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INVESTMENT ARBITRATION IN ENERGY CONFLICTS

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ABSTRACT

The purpose of this Thesis is to provide an overview of the world of international arbitration regarding investment protection in energy disputes under the ECT and BITs.

Significant reverberations of globalisation can be seen in all sectors with no exception in the field of law. Rapid dispute settlement of many disputes is produced independently of national jurisdiction, specifically in the energy sector, as a result of international investors' and investments' mechanisms. International investment law and arbitration are one of the fastest-developing areas of public international law.

International investment law has become increasingly prominent in the international legal order and the catalyst was the explosion of Bilateral Investment Treaties between States and a sharp increase in international investment disputes. In the past decades, there has been an impressive rise in the number of bilateral investment treaties and other agreements with investment-related provisions, followed by a drastic rise in the number of disputes between private investors and sovereign states.

This Thesis will highlight decisions under the ECT jurisdiction, but it is not desirable and possible to discuss all issues raised in the field of international investment arbitration.

This Thesis' conclusion is that, since future investment disputes between companies and Host States are inevitable, there are some developing tendencies, that deal with the consideration of the Host States to reclaim part of their regulatory sovereignty.

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I do hereby state that I owe every responsibility for any typographical and grammatical error that is contained in this work.

Konstantinos Gourgiotis,

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CHAPTER I

INTRODUCTION

1. Why does this thesis deal with the energy sector?

The energy sector is the sum of all industries in the creation and offer of vitality, including fuel extraction, assembling, refining and conveyance[1]. Nowadays, humans waste large amounts of fuel, and the energy industry is a central part of our day life.

The utilisation of energy is of paramount importance to the human culture by helping it to control and adjust to nature. Dealing with the utilisation of energy is unavoidable in any practical society. In the industrialised world, the advancement of vitality assets has become a key factor for agribusiness, transportation, waste accumulation, data innovation, correspondences that have ended up requirements of a created society. The expanding utilisation of vitality since the Industrial Revolution has additionally carried with it various major issues, some of which, for example, global warming, present conceivably severe dangers to the world.

Developing countries that are rich in natural resources and fossil fuels intend to enhance their economies through the exploitation of these resources. The energy sector has played a crucial role in the context of the global economy. Prices of oil and such other sources of energy have been affecting the economies of various developing nations and have been playing crucial roles in shaping them.[2]

2. Methods of solving conflicts and disputes in energy sector in general

[1] See the definition given in http://encyclopedia2.thefreedictionary.com/Energy+Industry

[2] See Odze Varis « International Energy Investments: Tracking the Legal Concept » Groningen Journal of International Law. Vol. 2, No.1: Energy and Environmental Law p.84

Energy disputes are often associated with a high financial stake, a strong public interest and have a cross-border character, due to the origin of the parties involved. Increasingly, disputes involve renewable sources as well as non-renewable sources, such as oil and gas, and network-bound energies, such as electricity and gas. The main reason for these disputes lies in sudden, drastic fluctuations in market prices.

Ventures in energy sector require a relentless and solid environment. When a dispute comes up the energy players need assurances that there is enough protection for their interests. Although this thesis will refer specifically to International Investment Arbitration, it is appropriate to first outline other significant existing ways of solving energy disputes.

i) Negotiation[3]

Negotiation is the most basic means of settling disputes. It is back-and-forth communication between the parties of the conflict with a view to trying to find a solution. There are no specific procedures to follow - parties can determine their own - but it works best if all parties agree to remain calm and not talk at the same time. Depending on their situation, they can negotiate in the boardroom of a big company, in an office or even in their own living room.

In the most successful negotiations, the needs and interests of both parties are considered[4]. A negotiated agreement can become a contract and be enforceable. This process can be appropriately used at any stage of the conflict - before a lawsuit is filed, while a lawsuit is in progress, at the conclusion of a trial, even before or after an appeal is filed.

ii) Mediation

Mediation is a voluntary process in which a neutral third person steps in. His goal it to assist and facilitate the communication between the parties which will eventually

[3] ICEA *Dispute Resolution in the Energy Sector Initial Report* available online at « http://www.energyarbitration.org/wp-content/uploads/2015/05/ICEA-Dispute-Resolution-in-the-Energy-Sector-Initial-Report-Square-Booklet-Web-version.pdf »

[4] See a famous quote about negotiation “Negotiating in the classic diplomatic sense assumes parties more anxious to agree than to disagree.” **Dean Acheson, American Statesman, Lawyer**

reach an agreement. Mediation often is the next step if negotiation proves unsuccessful.

In particular, when the parties are unable to negotiate a resolution to their dispute by themselves, they may seek the assistance of a mediator who will help the parties explore ways of resolving their differences. Parties should always consult their counsel before signing an agreement to be sure that the agreement protects their rights.

The basic characteristics of mediation are its voluntary, informal, flexible, private and confidential character and the fact that allows the parties to avoid the uncertainty, time, cost and stress of going to trial. Above all, the interest of the parties matter, not their positions and *the mediator act as a neutral third party and facilitates rather than directs the process*[5]

iii) Ligitation

If parties cannot settle their differences through negotiation, mediation, arbitration or some other means, then they should pursue litigation through the courts with their lawyer.

Specific rules of procedure, discovery and presentation of evidence must be followed. There can be a number of court appearances by the parties or their lawyer. If the parties cannot agree how to settle the case, either the judge or a jury will decide the dispute for them through a trial. In litigation, attorneys and the judge nearly always run the show. Primary parties may take part in the formation of the case and may be called on to provide evidence and give testimony, but generally, need to allow attorneys to handle the legal technicalities of the issue. Also, the parties of a dispute can not choose the judges.

