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COMMENT ON IOAN MICULA AND OTHERS V. ROMANIA (ICSID CASE NO. ARB/05/20)

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1. Introduction

On 11.12.2013, the Arbitral Tribunal in the case of *Ioan Micula, Viorel Micula, S.C. Eropean Food S.A., S.C. Starmill S.R.L. and S.C. Multipack S.R.L v. Romania*[1] rendered an Award holding that Romania had violated Article 2(3) of the Bilateral Investment Treaty between Sweden and Romania by failing to ensure fair and equitable treatment. Consequently, the claimants were entitled to damages of approximately 85 million Euro plus compound interest on a quarterly basis. The Tribunal dismissed the claimant's allegations that Romania had violated Article 2(4) of the treaty by failing to observe obligations entered into with the claimants.[2] In light of this decision, the Tribunal found that it did not need to determine

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[1] Ioan Micula, Viorel Micula, S.C. European Food S.A., S.C. Starmill S.R.L. and S.C. Multipack S.R.L v. Romania, Award, 11.12.2013, www.italaw.com.

[2] Certain decisions of the Tribunal were reached by the majority. This refers to: the finding that Romania breached Article 2(3) (Laurent Lévy and Stanimir A. Alexandrov with a dissent of Georges Abi-Saab), the dismissal of the Claimants' claim under Article 2(4) (Laurent Lévy and Georges Abi-Saab), awarding lost profits as damages (Laurent Lévy and Stanimir A. Alexandrov). For the ease of reading this article, all decisions of

whether or not Romania had breached other provisions of the treaty (i.e. the obligation not to undertake unreasonable or discriminatory measures or the undertaking to avoid expropriation).

The 370 pages award is instructive for its thorough analyses of the umbrella clause and the fair and equitable standard. It also provides a detailed study on the impact of the European Union accession process and how European Union legislation might affect a state's obligations arising from bilateral investment treaties.

The dispute was brought by Ioan Micula, Viorel Micula, S.C. Eropean Food S.A., S.C. Starmill S.R.L. and S.C. Multipack S.R.L (**"***Claimants***"**, "*Investors*") against Romania ("*Respondent*") on 2.8.20015 under the Agreement between the Government of the Kingdom of Sweden and the Government of Romania on the Promotion and Reciprocal Protection of Investments which entered into force on 1.4.2003 ("*BIT*", "*Treaty*"). The Tribunal was constituted in September 2006 with three members: Professor Dr. Stanimir A. Alexandrov (United States), Professor Georges Abi-Saab (who was appointed by the Respondent to fill in the vacancy left by Dr. Claus-Dieter Ehlermann) and Dr. Laurent Lévy, who was the presiding arbitrator. The proceedings were conducted under the Convention on the Settlement of Investment Disputes between States and Nationals of Other States of 1966 (**"ICSID Convention"**).

The dispute arose out of Romania's introduction and subsequent revocation of economic incentives to develop disadvantaged regions of Romania. The Claimants claimed that, in reliance on certain incentives and assuming that these incentives would be maintained for a period of 10 years, they made substantial investments in Romania. The Claimants further claimed that Romania's premature revocation of such incentives constituted a breach of its obligations under the BIT.

The second part of this article sets forth the factual background of the dispute, followed by the parties' position in the third part. The forth part provides an analysis of the Tribunal's findings on the merits of the claim and the last part contains conclusions.

the Tribunal will be referred to as the decisions of the Tribunal, not its majority (unless otherwise explicitly stipulated).

2. Factual Background of the Dispute

2.1. Incentives

In 1998, Romania passed the Emergency Government Ordinance 24/1998 (**"1998 Ordinance"**) pursuant to which it made available tax and customs duty incentives to investors in certain underdeveloped regions who met the requirements set forth in the 1998 Ordinance and its implementing legislation.[3] The 1998 Ordinance established the legal framework for the granting of incentives. It provided that the Government of Romania could declare certain regions as being underdeveloped by means of a government decision, which would also define: (i) the period (at least 3 years but not exceeding 10 years) for which the region would be categorized as underdeveloped, (ii) the categories of investments which would be incentivized and (iii) the type of incentives offered. It also included specific requirements for investors to qualify for the incentives and set out investors' obligations to remain in the underdeveloped area for twice the period for which they benefitted from the incentives. Finally, the 1998 Ordinance required the Government to approve, by way of a decision, the methodological standards to be used for implementation of the incentives.

By means of Government Decision 194/1999 ("*194/1999 Decision*"), Romania designated certain areas (including the region in which the Claimants invested) as underdeveloped for a period of 10 years commencing on 1.4.1999. Furthermore, the Government issued Decision 525/1999 ("*525/1999 Decision*") which set out the methodological norms for the application of the 1998 Ordinance. *Inter alia*, it provided that investors which were granted permanent investor certificates by the Regional Development Agency (upon their application) would be entitled to benefit from the incentives. During the period 2000–2002, S.C. European Food S.A., S.C. Starmill S.R.L. and S.C. Multipack S.R.L

[3] As the factual background of the case is complex and detailed, the summary presented in this section includes only those facts which are relevant from the point of view of the analyses made in this article.

("Corporate Claimants", "*Corporate Investors*") received the permanent investor certificates ("*Certificates*") envisaged by the 525/1999 Decision. All three permits were valid until 1.4.2009.

