# JUDGMENT OF THE COURT (First Chamber)

15 September 2011 *

In Case C-264/09,

ACTION under Article 226 EC for failure to fulfil obligations, brought on 14 July 2009,

**European Commission,** represented by O. Beynet, F. Hoffmeister and J. Javorský, acting as Agents, with an address for service in Luxembourg,

applicant,

v

**Slovak Republic,** represented by B. Ricziová, acting as Agent,

defendant,

* Language of the case: Slovak.

THE COURT (First Chamber),

composed of A Tizzano, President of the Chamber, J.-J. Kasel, A. Borg Barthet (Rapporteur), E. Levits and M. Berger, Judges,

Advocate General: N. Jääskinen,
Registrar: A. Calot Escobar,

having regard to the written procedure,

after hearing the Opinion of the Advocate General at the sitting on 15 March 2011,

gives the following

**Judgment**

1 By its application, the Commission of the European Communities requests the Court to declare that, by failing to grant non-discriminatory access to its transmission system, the Slovak Republic has failed to fulfil its obligations under Articles 20(1) and 9(e) of Directive 2003/54/EC of the European Parliament and of the Council of

26 June 2003 concerning common rules for the internal market in electricity and repealing Directive 96/92/EC (OJ 2003 L 176, p. 37).

## Legal context

*The agreement between the Swiss Confederation and the Czech and Slovak Federative Republic on the reciprocal promotion and protection of investments*

2 Under Article 1(1) of the agreement concluded on 5 October 1990 between the Swiss Confederation and the Czech and Slovak Federative Republic on the reciprocal promotion and protection of investments ('the Investment Protection Agreement'), the term 'investor' is to be understood to mean:

'...

(b) legal entities, including companies, registered companies, partnerships or other organisations, which are constituted or organised in any other manner in accordance with the legislation of that Contracting Party, and which have their headquarters and actual economic activities in the territory of that same Contracting Party;

...'

3 Under Article 1(2) of that agreement, the term 'investment' includes every kind of assets and in particular:

'…;

(c) monetary claims and rights to any performance having an economic value;

…'

4 Article 4 of that agreement, entitled 'Protection, treatment', states:

'…

(2) Each Contracting Party shall ensure fair and equitable treatment within its territory of the investments of the investors of the other Contracting Party. …

…'

5 Article 6 of that agreement, entitled 'Dispossession, compensation', states:

'(1) Neither of the Contracting Parties shall take, either directly or indirectly, measures of expropriation, nationalisation or any other measure having the same nature or the same effect against investments of investors of the other Contracting

Party, unless the measures are taken in the public interest, on a non-discriminatory basis, and under due process of law, and provided that provisions be made for effective and adequate compensation. …

…'

*The Energy Charter Treaty*

6 Article 10(1) of the Energy Charter Treaty, signed in Lisbon on 17 December 1994 ('the ECT') and approved on behalf of the European Communities by Council and Commission Decision 98/181/EC, ECSC, Euratom 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 (OJ 1998 L 69, p. 1), provides as follows:

'Each Contracting Party shall, in accordance with the provisions of this Treaty, encourage and create stable, equitable, favourable and transparent conditions for Investors of other Contracting Parties to make investments in its area. Such conditions shall include a commitment to accord at all times to investments of investors of other Contracting Parties fair and equitable treatment. Such investments shall also enjoy the most constant protection and security and no Contracting Party shall in any way impair by unreasonable or discriminatory measures their management, maintenance, use, enjoyment or disposal. In no case shall such investments be accorded treatment less favourable than that required by international law, including treaty obligations. Each Contracting Party shall observe any obligations it has entered into with an investor or an investment of an investor of any other Contracting Party.'

7 Article 13 of that treaty, entitled 'Expropriation', provides as follows:

'1. Investments of investors of a Contracting Party in the area of any other Contracting Party shall not be nationalised, expropriated or subjected to a measure or measures having effect equivalent to nationalisation or expropriation (hereinafter referred to as "expropriation") except where such expropriation is:

(a) for a purpose which is in the public interest;

(b) not discriminatory;

(c) carried out under due process of law;

and

(d) accompanied by the payment of prompt, adequate and effective compensation.