A trial is a formal judicial proceeding allowing full examination and determination of all the issues between the parties with each side presenting its case to either a jury or a judge. Therefore, litigation may delay cases, cause Courts typically having a larger

[5] See the official definition given in wikipedia « https://en.wikipedia.org/wiki/Mediation#Litigation »

caseload and more inbuilt pre-trial procedures. Court trials are nearly always open to the public unless the judge has a specific reason to order the trial to be sealed.

The decision is rendered by applying the facts of the case to the applicable law. Judges are bound to apply the rules of evidence and follow all relevant case law and Court rules. That verdict or decision can conclude the litigation process and be enforceable; however, if appropriate, the loser can appeal the decision to a higher court. In some cases, the losing party may have to pay the costs of the lawsuit and may have to pay the other party's attorney fees.

CHAPTER II

INVESTMENT ARBITRATION

1. What is Investment Arbitration in General?

Arbitration[6] is the submission of a disputed matter to an impartial person for decision. An arbitration is generally more private and efficient than a litigation. The agreement between the parties involves specialist or industry-specific subject matter and the parties feel more comfortable being able to either directly choose an arbitrator, or set parameters on who may arbitrate

Arbitration is typically an out-of-court method for resolving a dispute. Typically, arbitrators are not bound to follow and apply all rules of evidence and relevant case law rules, like judges (and the failure to do so is not a ground for appeal). The arbitrator controls the process, will listen to both sides and make a decision. Like a trial, only one side will prevail. In arbitration, unless the parties agree otherwise, there is generally only very limited rights of appeal. For instance, under Greek Civil Procedural Law there is no right of appeal.[7]

In a more formal setting, the arbitrator will conduct a hearing where all of the parties present evidence through documents, exhibits and testimony. The parties may agree

[6] See C.L. Lim, Jean Ho «International Investment Arbitration». The article is available online at http://www.oxfordbibliographies.com/view/document/obo-9780199796953/obo-9780199796953-0135.xml

[7] See Article 895 of Greek Civil Procedural Law

to, in some instances, establish their own procedure; or an administrating organisation may provide procedures. There can be either one arbitrator or a panel of three arbitrators. An arbitration hearing is usually held in offices or other meeting rooms or in specific institutions. As a result, an arbitration will likely be concluded in less time than a litigation.

The result can be binding if all parties have agreed to be bound by the decision and they gave consent to the jurisdiction of the arbitral tribunal. In that case, the right to appeal the arbitrator's decision is very limited. The rendered award will be converted into a judgment, which is often a typical procedure, at which point it has the effect of being a judgment. A party who opposes converting an award into a judgment has a high burden of proof to satisfy and with this attitude, it may breach international obligations. Conversely, a party aggrieved by a judicial judgment usually has at least one "of right" right of appeal. In nonbinding arbitration, a decision may become final if all parties agree to accept it or it may serve to help you evaluate the case and be a starting point for settlement talks.

Many lawyers, judges, other professionals such as professors or professional associations offer their services as arbitrators. Typically, parties' lawyers will select the arbitrator based upon the particular type of the dispute and his professional background. In complex and highly technical cases, often an arbitrator who is knowledgeable in that field is chosen. Usually, fees are charged.

Some courts offer court-sponsored, nonbinding arbitration and have specific procedural rules to follow.

There are two types of arbitration depending on the process followed: institutional arbitration and ad hoc arbitration.

Various arbitral institutions around the world supervise and administer arbitrations. These institutions typically have a formal set of procedures and arbitration rules that disputing parties have chosen to follow through the arbitration process. Most commonly, institutions are the London Court of International Arbitration (LCIA), the International Chamber of Commerce (ICC), and the Dubai International Arbitration Centre (DIAC).

In ad hoc arbitration,[8] *the disputing parties are responsible for determining and agreeing on their own arbitration procedures, without the administration of an arbitration court.*

On the other hand, the most known types of arbitration are commercial and investment arbitration. It is important at this point to separate those two types of arbitration and describe their main differences.

This process is used for solving an investment dispute, which is a dispute between a foreign investor and a host state that relates to an investment made in the territory of the host state.

Investment arbitration is different from commercial arbitration. Commercial arbitration[9] mostly concerns a contractual agreement, whereas investment arbitration may be based either on (a) an investment treaty, either multi (NAFTA-ECT e.t.c.) - or bilateral (BIT), (b) the host State's national investment law, which often provides for protection of foreign investors or (c) in certain circumstances, an investment agreement. *Also, In commercial arbitration, the arbitral tribunal judges decides upon the contract between the parties, i.e. its conclusion, performance and termination, whereas in investment arbitration, the arbitral tribunal makes findings on the host State's behaviour towards a foreign investor.*[10]

2. In Particular: Investment Arbitration in Energy Disputes

The energy sector is a standout amongst essential parts of the worldwide investment regime. Energy deals with both downstream and upstream enterprises. Therefore, foreign investors support many investments in the energy sector. Due to the above,

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[8] See *A basic guide to international arbitration* published by Norton Rose Fulbright (Law firm), p.8. Available online at http://www.nortonrosefulbright.com/files/arbitration-a-guide-to-international-arbitration-26050.pdf

[9] See Margharet L. Moses «The Principles and Practice of International Commercial Arbitration» Cambridge University Press, p. 1-9

[10] See *Lise Johnson & Oleksandr Volkov, INVESTOR-STATE CONTRACTS, HOST-STATE "COMMITMENTS" AND THE MYTH OF STABILITY IN INTERNATIONAL LAW p. 13-19*

keeping in mind the end goal to comprehend vitality ventures, international investment law and energy need to collaborate with each other.[11]

The energy sector works in a highly complex and technical environment, hence the investors prefer arbitration as a solution. Contracts in the energy sector, be it oil and gas, electricity, the wind or solar, now have arbitration clauses that steer disputes to the venue of binding arbitration instead of litigation.