The Corporate Claimants allege that, following Romania's introduction of the incentives program, they constructed a food processing facilities in reliance on these incentives.

2.2. Romania's Accession to the EU

One of the key areas of dispute between the parties concerned the alignment of Romania's state aid laws with the *acquis communautaire* prior to its accession to the EU. Given this, it is necessary to outline certain basic facts concerning the accession process.

On 1.2.1993, Romania and the European Community (predecessor of EU) signed the Europe Agreement which entered into force on 1.2.1995 ("*Europe Agreement*"). The Europe Agreement provided the legal framework for Romania's accession to EU. Notably, it stipulated that Romania would be required to harmonize its existing and future legislation with that of the EU. On 22.6.1995, Romania filed its application for EU membership. In the period between 1995 and 2000, several documents and statements were published by the European Community/EU which underlined the importance of the approximation of laws in the associated countries to those applicable in the EU. It noted further that Romania had not met these requirements. In the context of the above facts, on 15.5.2000 the Romanian Competition Council issued a decision in which it determined that certain facilities provided for under the 1998 Ordinance distorted competition and required elimination (the "*2000 Decision*"). On 16.6.2000, Romania amended the 1998 Ordinance, but to a lesser degree than had been recommended by the Competition Council. Consequently, the Competition Council sought to enforce the 2000 Decision before the Romanian courts, but its action was dismissed by the courts of first and second instance on admissibility grounds (they found that the Competition Council lacked the authority to request that the incentives be abolished).

On 1.8.2000, Romania presented a Position Paper on Competition Policy (which included state aid) in which it accepted the entire *acquis communautaire* in force as of 31.12.1999 and did not request transition periods or derogations and declared that it would be able to entirely implement it upon accession. However, Romania added that it was necessary to grant state aid to sensitive sectors of the economy and deprived areas given the difficulties confronting the Romanian economy during the transition to a market economy.

Over 2001 and 2002, several documents were presented by Romania to the European Commission with a detailed description of the existing state aid schemes, including the 1998 Ordinance. The EU's position during that period (made clear in several documents) was that incompatible fiscal aid schemes continued to exist in Romania which required alignment with the *acquis*. Contrary to these statements, on 7.11.2001 Romania passed a law amending the 1998 Ordinance by reinstating certain incentives. In June 2002, Romania issued a report in which it stated that state aid (including state aid granted pursuant to the 1998 Ordinance) must be converted into compatible state aid and the government commenced talks with the beneficiary associations in order to identify possible solutions. In the second half of 2002 (i.e. 1.6.202, 1.7.2002 and 19.11.2002) Romania introduced amendments to the 1998 Ordinance which resulted in significant limitations being placed on the incentives.

In April and May 2003, the EU issued documents requesting that Romania either end the incompatible state aid measures or align them with the *acquis*. Contrary to such requests, on 23.12.2003 a new law was passed, reinstating certain incentives under the 1998 Ordinance. However, on 7.6.2004 Romania subjected all state aid (including the 1998 Ordinance) to a maximum intensity requirement. Finally, on 31.8.2004 it decided to revoke the 1998 Ordinance with effect from 22.2.2005 (with the exception of one incentive concerning profit tax) ("*2004 Ordinance*").

On 25.4.2005, the EU's Member States and Romania (and Bulgaria) signed the Accession Treaty ("*Accession Treaty*"). It entered into force on 1.1.2007 and Romania became a Member State of the EU.

3. Parties' Position

The Claimants allege that:

1. Romania entered into binding commitments in the 1998 Ordinance and its implementing legislation (194/1999 Decision and 525/1999

Decision) as well as through the issuance of the Certificates to the Corporate Investors;

2. such binding commitments concerned Corporate Investors' rights to receive the incentives provided for in the 1998 Ordinance until 1.4.2009;
3. the Certificates certify that Corporate Investors have the right to receive incentives until 1.4.2009;
4. in reliance on these commitments, in particular on the expectation (created by Romania) that the incentives would last until 1.4.2009, the Claimants invested in one of the underdeveloped regions of Romania; and
5. early revocation of the incentives by Romania (with effect from 22.2.2005, i.e. approximately 4 years before they envisaged to expire) resulted in Romania's breach of its binding commitments.

In view of the above, the Claimants claimed that the premature revocation of the 1999 Ordinance:

1. breached Romania's binding commitment, and therefore violated the umbrella clause (Article 2(4)); [4]
2. undermined the Claimant's legitimate expectations, upset the stability of the regulatory regime, lacked transparency and consistency, and was taken in bad faith, and therefore breached the obligation to act fairly and equitably (Article 2(3));[5]
3. impaired by unreasonable measures the management, maintenance, use, enjoyment and disposal of the Claimants' investment (second part of Article 2(3));[6] and
4. expropriated without compensation the Claimants' right to receive the incentives and substantially deprived their investment of value,

[4] Article 2(4) of the BIT: „Each Contracting Party shall observe any obligation it has entered into with an investor of the other Contracting Party with regard to his or her investment."

[5] Article 2(3) of the BIT: "Each Contracting Party shall at all times ensure fair and equitable treatment of the investments by investors of the other Contracting Party (…)."