Such compensation shall amount to the fair market value of the investment expropriated at the time immediately before the expropriation or impending expropriation became known in such a way as to affect the value of the investment (hereinafter referred to as the "valuation date").

Such fair market value shall, at the request of the investor, be expressed in a freely convertible currency on the basis of the market rate of exchange existing for that currency on the valuation date. Compensation shall also include interest at a commercial rate established on a market basis from the date of expropriation until the date of payment.

…'

*European Union legislation*

8 Article 2 of the 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 (OJ 2003 L 236, p. 33) provides that '… the provisions of the original Treaties and the acts adopted by the institutions … shall be binding on the new Member States and shall apply in those States under the conditions laid down in those Treaties and in this Act'.

9 Article 9(e) of Directive 2003/54 provides:

'Each transmission system operator shall be responsible for:

…

(e) ensuring non-discrimination as between system users or classes of system users, particularly in favour of its related undertakings;

…'

10 Article 20(1) of Directive 2003/54 provides:

'Member States shall ensure the implementation of a system of third party access to the transmission and distribution systems based on published tariffs, applicable to all eligible customers and applied objectively and without discrimination between system users. Member States shall ensure that these tariffs, or the methodologies underlying their calculation, are approved prior to their entry into force in accordance with Article 23 and that these tariffs, and the methodologies – where only methodologies are approved – are published prior to their entry into force.'

**Background to the dispute and pre-litigation procedure**

11 On 27 October 1997, Aare-Tessin AG für Elektrizität ('ATEL'), an undertaking established in Olten (Switzerland), and Slovenské elektrárne a.s., an undertaking established in Bratislava (Slovakia), the successor to which was Slovenská elektrizačná prenosová sústava, a.s. ('SEPS'), acting as the Slovak transmission system operator, entered into a contract granting a right of transmission on Slovenské elektrárne's high-voltage system in Slovakia ('the contract at issue'). Under Article 3 of that contract, SEPS granted ATEL a guaranteed right of 300 MW of transmission capacity

between Poland and Hungary, from 1 October 1998 to 30 September 2014. ATEL is free to avail itself of that right as it sees fit.

12 The right of transmission reserved for ATEL is in return for its financial contribution to the construction of the transmission line on which it enjoys that right, which represented more than 50 % of the construction costs incurred.

13 After putting the Slovak Republic on formal notice, the Commission sent to it, on 15 December 2006, a reasoned opinion in which it expressed the view that, by reserving capacity at the 'SEPS interconnection' on the lines connecting the Slovak system to the Polish and Hungarian systems, the Slovak Republic was in breach of its obligations under Directive 2003/54.

14 By letter of 9 February 2007, the Slovak Republic replied to that reasoned opinion by stating that the contract at issue was not a contract for preferential access but an investment contract. The Slovak Republic also indicated that, despite negotiations conducted with a view to terminating or amending that contract, ATEL was insisting on its performance and on compliance with the Investment Protection Agreement.

15 Taking the view that the Slovak Republic had not remedied the failure to fulfil its obligations, the Commission decided to bring the present action.

**The action**

*Arguments of the parties*

16 The Commission submits, first of all, that the Slovak Republic has failed to fulfil its obligations under Articles 9(e) and 20(1) of Directive 2003/54, which require guaranteed, non-discriminatory access to the transmission system.

17 In the Commission's submission, the preferential right of transmission granted by SEPS to ATEL until 30 September 2014 places ATEL in a privileged position in relation to other users of the system.

