economic law at undergraduate and postgraduate level (since 1998)

Visiting Professor, College of Europe, Bruges, course on "WTO Law: Substantive and Institutional Aspects" (since 1999)

Associate academic member, Matrix Chambers, London (since 2004)

Joint editor with Professor Takis Tridimas, *Yearbook of European Law*, Oxford University Press (since 1998)

Member of the Editorial Board, *Journal of International Economic Law*, *European Business Law Review*, *Legal Issues of Economic Integration*, *European Foreign Affairs Review*

Publications

Books

The European Internal Market and International Trade: A Legal Analysis, Oxford European Community Law Series (general ed. F.G. Jacobs), Oxford, Clarendon Press, 1994, XXXV + 399 p.

18 *Yearbook of European Law* (1998), editor with Takis Tridimas, Oxford University Press

19 *Yearbook of European Law* (1999-2000), editor with Takis Tridimas, Oxford University Press

20 *Yearbook of European Law* (2001), editor with Takis Tridimas, Oxford University Press

21 *Yearbook of European Law* (2002), editor with Takis Tridimas, Oxford University Press

22 *Yearbook of European Law* (2003), editor with Takis Tridimas, Oxford University Press

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Academic Awards

Classified *ex aequo* with award winner for PhD on the external dimension of the internal market, Wolters Kluwer Award 1993

Henri Rolin award 1994 for PhD

Languages

Dutch, native language
English and French, fluent
German, intermediate