[6] Investor's claims that Romania breached its obligation not to impair the management, maintenance, use, enjoyment and disposal of the investment (second part of Article 2(3)) will not be further analyzed in this article as the Tribunal decided that it did not need to address it in the light of the Tribunal's earlier finding that Romania breached its obligation to treat Claimants' investments in a fair and equitable manner.

and therefore violated the obligation not to expropriate (Article 4(1)).[7]

The Claimants refuted the suggestion that termination of the incentives was required by EU law.

The Respondent's fundamental argument was that each state is entitled to exercise its sovereign powers to regulate and advance public welfare in a general, non-discriminatory way and that such conduct does not breach the provisions of an investment protection treaty. Absent a clear promise to stabilize a regulatory framework, states are free to amend their laws as they see fit.

On the basis of the above, the Respondent argued that:

1. Romania did not make a binding commitment that the incentives under the 1998 Ordinance would remain unchanged until 2009;
2. irrespective of whether such a promise existed or not, either the Claimants did not rely on the existence of that promise or any such reliance by the Claimants would be unreasonable;
3. in any case, the Claimants' claims should fail because Romania's actions were reasonably related to a rational policy, namely EU accession.

The parties also disagreed on the relationship between EU law and the BIT. The Claimants argued that no conflict exists between the BIT and EU law, since the Accession Treaty (which entered into force on 1.1.2007) and the EC Treaty did not bind Romania at the time the BIT entered into force (1.4.2003) or when the breaches occurred. The Claimants denied that a conflict exists between the Europe Agreement and the BIT for three additional reasons: (i) under the preservation of rights provision in Article 9(2), the BIT prevails over any other treaty; (ii) the BIT is *lex posterior* pursuant Article 30(3) of the Vienna Convention on the Law of Treaties of 1969 ("*VCLT*") and (iii) the BIT is *lex specialis*, since it is a treaty with a more precisely determined scope of application. Conversely, Romania claimed that the BIT must be interpreted in light of Romania's other

[7] Investor's claims that Romania breached its obligation not to expropriate the investment (Article 4(1)) will not be further analyzed in this article as the Tribunal decided that it did not need to address it in the light of the Tribunal's earlier finding that Romania breached its obligation to treat Claimants' investments in a fair and equitable manner.

international obligations, in particular those arising from the Europe Agreement and the EC Treaty. The conclusion of the BIT was, according to the Respondent, a direct consequence of the Europe Agreement. Article 74 of the Europe Agreement explicitly provided that one of Romania's goals was to sign investment protection treaties with Member States. Therefore, Romania's measures to comply with EU law cannot trigger its liability under the BIT.

4. Tribunal's Analyses and Findings

4.1. EU Law v. BIT

Since the enlargement of the European Union by 12 new Member States in 2004, the existence of the intra-EU BITs has sparked a wide debate that involves the European Commission. At the core of the discussion is the validity of such BITs. The European Commission has repeatedly argued that bilateral investment treaties between EU Member States conflict with EU law, are incompatible with the EU single market and, therefore, should be phased out. The EC has maintained that intra-EU BITs discriminate between EU investors from different Member States, since they grant some (but not all) the right to sue Member States before international tribunals. Furthermore, the EC is concerned that investor-to-state arbitration is binding and is not subject to review by the European Court of Justice, whereas the European Court of Justice is the forum to resolve issues of EU law involving an EU Member State.[8]

These matters were thoroughly analyzed by arbitral tribunals in two cases *Eastern Sugar B.V. v. The Czech Republic*[9] and *Eureko B.V. v. The Slovak Republic*.[10] In both cases, the European Commission was invited to submit a legal brief. In its observations delivered to the arbitral tribunals,

[8] European Commission (2012) Commission staff working document Capital Movements and Investment in the EU Commission Services Paper on Market Monitoring, SWD(2012)6 final. http://ec.europa.eu/internal_market/capital/docs/20120203_market-monitoring_en.pdf [4.12.2012].

[9] Eastern Sugar B.V. v. The Czech Republic, Partial Award, 27.3.2007, www.italaw.com.

[10] Eureko B.V. v. The Slovak Republic, Award on Jurisdiction, Arbitrability and Suspension, 26.10.2010, www.italaw.com.

the European Commission made it clear that EU law provides protection for intra-EU investment (including protection available to ensure the free flow of capital and right of establishment). The European Commission added that EU law should take precedence over provisions of any BIT as a substantive matter and that investors cannot rely on intra-EU BIT provisions which are inconsistent with EU law, but should instead bring any disputes to the member-state courts and the European Court of Justice.[11] Neither tribunal shared these views and held that they did not lack jurisdiction for the reasons raised by the European Commission.[12]

Although the approach of the European Commission regarding the intra-EU BITs is unlikely to change, the views of academics and jurisprudence seem to be settled. Despite the existing incompatibility of EU BITs (including intra-EU BITs) with EU law,[13] as long as the intra-EU BITs are not terminated they remain in force and may be relied upon by the investors in intra-EU disputes.[14]

Taking into account the awards in the *Eastern Sugar* and *Eureko* cases and the persuading analyses offered by both tribunals, the Respondent decided not advance an argument alleging the invalidity of the BIT. Rather, Romania argued that the BIT must be interpreted consistently with EU laws, in particular that its conclusion was a direct consequence of the Europe Agreement; therefore any interpretation cannot lead to a situation in which Romania is held responsible under international law for breaching one treaty whilst simultaneously complying with another. Alternatively, the Respondent submitted that, in the event that the

[11] Eastern Sugar B.V. v. The Czech Republic, Partial Award, 27.3.2007, *ibid.*, para. 119, Eureko B.V. v. The Slovak Republic, Award on Jurisdiction, Arbitrability and Suspension, 26.10.2010, *ibid.*, paras 175–196.