The investments regarding energy sector in developing or underdeveloped countries are made by multinational enterprises. So, these enterprises face risks regarding the legal system of the invested country. These risks are not necessarily those inherent in the investment, but rather the risks an investor runs in other countries as a result of interference by local governments, import and export restrictions, political unrest—and even war. What are an investor's remedies if new legislation in the host state renders an investment worthless? Or if the property is damaged, seized or even destroyed because of political riots, such as what has taken place in Egypt, Libya and Syria? Or if a host state, unexpectedly revokes a licence, thus preventing the investor from doing business any further, ending up in huge losses? Or if a host state government expropriates the investor's business without a prompt compensation?

Ordinarily, there is no contractual relationship between an investor and the local government.[12] This makes it difficult, if not impossible, for an individual or company to pursue a contractual claim in the local courts and the State Responsibility clause, always, offers protection to the State through the principle of International Law. As a result, the investors prefer as a dispute settlement method the road of the international investment arbitration, which provides them with an equal, effective and rapid dispute settlement concerning their investments.[13]

Investment arbitration in energy disputes functions under a legal framework that comes up from investment treaties.Investment treaties can take different forms. They can be multilateral treaties. They can be bilateral treaties. They can be free trade

[11] See *Ozge Varis,* International Energy Investments: Tracking the Legal Concept, Copyright 2014: Groningen Journal of International Law. Vol. 2, No.1: Energy and Environmental Law
[12] See V. Inbavijayan and Kirthi Jayakumar «*ARBITRATION AND INVESTMENTS – INITIAL FOCUS*» published by Indian Journal of Arbitration Law, p.39-45

agreements like NAFTA. They can be treaties specified in one sector like the Energy Charter Treaty, which focuses on energy disputes.

CHAPTER III: Investment Arbitration under the Energy Charter Treaty

a) Overview of the Energy Charter Treaty

The main goal of the Energy Charter Treaty ("ECT" or the "Treaty") is to provide the proper environment by means of rules and measures designed to create a ΄level playing field΄ for energy sector investments, liberalise trade and investment flows in the energy sector and minimises the risks associated with energy-related trade and investments.The ECT[14] is a significant multilateral instrument for the promotion of cooperation in the energy sector.

The end of Cold War came up with an opportunity for collaboration in the energy sector among the states of Europe and Asia. On the one hand countries independent from the Union of Soviet Socialist Republics that they were rich in energy supplies, on the other hand, the countries of Western Europe were trying to diversify their energy sources, therefore the Energy Charter process was born [15]. In June 1990 Dutch Prime Minister Ruud Lubbers launches the proposal for a European Energy Community at a European Council meeting in Dublin. He suggested the idea of a "European Energy Community" to promote East-West cooperation in the energy sector[16]. These efforts culminated in the adoption of a political declaration (the Energy Charter of 1991) and in the negotiation of a multilateral treaty (the Energy Charter Treaty of 1994). Moreover, the Contracting Parties adopted the International Energy Charter on 21 May 2015, a non-binding political declaration seeking to strengthen regional cooperation in the energy market.

[13] See «INVESTMENT ARBITRATION THE ROLE OF BILATERAL INVESTMENT TREATIES» published by Houthoff Buruma(Law frim), p. 9-11
[14] See the official site of ECT http://www.energycharter.org/
[15] See Graham Coop, 'The Energy Charter Treaty: More than a MIT' in C Ribeiro, Investment Arbitration and the Energy Charter Treaty, p. 4–9.
[16] See the Final Act of the European Energy Charter Conference

Fifty-two European and Asian countries have signed the Energy Charter Treaty[17]. All EU states are individual signatories, but the Treaty has also been signed collectively by the European Community and Euratom so the total number of parties to the Treaty is fifty-four.Of these fifty-four, all have ratified the Treaty apart from five. These countries are Australia, Belarus, Iceland, Norway, and the Russian Federation. Belarus and the Russian Federation[18] have accepted the provisional application of the Treaty, pending ratification.

With its current membership, the Energy Charter has a natural goal on the evolving Eurasian energy market, including the Mediterranean region, the Middle East and North Africa. Although the Treaty was conceived as a European initiative with a focus on 'East-West' cooperation, the scope of the Energy Charter is now considerably broader. Pakistan, China, Korea, Iran and Association of South-East Asian Nations have all taken on observer status in recent years.