18 The Commission submits, second, that, contrary to the Slovak Republic's assertions, the breach of Directive 2003/54 cannot be justified by reliance on the first paragraph of Article 307 EC. That provision, it argues, applies only where there is incompatibility between Community law and the obligations which Contracting States have under agreements concluded prior to the date of their accession to the European Union. According to the Commission, however, there is no incompatibility between the Investment Protection Agreement and Community law. Moreover, that agreement in no way obliges the Slovak Republic to maintain the contract at issue in effect. On the contrary, it is perfectly free to terminate that contract in order to comply with its obligations under Directive 2003/54.

19 Third, the Commission submits that, since Articles 4(2) and 6 of that agreement do not require that the contract at issue be performed up to its expiry date of 30 September 2014, there is no obligation, within the meaning of the first paragraph of

Article 307 EC, which prevents the Slovak Republic from terminating the contract, thereby establishing non-discriminatory access to the transmission system in accordance with Directive 2003/54.

20 In its statement in defence, the Slovak Republic expresses the view, first, that the contract at issue does not discriminate against other operators on the Slovak electricity market.

21 Second, the Slovak Republic submits that it is necessary to take the view that the contract at issue is not a contract for preferential access but an investment contract. It states that the right of transmission is merely one specific means by which ATEL may recover its investment made under the contract and that actual withdrawal of the guarantee of the right of transmission would give rise to discrimination against that company in relation to other operators on the market. That withdrawal would make ATEL subject to the same conditions as the market operators, even though the latter have not made any investment in the Slovak transmission system. This, it argues, would amount to depriving ATEL of its rights without appropriate compensation, which would be at variance not only with the contract at issue but also with the ECT, which forms an integral part of Community law.

22 Third, as regards the protection of ATEL's investment, on the basis of the ECT, the Slovak Republic submits that that treaty precludes an interpretation of Directive 2003/54 as meaning that it requires the withdrawal of the guarantee of ATEL's right of transmission, as that directive cannot adversely affect the protection of investors guaranteed by the ECT. The interpretation of Directive 2003/54 advocated by the Commission would enable ATEL to argue, in any arbitration proceedings, that the withdrawal of the guarantee of the right of transmission, without the payment of

appropriate compensation, infringes the provisions governing expropriation (Article 13 of the ECT), the right to fair and equitable treatment (Article 10 of the ECT) or the clause of the contract at issue (last sentence of Article 10(1) of the ECT).

23 Fourth, the Slovak Republic submits that, even if the withdrawal of the guarantee of the right of transmission did not meet the conditions of direct expropriation and even if that withdrawal was carried out in the general interest, ATEL would be able to show that there had been an indirect, legislatively-sanctioned expropriation which could be carried out only in compliance with all the conditions provided for in respect of expropriation, including that which requires payment of compensation to the investor concerned.

24 Fifth, the Slovak Republic regards as unfounded the Commission's assertions that, first, the termination of the contract at issue would not be contrary to Article 4(2) of the Investment Protection Agreement, which requires fair and equitable treatment of investments, in that ATEL was able to anticipate the accession of the Slovak Republic to the European Union and the liberalisation of the energy market and, second, the Slovak Republic had not given any undertaking to the Swiss Confederation that it would not introduce regulatory amendments which would result in termination of the contract at issue before its expiry date of 30 September 2014.

25 In its statement in reply, the Commission rejects as completely unfounded the Slovak Republic's arguments that, first, the infringement has ceased because the practices in effect changed as from 1 January 2008, with the result that, since then, ATEL has no longer enjoyed preferential access and, second, amendment of the contract at issue would involve the provision of significant financial compensation under international law.

26 The Commission argues in that regard that, first, according to settled case-law, a mere practice cannot put an end to an infringement, since binding provisions which are contrary to Community law remain in force, and that, in the present case, the infringement continues as long as the contract at issue has not been amended or terminated. Second, undertakings may or may not have a right to compensation under international law or national law provisions, due to the loss of contractual rights on which the preferential treatment of the investments they have made is based.

27 The Commission infers from this that, since the Slovak Republic has not succeeded in establishing that Directive 2003/54 is contrary to the ECT, its line of argument, based on Article 307 EC and relating to the European Community's international commitments, is unfounded.