[12] Eastern Sugar B.V. v. The Czech Republic, Partial Award, 27.3.2007, *ibid.*, paras 157–191, Eureko B.V. v. The Slovak Republic, Award on Jurisdiction, Arbitrability and Suspension, 26.10.2010, *ibid.*, paras 217–292.

[13] A. Dimopoulos, *EU Foreign Investment Law,* Oxford University Press, Oxford 2011, pp. 305–325.

[14] A. Różalska-Kucal, *Intra-EU BITS – Are They Really Still Necessary? The Best Award of the Year 2012 and Prof. Emmanuel Gaillard Say "Yes"*, 'Polish Review of International and European Law' 2012, vol. 1, no 3–4, pp. at 58, 63–65, M. Burgstaller, *European Law Challenges to Investment Arbitration* [in:] M. Waibel, A. Kaushal, K. Chung, C. Balchin, 'The Backlash against Investment Arbitration', Wolters Kluwer, The Netherlands 2010, p. 464.

Tribunal found the obligations under EU law and the BIT impossible to reconcile, any conflict should be resolved in favour of EU law. In conclusion, the parties to the dispute were in agreement that the BIT constituted a source of law for the Tribunal, but had conflicting views on the role and effects of EU law.

The Tribunal held that there was no real conflict between the treaties. During the disputed period, the relevant rules of international law applicable to Romania and Sweden were the Europe Agreement (which entered into force on 1.4.2005) and the BIT (which entered into force on 1.4.2003). The Accession Treaty was signed on 25.4.2005 and entered into force on 1.1.2007 which means that, from 1.2.1995 until 1.1.2007, Romania was in the negotiation phase, during which it declared that it accepted the *acquis* but was not yet bound by the obligations arising from EU law (other than the Europe Agreement). Therefore, the key question, according to the Tribunal, was whether EU law should play a role in interpreting the BIT. The Tribunal gave an affirmative answer to this question and emphasized that the various treaties should be interpreted having due regard to the other applicable treaties, assuming that the parties entered into each of those treaties in full awareness of their legal obligations under all of them. Since the BIT contains no reference to EU law and the Accession Treaty does not refer to the BIT, it could not be assumed that Romania or Sweden had any intent to deny or modify their obligations under any of the applicable treaties and therefore each treaty, in particular the BIT, must be interpreted in accordance with such intent.

In addition, both the Respondent and the European Commission (acting as *amicus curiae*) argued that the payment, on the basis of the award issued by the Tribunal, of any compensation to the Claimants for the revocation of incentives held to contradict EU law would constitute illegal state aid and thus render the award unenforceable within the EU. The European Commission argued that the European Court of Justice has taken the position that EU competition law forms part of the "public policy" criterion to be taken into account when deciding whether or not to enforce an arbitral award. Under the Convention on the Recognition and Enforcement of Foreign Arbitral Awards of 1958 (the "*New York Convention*"), when a national court is called upon to enforce an award, it must determine whether the formal requirements necessary to make it enforceable have been complied with. In doing so, it may determine on its own motion or upon the basis of a defense raised by the respondent, that the award is contrary to "public policy" (Article V(2)(b) of the New York Convention). In such an event, the recognition and enforcement of an arbitral award by the national court should be denied. Although arbitral awards rendered under the ICSID Convention[15] are to be automatically enforceable as if they were a final court judgment (without the need to be formally recognized), doubts were raised as to whether the ICSID Convention forms part of the EU's legal order, given that the EU itself is not a party to the ICSID Convention. The Tribunal refrained from speculating what might transpire after the rendering of an award, since it held that it was inappropriate to base its decision referring to the merits of the case on matters of EU law that may come into play at the enforcement stage. Despite the Tribunal failing to provide any analyses of that argument, it may certainly be further exploited by respondent states as their defense at the enforcement stage of ICSID awards and, more importantly, non-ICSID awards (provided that the awards are enforced within EU countries).

4.2. Umbrella Clause

Much of the umbrella clause debate visible in jurisprudence and literature to date has been devoted to determining whether commercial obligations fell within its scope or whether it or only applied to obligations that can be said to have been entered into by the host state as a sovereign entity.[16] However, the Tribunal did not have to take a stance on this issue, since all of the actions complained of by the Claimants were undertaken by Romania in its sovereign capacity.

[15] The award in Micula v. Romania was rendered on the basis of the ICSID Convention.

[16] M. Świątkowski, *Naruszenie przez państwo umowy z inwestorem zagranicznym w świetle traktatów inwestycyjnych [Breach of a Contract entered into by a State with a Foreign Investor under the Investment Treaties]*, Beck, Warsaw 2009, pp. 51–103; A. Sinclair, *The Umbrella Clause Debate,* [in:] A. Bjorklund, I. Laird, S. Ripinsky (eds.), 'Investment Treaty Law', British Institute of International and Comparative Law, London 2009, p. 286–311, M. Dimsey, *The Resolution of International Investment Disputes*, Eleven International Publishing, The Netherlands 2008, pp. 56–62.