According to Article 2 of the ECT, the purpose of the Treaty is to '*establish a legal framework in order to promote long-term cooperation in the energy field, based on complementarities and mutual benefits, in accordance with the objectives and principles of the Energy Charter'*. It is a milestone in international energy co-operation. By creating a stable, comprehensive and non-discriminatory legal foundation for cross-border energy relations, the ECT reduces political risks associated with economic activities in transition economies. It creates an economic alliance between countries with different cultural, economic and legal backgrounds, but all united in their commitment to achieving the following common goals:

- Offering to the investor's protection through international dispute settlement and clauses such as MFN, expropriation, National Treatment, umbrella clauses, FPS

[17] See Emmanuel Gaillard, *How does the so-called fork-in-theroad' provision in Article 26(3)(b)(i) of the Energy Charter Treaty work? Why did the United States decline to sign the Energy Charter Treaty*?, in INVESTMENT PROTECTION AND THE ENERGY CHARTER TREATY 215

[18] *"On 20 August 2009 the Russian Federation has officially informed the Depository that it did not intend to become a Contracting Party to the Energy Charter Treaty (…). In accordance with Article 45(3(a)) of the Energy Charter Treaty, such notification results in Russia's termination of its provisional application of the ECT (…) upon expiration of 60 calendar days from the date on which the notification is received by the Depository »* - ECT Secretariat, Also see L. E. Peterson, Italy Follows Russia in Withdrawing from Energy Charter Treaty, but for Surprising Reason, International Arbitration Reporter, 17 April 2015,

- Limiting the risk of investing in a developing country
- Enhancing energy efficiency
- Providing energy security
- Energy products trading, establishing a legal framework similar to WTO rules.

To date, 96 cases have been brought by investors to international arbitration under the ECT.[19] Some of these cases are still pending[20], and others have been settled by the parties.

b) Investments and Investors under the ECT

All treaties that aim for the protection of foreign investment define the investments and investors that qualify for that protection. There are no de facto definitions, hence the meaning that each treaty gives to these terms contributes to the treaty interpretation and the jurisdiction of the arbitral tribunals.

[19] See some of the cases: No 126/2003 Petrobart Ltd. (Gibraltar) v Kyrgyzstan; ICSID Case No ARB/04/10 Alstom Power Italia SpA, Alstom SpA (Italy) v Mongolia; Yukos Universal Ltd. (UK—Isle of Man) v Russian Federation (UNCITRAL Arbitration Rules); Hulley Enterprises Ltd. (Cyprus) v Russian Federation (UNCITRAL Arbitration Rules); Veteran Petroleum Trust (Cyprus) v Russian Federation (UNCITRAL Arbitration Rules); ICSID Case No ARB/05/18 Ioannis Kardossopoulos (Greece) v Georgia; Amto (Latvia) v Ukraine (SCC); ICSID Case No ARB/05/24 Hrvatska Elektropriveda d.d. (HEP) (Croatia) v Republic of Slovenia; ICSID Case No ARB/06/8 Libananco Holdings Co. Limited (Cyprus) v Republic of Turkey; ICSID Case No ARB/06/15 Azpetrol International Holdings B.V., Azpetrol Group B.V. and Azpetrol Oil Services Group B.V. (Netherlands) v Azerbaijan; ICSID Case No ARB(AF)/06/2 Cementownia ''Nowa Huta'' S.A. (Poland) v Republic of Turkey; Europe Cement Investment and Trade S.A. (Poland) v the Republic of Turkey (ICSID); ICSID Case No ARB/ 07/14 Liman Caspian Oil B.V. (the Netherlands) and NCL Dutch Investment B.V. (the Netherlands) v Republic of Kazakhstan; ICSID Case No ARB/07/19 Electrabel S.A. v Republic of Hungary; ICSID Case No ARB/07/22 AES Summit Generation Limited and AES-Tisza Er o 00 mu 00 Kft. v Republic of Hungary; Mercuria Energy Group Ltd. v Republic of Poland (Arbitration Institute of the SCC); ICSID Case No ARB/08/13 Alapli Elektrik B.V. v Republic of Turkey,
ICSID Case No. ARB/15/42Hydro Energy 1 S.à r.l. and Hydroxana Sweden AB v. Spain, ICSID Case No. ARB/15/44 Watkins Holdings S.à r.l. and others v. Spain

[20] Yukos Universal Ltd. (UK—Isle of Man) v Russian Federation (UNCITRAL Arbitration Rules); Hulley Enterprises Ltd. (Cyprus) v Russian Federation (UNCITRAL Arbitration Rules); Veteran Petroleum Trust (Cyprus) v Russian Federation (UNCITRAL Arbitration Rules); ICSID Case No ARB/05/18 Ioannis Kardossopoulos (Greece) v Georgia; ICSID Case No ARB/05/24 Hrvatska Elektropriveda d.d. (HEP) (Croatia) v Republic of Slovenia; ICSID Case No ARB/06/8 Libananco Holdings Co. Limited (Cyprus) v Republic of Turkey; ICSID Case No ARB/06/15 Azpetrol International Holdings B.V, Azpetrol Group B.V. and Azpetrol Oil Services Group B.V. (Netherlands) v Azerbaijan;

The definition "Investment" is given at Article l(6) of the ECT. This provision provides an in-depth catalogue of the types of capital that could be recognised as an investment. The Article l(6) reads as follows:

"'Investment' means every kind of asset, owned or controlled directly or indirectly by an Investor and includes:

(a) tangible and intangible, and movable and immovable, property, and any property rights such as leases, mortgages, liens, and pledges

(b) a company or business enterprise, or shares, stock, or other forms of equity participation in a company or business enterprise, and bonds and other debt of a company or business enterprise

(c) claims to money and claims to performance pursuant to contract having an economic value and associated with an Investment

(d) intellectual property

(e) returns

(f) any right conferred by law or contract or by virtue of any licenses and permits granted pursuant to law to undertake any Economic Activity in the Energy Sector.