28 As regards the argument relied on by the Slovak Republic, to the effect that termination of the contract at issue would be contrary to Article 4(2) of the Investment Protection Agreement because it does not constitute fair and equitable treatment, the Commission replies that no investor can legitimately expect the regulatory framework to remain immutable and that informed investors knew, or ought to have known, that the repercussions which accession to the European Union would have on the legal situation in the Slovak Republic would be significant. Thus, Article 4(2) of that agreement does not in any way oblige the Slovak Republic to maintain in place a discriminatory scheme of access to the transmission system such as that which results from the contract at issue.

*Findings of the Court*

29 The Slovak Republic's defence is based on both the ECT and the Investment Protection Agreement.

30 Since the latter agreement relates directly to investment protection, it is appropriate to consider the Slovak Republic's defence based on that agreement.

31 The Investment Protection Agreement was concluded on 5 October 1990, that is to say, before the accession of the Slovak Republic to the European Union, which occurred only on 1 May 2004. That agreement, which binds the Slovak Republic in respect of investments made within its territory, contains terms which safeguard the protection of investments made by Swiss investors in Slovakia.

32 Consequently, as noted by the Advocate General in point 77 of his Opinion, if the Slovak Republic was required under that agreement to fulfil obligations resulting from the contract at issue, any discriminatory treatment arising from the preferential treatment granted to ATEL would be justified, even if it was to be regarded as incompatible with Directive 2003/54.

33 In order to ascertain whether that is the case, it is appropriate to examine whether the preferential access granted to ATEL must be considered as an investment covered, at the time, by that agreement. Only if that is so will it also be necessary to examine whether the Slovak Republic could have terminated the contract at issue without breaching that agreement.

34 Article 1(2)(c) of the Investment Protection Agreement provides that it applies to investments, defined as 'every kind of assets', in particular 'monetary claims and rights to any performance having an economic value'.

35 In the present case, by covering more than 50 % of the construction costs of the transmission line from Krosno (Poland) to Lemesany (Slovakia), ATEL was able to obtain a right of transmission on that line for a specific capacity. In other words, the obligation assumed by SEPS to grant ATEL a specific transmission capacity, merely at the latter's request, forms part of the contractually-stipulated remuneration provided for by way of consideration for ATEL's financial contribution towards the construction costs of the transmission line in question.

36 In those circumstances, the right of transmission acquired by ATEL clearly has economic value since it guarantees to ATEL access, for a specific capacity, to the Slovak transmission system which it requires to enable it to sell electricity in Poland via Hungary.

37 Consequently, as the Advocate General has noted in point 71 of his Opinion, the investment made by ATEL must be regarded as an investment within the meaning of Article 1(c) of the Investment Protection Agreement which the Slovak Republic is under an obligation to protect pursuant to Article 4(1) and (2) of that agreement.

38 It is thus necessary to examine whether a possible termination of the contract at issue by SEPS would give rise to a breach of that agreement by the Slovak Republic in the light of that Member State's international obligations.

39 The Commission argues that, in the circumstances of the present case and contrary to the assertions of the Slovak Republic, termination of that contract would not be contrary to either Article 4(2) of that agreement, which provides for fair and equitable treatment of investments, or Article 6 thereof, since it does not constitute expropriation within the meaning of that term.

40 It should be borne in mind in this regard that, even though it is not for the Court to interpret the Investment Protection Agreement, it is none the less appropriate to examine the factors which make it possible to determine whether that agreement imposes an obligation on the Slovak Republic which cannot be affected by the provisions of the EC Treaty, within the terms of the first paragraph of Article 307 EC.

41 According to settled case-law, the purpose of the first paragraph of Article 307 EC is to make clear, in accordance with the principles of international law, as set out in, inter alia, Article 30(4)(b) of the Vienna Convention on the Law of Treaties of 23 May 1969, that the application of the EC Treaty does not affect the duty of the Member State concerned to respect the rights of non-member countries under a prior agreement and to perform its obligations thereunder (see, to that effect, Case 812/79 *Burgoa* [1980] ECR 2787, paragraph 8).