The parties agreed that, in order for the umbrella clause contained in Article 2(4) to apply, Romania must have had entered into an obligation with the Claimants with regard to their investment and that this obligation must be specific[17]. The parties disagreed, however, as to whether or not the 1998 Ordinance and the Certificates created such an obligation. In resolving the dispute, the Tribunal reached several conclusions.

First, contrary to the Respondent's argument, the umbrella clause does not only protect contractual or quasi-contractual obligations, but all obligations entered into by investors.[18]

Second, establishing whether or not such obligations exist is a question that cannot be answered by relying solely on an interpretation of a particular BIT provision. The interpretation of the obligation for the purpose of the umbrella clause must be made on the basis of the law governing that obligation. In the case at hand, this was Romanian law.[19]

Third, the 1999 Ordinance and its implementing legislation (194/1999 Decision and 525/1999 Decision) created a general entitlement that could be claimed by any qualified investor and this general entitlement in itself did not gave rise to any specific obligations vis-à-vis the Corporate Claimants.[20]

Fourth, the general entitlement established by the 1998 Ordinance and its implementing legislation (194/1999 Decision and 525/1999

[17] The minority view is that also general obligations may fall within the scope of the umbrella clause (i.e. Eureko B.V. v. Republic of Poland, Partial Award, 19.08.2005, www.italaw.com, para. 246, *LG&E Energy Corp., LG&E Capital Corp., LG&E International Inc. v. Argentina Republic,* Decision on Liability, 3.10.2006, www.italaw.com, para. 175).

[18] *Ibid*., paras 414, 415; the Tribunal shared a view which is dominant in literature, see K. Vandevelde, *Bilateral Investment Treaties. History, Policy and Interpretation*, Oxford University Press, New York 2010, p. 258, A. Newcombe, L. Paradell, *Law and Practice of Investment Treaties*, Wolters Kluwer, The Netherlands 2009, pp. 457–460, R. Dolzer, Ch. Schreuer, *Principles of International Investment Law,* Oxford University Press, Oxford 2012, pp. 177, 178.

[19] *Ibid*., paras 417, 418.

[20] *Ibid*., para. 427; the Tribunal seemed to disagree with the minority view expressed by other tribunals that the existence of the obligation to which the umbrella clause may attach is to be determined by international law (i.e. Eureko B.V. v. Republic of Poland, Partial Award, 19.08.2005, *ibid*., paras 121–126, LG&E Energy Corp., LG&E Capital Corp., LG&E International Inc. v. Argentina Republic, Decision on Liability, 3.10.2006, *ibid*., para. 174).

Decision) was transformed into a specific entitlement with regard to Corporate Investors via the issuing of Certificates.[21]

Fifth, the regulatory framework (the 1998 Ordinance, 194/1999 Decision, 525/1999 Decision and the Certificates) provided that the specific entitlement would last until 1.4.2009.[22]

Having decided the above issues, the Tribunal analyzed whether the specific entitlement amounted to an "obligation" under Romanian law for the purposes of the umbrella clause. It held that it did not.[23] Consequently, the Respondent could not be held liable for breaching the umbrella clause. The Tribunal presented a very detailed and interesting reasoning for having reached this conclusion.

According to the Tribunal, it was undisputed that Romania (as any other state) may validly amend its laws. This right arises from general principles of international law and was not waived by Romania by it having given an assurance to the Claimants that it would not amend the 1998 Ordinance or its implementing legislation. In fact, during the period between 2000 and 2004 the legislative framework surrounding the 1998 Ordinance was amended on several occasions, either to the benefit or to the detriment of the Corporate Claimants. Therefore, the issue to be resolved by the Tribunal for the purpose of the umbrella clause did not concern Romania's authority to amend legislation relating to the 1998 Ordinance but, rather, whether or not such an amendment could affect rights created by previous laws with respect to the Corporate Claimants. In answering this question the Tribunal analyzed: (i) whether Romania's undertaking amounted to an "obligation" under Romanian law, and, in the case of an affirmative answer, (ii) whether Romania's "obligation" consisted of providing the Corporate Claimants the same (unchanged) incentives (i.e. those to which they were entitled at the moment of receiving the Certificates) for the whole period ending on 1.4.2009. The Tribunal noted that if it transpired that no "obligation" existed or that such "obligation" was limited to providing the Corporate Claimants with whatever incentives were currently available (i.e. not necessarily those which existed at the moment the Corporate Claimants received the Certificates), then Romania

21 *Ibid.*, paras 430, 431.

22 *Ibid.*, para. 432.

23 *Ibid.*, para. 459.

would not be liable for breaching the umbrella clause. In other words, Romania may be found liable only if it were proven that an "obligation" existed under Romanian law to maintain the same (unchanged) incentives with respect to the Corporate Claimants until 1.4.2009.