A change in the form in which assets are invested does not affect their character as investments and the term "Investment" includes all investments, whether existing at or made after the later of the date of entry into force of this Treaty for the Contracting Party of the Investor making the investment and that for the Contracting Party in the Area of which the investment is made (hereinafter referred to as the "Effective Date") provided that the Treaty shall only apply to matters affecting such investments after the Effective Date.

"Investment" refers to any investment associated with an Economic Activity in the Energy Sector and to investments or classes of investments designated by a Contracting Party in its Area as "Charter efficiency projects" and so notified to the Secretariat.

The main limiting factor in Article 1(6) of the ECT is that it covers only investments *"associated with an Economic Activity in the Energy Sector."* Article 1(5) defines Economic Activity in the Energy Sector as *"an economic activity concerning the exploration, extraction, refining, production, storage, land transport, transmission, distribution, trade, marketing, or sale of Energy Materials and Products except those included in Annex N1, or concerning the distribution of heat to multiple premises."*[21]

The extensive sphere of the definition of investments under Article l(6) of the ECT is further regulated by the fact that every kind of asset may be "owned or controlled directly or indirectly" by an investor. The Treaty offers guidance as to the context of "control" and its content as "control in fact" in the Understandings to the Final Act of the European Energy Charter Conference.[22]

There is a discussion on whether the catalogue of possibilities mentioned in Article 1(6) of the ECT is a limited list, or whether other investments can also be included in the list on analogous grounds. In this sense, the tribunal in the Yukos arbitrations read Article 1 (6)(b) of the ECT as containing the widest possible definition of an interest in a company with no indication that the drafters of the ECT intended to

[21] The Final Act of the European Energy Charter Conference provides the following examples of "economic activity in the energy sector":
(i) prospecting and exploration for, and extraction of, e.g., oil, gas, coal and uranium;
(ii) construction and operation of power generation facilities, including those powered by wind and other renewable energy sources;
(iii) land transportation, distribution, storage and supply of Energy Materials and Products, e.g., by way of transmission and distribution grids and pipelines or dedicated rail lines, and construction of facilities for such, including the laying of oil, gas, and coal-slurry pipelines;
(iv) removal and disposal of wastes from energy related facilities such as power stations, including radioactive wastes from nuclear power stations;
(v) decommissioning of energy related facilities, including oil rigs, oil refineries and power generating plants;
(vi) marketing and sale of, and trade in Energy Materials and Products, e.g., retail sales of gasoline; and
(vii) research, consulting, planning, management and design activities related to the activities mentioned above, including those aimed at Improving Energy Efficiency. 15

[22] The Understandings with respect to Article l(6) reads as follows: *"For greater clarity as to whether an Investment made in the Area of one Contracting Party is controlled, directly or indirectly, by an Investor of any other Contracting Party, control of an Investment means control in fact, determined after an examination of the actual circumstances in each situation. In any such examination, all relevant factors should be considered, including the Investor's (a) financial interest, including equity interest, in the Investment; (b) ability to exercise substantial influence over the management and operation of the Investment; and (c) ability to exercise substantial influence over the selection of members of the board of directors or any other managing body. Where there is doubt as to whether an Investor controls, directly or indirectly, an Investment, an Investor claiming such control has the burden of proof that such control exists."*

limit, ownership to *"beneficial"* ownership, as suggested by the Russian Federation. The tribunal rejected the Russian Federation's arguments that the shareholdings in Yukos did not qualify as protected "Investment." It also noted that *"the definition of investment in Article 1 (6) of the ECT does not include any additional requirement with regard to the origin of capital or the necessity of an injection of foreign capital."*[23]

In conclusion, it can be a complex process to determine whether a specific economic activity can be considered as an investment under the provisions set out by the ECT, even though it is highlighted that the concept of investment as defined by the ECT is particularly broad[24].

The definition of an "investor" under the ECT is provided at Article l(7) in the following terms:

Investor' means:

(a) with respect to a Contracting party: (i) a natural person having the citizenship or nationality of or who is permanently residing in that Contracting Party in accordance with its applicable law;

(ii) a company or other organisation organised in accordance with the law applicable in that Contracting Party; (b) with respect to a 'third state', a natural person, company or other organisation which fulfils, mutatis mutandis, the conditions specified in subparagraph (a) for a Contracting Party."

According to the general principles of Public International law, the nationality of a person is regulated by the domestic law of each State. Accordingly, for a natural person to benefit from the Treaty, he or she must either be a citizen, national, or permanent resident of a Contracting Party. For a corporation to qualify for Treaty benefits, it need only be organised under the laws of a Contracting State. Article 1(7) imposes no further requirements with respect to shareholding, management, siege social or location of its business activities. The ECT offers a broader coverage by

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[23] See Yukos Universal Ltd. (UK - Isle of Man) v. Russian Federation (Ad hoc UNCITRAL Arbitration Rules)

[24] See Gaillard, E., «Investments and Investors covered by the Energy Charter Treaty» en Ribeiro C., Investment Arbitration and the Energy Charter Treaty, Jurisnet LLC, New York, 2006, page 59.

simply requiring that a legal entity is "organised" in accordance with the law applicable in a Contracting State.

c) Settlement of Disputes between an Investor and a Contracting Party

The promotion and protection of energy investments and investment dispute resolution are the foundations of the ECT structure. The investment protection provisions of the ECT, are structured in a way to provide investors with a minimum level of protection, according to international standards. As for investment dispute resolution, the ECT offers three specific paths: (i) ICSID arbitrations[25] (ii) arbitration under the auspices of the Stockholm Chamber of Commerce («SCC»); and (iii) ad hoc arbitration under the UNCITRAL[26] Arbitration Rules.