42 Furthermore, in order to determine whether a Community rule may be deprived of effect by an earlier international agreement, it is necessary to examine whether that agreement imposes on the Member State concerned obligations the performance of which may still be required by non-member countries which are parties to it (Case C-158/91 *Levy* [1993] ECR I-4287, paragraph 13).

43 According to the Slovak Republic, the Investment Protection Agreement requires it to maintain in force the obligation imposed on SEPS to guarantee preferential access for ATEL to the transmission line referred to in the contract at issue.

44 It should, however, be borne in mind that, in its judgment in Case C-62/98 *Commission* v *Portugal* [2000] ECR I-5171, paragraph 49, the Court stated that, although, in the context of Article 307 EC, the Member States have a choice as to the appropriate steps to be taken to eliminate any incompatibilities existing between a pre-Community

convention and the EC Treaty, if a Member State encounters difficulties which make adjustment of an agreement impossible, an obligation to denounce that agreement cannot be excluded.

45 In that case the Court had held, inter alia, that, since the agreement in question contained a clause which made express provision for the possibility of denunciation, its denunciation by the Portuguese Republic did not breach the rights which, in that case, the Republic of Angola enjoyed under it (*Commission* v *Portugal*, paragraph 46).

46 It must, however, be stated that the contract at issue in the present case does not contain any clause providing for a possibility of denunciation.

47 With regard to the possibility for the Slovak Republic to terminate that contract in compliance with Article 6 of the Investment Protection Agreement, it should be noted that that provision provides for broad investment protection, covering not only direct and indirect expropriation measures, but also measures which have an effect equivalent to expropriation.

48 Consequently, in so far as such a termination of the contract at issue would have the consequence of depriving ATEL of the remuneration provided for by that contract in return for its financial contribution towards the construction of the transmission line between Krosno and Lemesany, such a measure would impact adversely on ATEL's rights and would thus have the same effect as expropriation within the meaning of Article 6 of the Investment Protection Agreement.

49 Admittedly, that Article 6 also provides for entitlement to compensation on the basis of the breach of the right of the investor not to be expropriated. However, the obligation to provide compensation in the event of expropriation does not have the effect of cancelling out the Slovak Republic's obligation not to take expropriation measures against investments which are protected by the Investment Protection Agreement.

50 It should also be noted that, as pointed out by the Advocate General in point 105 of his Opinion, the Slovak Republic cannot modify the terms or effects of the contract at issue by its legislation, or deprive that contract of legal effects. Slovak legislation declaring contracts providing for privileged access to the transmission system invalid and inapplicable would not alter the fact that SEPS would remain bound by the contract at issue. Therefore, the only way for the Slovak Republic to comply with its obligation in the present case would be to enact legislation which targets SEPS and prevents it from implementing that contract, which would be tantamount to an indirect expropriation of ATEL's right of transmission.

51 In the light of the foregoing, the Court finds that the preferential access granted to ATEL may be regarded as an investment protected by the Investment Protection Agreement and that, under the first paragraph of Article 307 EC, it cannot be affected by the provisions of the EC Treaty.

52 In those circumstances, it must be held that, even if it were to be assumed that the preferential access granted to ATEL were not compliant with Directive 2003/54, that preferential access is protected by the first paragraph of Article 307 EC.

53 Consequently, the Commission's action must be dismissed.

**Costs**

54 Under Article 69(2) of the Rules of Procedure, the unsuccessful party is to be ordered to pay the costs if they have been applied for in the successful party's pleadings. Since the Slovak Republic has applied for costs and the Commission has been unsuccessful, the Commissiobn must be ordered to pay the costs.

On those grounds, the Court (First Chamber) hereby:

**1. Dismisses the action;**

**2. Orders the European Commission to pay the costs.**

[Signatures]