The Tribunal observed that it was essential to ascertain whether the 1998 Ordinance and its implementing legislation, together with the Certificates, entitled the Corporate Claimants to vested rights[24] to the incentives (in an unchanged form). In its view, the Claimants and their expert were unable to establish the existence of such vested rights under Romanian law. The Tribunal admitted that the 1998 Ordinance and the whole legal formwork (together with the Certificates) created the appearance of vested rights, but it lacked sufficient evidence on the content of Romania law to be confirm that such rights in fact existed.

It is interesting to note that the Tribunal also presented an alternative approach to its analysis of the "obligation" for the purpose of Article 2(4). Under this approach, the existence of a vested right was insufficient to find that an "obligation" existed within the meaning of the umbrella clause. It would be sufficient to prove that: (i) Romania made an offer to grant incentives and to maintain them until 1.4.2009 in exchange for the investors meeting certain requirements and maintaining them for a period twice as long as the period during which the incentives existed, (ii) the Corporate Claimants accepted the offer, (iii) a relationship of mutual rights and obligations between Romania and Corporate Claimants had arisen which included Romania's assurance (guarantee of stability) to maintain the incentives regime until 1.4.2009 in an unchanged form.[25] Had the Tribunal followed this line of reasoning, it would have arrived at a contrary conclusion, i.e. that Romania had in fact breached Article 2(4). Nevertheless, a majority of the Tribunal felt that the first approach was more suitable.[26]

[24] The Tribunal did not specify how it understand the term "vested rights". According to *Black's Law Dictionary* vested rights are "rights which have so completely and definitely accrued to or settled in a person that they are not subject to be defeated or canceled by the act of any other private person (...) and of which the individual could not be deprived arbitrarily without injustice (...)" (*Black's Law Dictionary*, West Publishing, St. Paul, 1990, p. 1564).

[25] *Ibid*., paras 456, 457.

[26] *Ibid*., para. 458.

From a theoretical perspective, the final decision reached by the Tribunal regarding the umbrella clause is not so important as the path of reasoning it chose to follow when reaching its decision. In the present case, Romania was found not to have breached Article 2(4), given the lack of sufficient evidence regarding the content of Romanian law. However, even if the Tribunal had been able to precisely define the rights possessed by the Corporate Claimants in relation to the incentives (i.e. whether or not such rights were vested not) and, on this basis, uphold or dismiss the Claimants' arguments, this would not have changed the line of reasoning accepted by a majority of the Tribunal. This line sets a relatively high threshold for investors to establish a breach of an umbrella clause where the commitment assumed by the state against an investor does not arise from a contractual or quasi-contractual relationship. If a state provides a foreign investor with certain rights or privileges through its domestic legislation, that state is entitled to amend such legislation even in a manner which will result in the amendment or revocation of such rights or privileges, and this will not amount to a breach of an umbrella clause contained in the investment treaty entered into by the host state with the state of the investor,[27] barring two exceptions. The state will breach an umbrella clause if an investor is able to prove that the state provided some guarantee of stability (i.e. that the legislation would remain un-amended for a period of time) or that it acquired vested rights.

4.3. Fair and Equitable Treatment

4.3.1. Legitimate Expectations

The Tribunal commenced its analyses with an observation that the fair and equitable standard does not guarantee investors the stability of a legal system and that, therefore, each state enjoys the right to amend its existing laws, unless there is a stabilization clause or any other similar commitment on the part of the state. Since neither exception existed

[27] It must be emphasized that this conclusion is limited to the application of an umbrella clause and does not extend to other provisions of the investment treaty. In other words, if in given circumstances the state is not found to be in a breach of an umbrella clause, it cannot be excluded that the same set of circumstance will not amount to breaches of other provisions of the investment treaty.

in the present case, the Claimants' claims, in the view of the Tribunal, could only be analyzed from the perspective of a breach of the investor's legitimate expectations. The Tribunal's view, namely that the host state's right to regulate it law in the public interest must be taken into consideration when evaluating legitimate expectations, is in accordance with the recent jurisprudence of arbitral tribunals.[28] The parties were in agreement that, in order to establish a violation of the fair and equitable standard on the basis that the Claimants' legitimate expectations were undermined, the Claimants must prove that:

1. Romania made a promise or assurance,
2. the Claimants relied on the promise or assurance, and
3. such reliance was reasonable.[29]

Ad. 1

Although the Tribunal had insufficient evidence to determine that the incentives gave rise to the Claimants' right protected by the umbrella clause, it found for the purpose of fair and equitable treatment that Romania acts amounted to a promise that the incentives would not be substantially changed over the period for which they were awarded (i.e. until 1.4.2009).[30] In the Tribunal's view, such a promise or assurance must be attributed to a competent governmental body, but it need not be specific (contrary to a commitment which enjoys protection under the umbrella clause).[31] The Tribunal based its findings on the fact that: (i) the

[28] Joseph Charles Lemire v. Ukraine, Decision on Jurisdiction and Liability, 14.1.2010, www.italaw.com, para. 500; Total S.A. v. Argentina Republic, Decision on Liability, 27.12.2010, www.italaw.com, para. 164; El Paso Energy Company International v. Argentina Republic, Award, 31.10.2011, www.italaw.com, para. 402; Sergei Paushok and others v. Mongolia, award, 28.4.2011, www.italaw.com, para. 302; Impregilo S.p.A. v. Argentina Republic, Award, 21.6.2011, www.italaw.com, paras 290, 291.

[29] *Ibid*., para. 668.