A typical dispute under the ECT arises when an ECT Signatory state breaches a number of its obligations under the ECT, causing substantial damage to an investor that is coming from another ECT Signatory State. Any one of the investors may, therefore, bring an arbitration under the auspices of the ECT in order to receive: (i) a declaration stating that a breach of obligation occurred and (ii) reimbursement from the ECT State for losses suffered as a result of infringement of the ECT.

The importance of determining the scope and meaning of the above terms — «protected Investment» and «Investor»— is that protection under the ECT is limited to specific cases, in accordance with Article 26 (1) of the ECT which covers the settlement of disputes between an Investor and a Contracting Party. In particular, this protection is only granted if all of the following requirements have been met. This means a dispute may be:

(i) *«… between a Contracting Party…»*
(ii) *Against «… an investor of another Contracting Party…»*
(iii) *«… relating to an Investment of the latter in the area of the former»*

[25] International Centre for Settlement of Investment Disputes (ICSID)

(iv) «... which concern an alleged breach of an obligation of the former under Part III [of the ECT] [...]»

Firstly, it is considered appropriate to analyse the definitions and purpose of a «Contracting Party» in contrast to a «third state» and an «Investor» of a «Contracting Party» under the ECT.

As a starting point, it is essential to get familiar with the difference between a Contracting Party and a third state. A Contracting Party is a state which has signed and ratified the ECT. In this regard, it should be noted that it is possible to accept to apply the ECT provisionally, creating different circumstances for different countries, for example in the case of Belarus. It is also possible to apply the ECT provisionally and subsequently decide to stop its application, for example in the case of the Russian Federation as of 2009.

For the purposes of the ECT, a third state[27] is a state outside the scope of Article 26 of the ECT: a third state is neither a Contracting Party nor an Investor. For example, a company incorporated under the laws of a state which has not signed the ECT (such as the United States [28]) cannot initiate an arbitration under the ECT.

Given that the dispute resolution mechanisms of the ECT are reserved for disputes between a Contracting Party and Investors of another Contracting Party, the ECT expressly excludes the following scenarios:

a) A dispute between a third state which is not a Contracting Party
b) A dispute involving an Investor which is a national of a third state
c) A dispute involving an Investor which is a national of the same Contracting Party against which the claim has been brought. In order to confirm that an Investor (never a natural person) is a national of a Contracting Party, it is

[26] The United Nations Commission on International Trade Law (UNCITRAL). The revised UNCITRAL Rules, which came into force on 1 April 2014, will apply to all future ECT disputes
[27] See Article 1 (7) of the ECT: *«[…] (b) with respect to a "third state", a natural person, company or other organization which fulfils, mutatis mutandis, the conditions specified in subparagraph (a) for a Contracting Party.»*
[28] The United States, Canada and China hold an observer status, and therefore, the ECT does not bind them.

necessary to confirm that the Investor is incorporated under the laws of that particular Contracting Party.

Even if the requirements established in Article 26 of the ECT are met, protection under the ECT is not always provided. Article 17 ECT, is called the «denial of benefits». The denial of benefits clause does not function as a denial of all benefits to an investor but is expressly limited to a denial of the advantages related to the substantial protection under Part III of the ECT.

In accordance with this Article, a Contracting Party is entitled to deny protection under the ECT to Investors if they are

(1) a legal entity if citizens or nationals of a third state own or control such entity and if that entity has no substantial business activities in the Area of the Contracting Party in which it is organised; or

(2) an Investment, if the denying Contracting Party establishes that such Investment is an Investment of an Investor of a third state with or as to which the denying Contracting Party: (a) does not maintain a diplomatic relationship; or (b) adopts or maintains measures that: (i) prohibit transactions with Investors of that state; or (ii) would be violated or circumvented if the benefits of this Part were accorded to Investors of that state or to their Investments.

In addition, it must be considered a contrasting case, in which, in a conflict between an Investor and the same Contracting Party in which it is incorporated, an Investor may qualify for protection under the ECT. Such a case may only exist under the ICSID arbitration forum. In particular, under Article 25(2) (b)[29] of the ICSID Convention, which is the cornerstone for the establishment of jurisdiction, there may be an agreement between a local company controlled by a foreign investor and a host state. Under such an agreement, the local company will have access to protection

[29] See Article 25(2)(b) of the ICSID Convention: *«National of another Contracting State» means: (…) b) any juridical person which had the nationality of a Contracting State other than the State party to the dispute on the date on which the parties consented to submit such dispute to conciliation or arbitration and any juridical person which had the nationality of the Contracting party to the dispute on that date and which, because of foreign control, the parties have agreed should be treated as a national of another Contracting State for the purposes of this Convention.»*

under the ICSID. This allows for a departure from the principle of the place of incorporation, in favour of foreign control.

Since ICSDI is among the selected arbitration institutions under the ECT, theRE has specifically provided a similar rule to that already set out by the ICSID. In Article 26(7), the ECT states that: *«An Investor other than a natural person which has the nationality of a Contracting Party to the dispute on the date of the consent in writing referred to in paragraph (4) and which, before a dispute between it and that Contracting Party arises, is controlled by Investors of another Contacting Party, shall for the purpose of Article 25(2)(b) of the ICSID Convention be treated as a "national of another Contracting State" [...].»*

Therefore, in the event that a company is able to prove that it is controlled by Investors of another Contracting Party, it would be able to file an arbitration claim under the ICSID mechanisms. In this sense, the concept of the control means either that (i) Investors holds a certain percentage of participation in that company or that (ii) Investors have a decisive influence on the Investment management of the company.