[30] *Ibid*., para. 677.

[31] See C. McLachlan, L. Shore, M. Weiniger, *International Investment Arbitration. Substantive Principles*, Oxford University Press, Oxford 2007, p. 238; A. Reinisch, *Standards of Investment Protection*, Oxford University Press, Oxford 2008, p. 126; A. Newcombe, L. Paradell, *Law and Practice of Investment Treaties*, *ibid*., pp. 280, 281; K. Yannaca-Small, *Arbitration Under International Investment Treaties. A Guide to the Key Issues,* Oxford University Press, Oxford 2009, p. 400; M. Sornarajah, *The International Law on Foreign Investment,* Cambridge University Press, Cambridge 2011 p. 354; A. Diehl, *The*

purpose of 1998 Ordinance was to attract investment in underdeveloped regions, (ii) in order to qualify for the incentives, the Claimants needed to meet specific criteria and to assume certain obligations (in particular, relating to the period of investment, employment, reporting), (iii) the Certificates were issued for a period until 1.4.2009.

Ad. 2

The Claimants began to invest in Romania in the early 1990s and alleged that, as of 1998, they decided to expand their business pursuant to a ten year plan in reliance on the 1998 Ordinance. The investment was completed in phases, with the final phase completing in 2006. The Claimants also alleged that they planned to further develop the business and that new investments had been initiated, but not completed, in light of the revocation of the incentives. The Tribunal disagreed and emphasized that some of the Claimants' investments were not predicated on the 1998 Ordinance. It held that legitimate expectations: (i) could only have crystallized at the time that the Corporate Claimants received the Certificates (which took place during the period 2000–2002) and (ii) such expectation must have ceased once it become clear that Romania would revoke the incentives, which occurred with the issuance of the 2004 Ordinance.[32]

Ad. 3

The Tribunal accepted Romania's view that the context of its EU accession must be taken into account, however it emphasized that it would not deem the revocation of the incentives to be fair merely because they were undertaken pursuant to Romania's duty to harmonize its laws with those of the EU. Furthermore, the Tribunal agreed to analyze whether the Claimant's legitimate expectations were breached in the light of an established principle that every state is free to amend its laws in the absence of a commitment to the contrary (i.e. stabilization clause). Therefore the Tribunal expressed the view that, in order to find that

Core Standard of International Investment Protection. Fair and Equitable Treatment, Wolters Kluwer, The Netherlands 2012, p. 411; R. Dolzer, Ch. Schreuer, *Principles of International Investment Law, ibid.*, p. 145.

[32] *Ibid.*, para. 722.

Romania had breached the fair and equitable treatment principle, it was insufficient for the Claimants to prove that Romania made a promise and that they relied on that promise, but it would also require proof that the Claimants' reliance on that promise was reasonable under both EU regulations (and Romania's EU accession process) and Romania's internal laws.[33] Such an approach seems justified since, otherwise, as stated by the *Maffezini* tribunal[34], the treaties would become insurance policies against bad and unreasonable business decisions, which was certainly not the aim of investment protection.

The Tribunal arrived at the conclusion that, until 2003, it was reasonable for the Claimants to believe that the incentives were compatible with EU law.[35] This conclusion was supported by expert opinion which stated that, from a purely legal point of view, it was not obvious that the incentives failed to meet the criteria of lawful regional aid, as set forth by the EU. Furthermore, the record showed that Romania itself believed, at the time the 1998 Ordinance was enacted, that its incentives were compatible with EU state aid requirements. The Tribunal pointed out that the same belief was expressed by many governmental officials in public statements, and it concluded that the Claimants should not be held to a higher standard than the government and its officials.[36]

Determining whether or not the Claimant's expectations were reasonable under Romanian law turned out to be a far more difficult task. The Respondents relied heavily on the fact that, as early as 2000, the Competition Council issued the 2000 Decision in which it found that the 1998 Ordinance was incompatible with the Europe Agreement and required elimination. According to the Respondent, the 2000 Decision undermined the reasonableness of the Claimant's expectations that the incentives would remain unchanged for 10 years. The Tribunal, however, disagreed with the Respondent. Although the Competition Council tried

[33] *Ibid*., para. 690; see also P. Muchlinski, *"Caveat Investor"? The relevance of the Conduct of the Investor under the Fair and Equitable Treatment Standard*, 'International and Comparative Law Quarterly' 2006, vol. 55, no 4, at pp. 527–530; A. Diehl, *the Core Standard of International Investment Protection. Fair and Equitable Treatment, op. cit.*, pp. 413–424.

[34] Emilio Agustin Maffezini v. The Kingdom of Spain, Award, 13.11.2000, www.italaw.com, para. 64.

[35] *Ibid*., para. 691.

[36] *Ibid*., para. 706.

to enforce the 2000 Decision before the Romanian courts, it failed. Given the government's failure to follow the 2000 Decision and had *de facto* overruled its recommendations before the common courts, the Tribunal considered that Romania had confirmed the legality of the incentives under the Romanian law. Accordingly, it held that it was reasonable for the Claimants, also from the perspective of Romanian law, to believe that the incentives would be maintained for 10 years.[37]

4.3.2. Lack of Transparency and Consistency

The Investors also claimed that Romania had breached its obligation to accord fair and equitable treatment by acting in a manner that was not transparent or consistent. They argued that Romania, on the one hand, promoted the 1998 Ordinance and incentives whilst, on the other hand, negotiating with the EU regarding their revocation. The Tribunal found that a majority of the claims regarding an alleged lack of transparency were unsubstantiated. In its view, Romania acted in good faith and had grounds to believe that the 1998 Ordinance would continue to remain in effect following its accession to the EU. However, the Tribunal decided that Romania had breached the BIT by failing to inform the Claimants in a timely manner that the 1998 Ordinance would be revoked prior to its date of expiry.[38]

4.3.3. Unreasonable Conduct

The Claimants argued that Romania had acted unreasonably by: (i) promoting the incentives despite the fact that it was negotiating with the EU regarding their revocation, (ii) revoking the incentives without being required to do so and (iii) requiring that the Claimants maintain the investment for twice the period they received the incentives (i.e. for 20 years). The Tribunal ruled that Romania had not acted unreasonably, with one exception. The Tribunal pointed out that, in the beginning, Romania believed that the 1998 Ordinance was compatible with EU law and later on that it would be able to negotiate a transition period in order to maintain the incentives. Furthermore, the revocation of the 1998 Ordinance took place only after it became apparent that the existence

[37] *Ibid.*, para. 717.

[38] *Ibid.*, para. 870.

of the incentives was considered by the European Commission to be an obstacle to Romania's accession to the EU. The exception specified by the Tribunal referred to Romania's decision to uphold the investors' (including the Corporate Claimants') obligation to maintain the investment for 20 years, despite repealing the incentives.[39]

The Tribunal also rejected the Investors' claim that Romania had acted in bad faith[40].

4.4. Damages

The Claimants provided three alternative methods according to which the Tribunal could calculate damages. First, two computations supported the calculation that their losses were at the level of 600 million Euro, whilst a third calculation indicated losses of approximately 200 million Euro.[41] The Tribunal rejected the second and third method and awarded damages of approximately 85 million Euro, plus compound interest.[42] A detailed analysis of how the Tribunal arrived at the above figure would exceed the scope of this article, but one issue is worth mentioning.

As a defense, the Respondent argued that Romania's accession to the EU benefited the Claimants. Therefore, despite any short-term disadvantages the Claimants suffered from the revocation of the 1998 Ordinance, any additional profits made by them in consequence of Romania's accession to the EU should be off-set against the losses from such disadvantages. The Respondent argued that, in situations where state measures both harmed and benefited a claimant's business activities, tribunals have taken the positive impact into account when assessing damages.[43] The Tribunal, in principle, agreed with such an approach to calculating damages but found that the Respondent was unable to provide a convincing and detailed calculation of benefits that Romania's accession to the EU brought the Claimants. In particular, it observed that the macroeconomic analysis relied upon by the Respondent, which showed

[39] *Ibid*., paras 825, 826.

[40] *Ibid*., para. 836.

[41] *Ibid*., paras 890–895.

[42] *Ibid*., para. 1329.

[43] *Ibid,* paras 1156–1163.

that the accession had the effect of increasing the Claimants' sales and profits, was insufficient since it failed to precisely quantify the alleged benefits for the Claimants.[44]

5. Concluding Remarks

The 370 pages award represents a well-structured and instructive analysis of a number of highly-debated matters in investment arbitration.

Much argument was devoted by the parties to the interplay between BIT provisions and EU law. The Tribunal held that there was no conflict between the two. Since the BIT contains no reference to EU law and the Accession Treaty does not refer to the BIT, it could not be assumed that either Romania or Sweden had any intent to deny or modify their obligations under any of the applicable treaties and therefore each treaty, in particular the BIT, must be interpreted in accordance with such intent. Accordingly, the Tribunal found that EU law should play a role in interpreting the BIT and emphasized that the various treaties should be read having due regard to the other applicable treaties (assuming that the parties entered into each of those treaties in full awareness of their legal obligations under all of them).

The Respondent and the European Commission (acting as *amicus curiae*) argued that the payment, on the basis of the award issued by the Tribunal, of any compensation to the Claimants would constitute illegal state aid and thus render the award unenforceable within the EU. The Tribunal decided not to analyze this matter, since it found it inappropriate to base its decision on the merits of the case on matters of EU law that may come into play at the enforcement stage.

The Tribunal set a relatively high threshold for investors to prove the breach of an umbrella clause where the commitment assumed by the state against an investor did not arise from a contractual or quasi-contractual relationship, but rather from domestic legislation. This conclusion was based upon the assumption that states are entitled to amend their legislation and that such amendment does not amount to a breach of an umbrella clause unless the state had earlier provided some guarantee of

[44] *Ibid,* paras 1167, 1168.

stability (i.e. that the legislation would not be amended for a period of time) or that the investor had acquired vested rights.

The award also offers a thorough and balanced analyses of an investor's legitimate expectations. According to the Tribunal, in order to establish a violation of the fair and equitable standard on the basis that its legitimate expectations had been undermined, an investor must prove that: (i) the state made a promise or assurance, (ii) the investor relied on such promise or assurance, and, most importantly, (iii) that such reliance was reasonable. The Tribunal added that the BIT only protects investments made in reliance on legitimate expectations and that it could not protect investments made after such expectations had ceased to exist.