CHAPTER IV: Investment Arbitration under BITs

a) What is a BIT;

When an investor decides on where to invest internationally, and where to set up the structure for the foreign investment, the investor's attention usually focuses on a comparison of the tax rules of the various countries under consideration. Due to this reason, if a domestic administration inadequately intervenes in the investment and a damage appears, whether an investment treaty is applicable and provides for recovery is largely a matter of chance. However, it would be cautious for an investor and its counsel, when considering where to set up the investment and where to place the structure for the foreign investment, to reconsider whether an international investment treaty protects the investment and what the requirements for this would

be. As a result, there was a need for a specific international agreement for the protection of the investment.

International agreements between countries granting corporation and private persons special rights and legal protections at the time of investment in a foreign country that is known as a Host State, constitute Bilateral Investment Treaties (BITs)[30]. BITs determine terms and conditions for investing in one country by private companies and individuals of another country by private companies and individuals of another country. Promotion of investments in the Host States is BIT main purpose. BITs are designed to protect, promote and facilitate foreign investment and constitute to date the most widely used instrument for these purposes.

On November 25, 1959, the world's first BIT between Pakistan and Germany, was established. Countries such as France and Switzerland rapidly followed suit.[31] The network of BITs grew significantly throughout the 1970s, prompted in large measure by a defensive impulse on the part of home country governments in the wake of the increasing number of expropriations and nationalisations, notably in Latin America. BITs have traditionally been negotiated between developing countries seeking to attract international investment and developed countries as the principal homes to foreign investors. Developing countries, as hosts to foreign direct investment (FDI), concluded BITs in order to create a favourable climate and in some cases to become eligible to participate in political risk insurance programs organised by capital exporting countries.[32]

The content of BITs has become increasingly standardised over the years. In addition, as the custom was used as a source of the international law, the content influence regulations at a domestic level, particularly during the last 15 years. In particular, there are differences between the provisions of BIT signed some decades ago and the more recent ones.[33]

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[30] See «INVESTMENT ARBITRATION THE ROLE OF BILATERAL INVESTMENT TREATIES» published by Houthoff Buruma(Law frim), p. 9-11

[31] See UNCTAD «BILATERAL INVESTMENT TREATIES 1995–2006:TRENDS IN INVESTMENT RULEMAKING» New York and Geneva, 2007

[32] See UNCTAD «Recent Developments in International Investment Agreements», New York and Geneva, 2009 and Mary Hallward-Driemeier « Do Bilateral Investment Treaties Attract FDI? Only a bit…and they could bite» June 2003, p.22-23

[33] See UNCTAD «Bilateral Investment Agreements in Mid-1990's» Geneva:United Nations (1998)

Nowadays, it is surprising that more and more developing countries tend to sign and ratify this kind of agreements since it is an efficient way of attracting investors. In terms of content, their practice does not seem to depart from the traditional BITs between developed and developing countries. From a legal perspective, the increasingly homogeneous state practice means that it is nowadays possible to argue that '*the BIT movement has moved beyond lex species (or better, legs specials) to the level of customary law effective even for non-signatories')*[34]

b) Protections under BIT – Interpretation of a BIT and Determination of its Scope

The purpose of a BIT, which is a treaty between two countries, is to promote foreign investments between the two countries and to offer protection to investors from one country investing in the other. For the success of this goal, a BIT's content includes obligatory rules, clauses, on the treatment of incoming investments.

A BIT is normally limited in length, in most cases encompassing not more than 15 articles. Most countries have developed a model BIT and they use it as a ground for negotiation. In general, most BITs share a certain number of standard, recurring provisions.

Commonly, the preamble of the BIT states its purpose and goal, which is to enhance the economic cooperation between the parties and to set up a framework for the investors' protection. In general, a BIT affords eligible investors certain minimum protection of their investments in a host state. If a host state breaches the substantive protection-related provision in the BIT, in a way affecting the investor, the latter may commence proceedings directly against the state.

Although the wording and provisions in the various BITs differ, the treaties generally include standard clauses relating to substantive protection under international legal principles. These clauses define the scope of the protection provided by a BIT.

[34] See A. Lowenfeld «Investment Agreements and International Law» Columbia Journal of Transnational Law, P.42,123-131,129

1. Expropriation without compensation

The rules concerning the expropriation of foreign property are the cornerstone and of great importance for the investors. The host state, though, according to the principle of territorial sovereignty has the right to expropriate foreign property under certain requirements. The host state can take an investment project for public purposes and must be accompanied by prompt, adequate and effective compensation. In addition, the measure should not be arbitrary and discriminatory.

At a basic level, we can separate two different categories of expropriation. Direct or Indirect.

Direct expropriation nowadays is a rare phenomenon. Generally, direct expropriation is a drastic action by the host state that transfers title of the project from the investors to the state. This act in the past used to attract negative publicity and harm the state's reputation.

Indirect expropriation is less specific. As GC Christie[35] surmised:

- *"a state may expropriate property, where it interferes with it, even though the state expressly disclaims any such intention, and*
- *even though a state may not purport to interfere with rights to property, it may, by its actions render those rights so useless that it will be deemed to have expropriated them."*

Investor's right to prompt, adequate and effective compensation is independent of whether an expropriation is "lawful" or "unlawful". Compensation is a requirement for the legality of the expropriation in the first case, while in the latter, equals to damages for the loss suffered by the investor, resulting of unlawful expropriation.[36]

2. Fair and equitable treatment

Almost all BITs provide "fair and equitable treatment" to foreign investors. Nowadays it is the most regularly claim in investment disputes. Stephan Schill[37] has said, "*fair and equitable treatment can be understood as embodying the rule of law*

[35] G. C. CHRISTIE is a professor in School of Law at University of Minnesota
[36] See A. Sheppard «*The Distinction between Lawful and Unlawful Expropriation*» in C Ribeiro (ed) Investment Arbitration and the Energy Charter Treaty 169-199
[37] Stephan Schill is a professor of Investment Law at the University of Amsterdam

as a standard that the legal systems of host states have to embrace in their treatment of foreign investors." Host states supposed to provide a transparent and predictable regulatory framework for the investment and respect the legitimate expectations upon which the investors relied when they made their investment. The cases on fair and equitable treatment fall into two broad categories. The first category concerns the treatment of investors by the courts of the host state. In *Azinian v.Mexico*, a claim brought under NAFTA, the tribunal accepted that in principle the host state could be liable for the decisions of its courts, *especially (i) if the courts refused to entertain the suit, (ii) subjected the suit to undue delay, (iii) administered justice in an inadequate way, or (iv) if there was a clear and malicious misapplication of the law*.[38] The second, more important category deals with decisions issued by administrations authorities. The majority of such cases concern with licenses or the with the granting or withholding of investment licenses or a fundamental change in the law affecting the investment climate.

3. *Full protection and security*

The principle of fair and equitable treatment is associated to that of full protection and security. It refers to protection towards physical violence, especially acts that are unwarranted and abusive. For example, if state authorities and police powers do not protect an investment during a rebellion or a seize of the property, then these acts may affect the rights of the investor.

In more recent arbitration cases, such as the *Siemens v. Argentina*[39], arbitration based on the Germany-Argentina BIT, the tribunal confirmed that *the standard of fair and equitable treatment extends beyond physical protection to the protection against infringements of the investor's rights by operation of laws and regulations of the host state.*

4. *Discriminatory or arbitrary measures*

Another classical standard provision in investment treaties is the exclusion of arbitrary behaviour. This principle applies if an investor is treated differently from other investors in similar or comparable circumstances. In general, host states act

[38] See *Azinian, Davitian, & Baca v. Mexico*, ICSID Case No. ARB (AF)/97/2 (NAFTA), Award 1 November 1999, available at: <http://italaw.com/documents/Azinian-English.pdf>.
[39] See *Siemens v. Argentina*, ICSID Case No. ARB/02/8, Decision on Jurisdiction, (Aug. 3, 2004).

unreasonably or discriminatorily if rules of law are de facto violated or if an investor has no access to due process. In addition, another category of arbitrary measure is the justification of the measure. If there are reasons different from those that legislator or the administration states.

5. Most favoured-nation-treatment

The simple intention of the MFN clause in treaties is to assure that the signatory parties will behave each other in a way at least as favourable as they act third parties. A regular result of an MFN clause in a BIT is to broaden the claims of the investor. For example, in *Maffezini v. Spain*, which was to be ruled by the Argentina-Spain BIT, the Argentinean investor initiate the arbitration proceedings against Spain, even though he had not previously submitted the dispute to the Spanish courts as required by the BIT. The Argentinean investor successfully contended, that by invoking the most favoured nation treatment clause, he could bring those claims under the Spain-Chile BIT, which did not require investors to first file a claim in the national court of the host state[40]. It remains a problematic issue, though, if the MFN clause covers both procedural and substantive rules.

6. Right to repatriate investment and returns

Many BITs impose an obligation on the host state to freely permit the transfer of funds relating to investments into and out of the host state. An investor will typically need to import funds into the host state to start a production facility or to expand its business. Repatriation of capital, including profits, into the home state or another country will often be the major business purpose of the investment. However, a host state may find that this is not at its interests; hence, it may regulate the control of large currency transfers in and out of its territory. Due to the capital inflows, the domestic economic markets may appear some insecurity. For this reason, BITs invariably include clauses covering the free transfer of funds related to investments.

7. Protection against breach of a legal obligation

The final standard clause recurring in BITs is a general "umbrella clause" that obligates a host state to comply with its obligations regarding the investments of

[40] See *Maffeziniv. Spain*, ICSID Case No. ARB/97/7, Award on Jurisdiction, 25 January 2000, available at: <http://italaw.com/documents/Maffezini-Jurisdiction-English_001.pdf>.

individuals and companies from the other country. Investors often rely on an 'umbrella clause' as an overall provision to pursue claims when a host state's actions do not otherwise breach the BIT. 'Umbrella clauses' are usually broadly written to "upgrade" the contractual disputes into breaches of the BIT.

It is calculated that, out of the 2,500 or more BITs in force, almost 40% include an umbrella clause. A review of the practices of the various states does not indicate a uniform approach to the treatment of these clauses. Switzerland, Netherlands, United Kingdom and Germany often include umbrella clauses in their BITs; however, France, Australia and Japan include umbrella clauses in only a minority of their BITs.[41]

c) Arbitration under international bilateral investment agreements

Typically, where there is a bilateral investment treaty, investors have the freedom of choice to initiate arbitration procedure in any of the arbitral institutions described in the treaty.

Most BITs allow investors to bring their disputes before one of several arbitration institutions, such as:

- **INTERNATIONAL CENTER FOR THE SETTLEMENT OF INVESTMENT DISPUTES (ICSID)**
- **INTERNATIONAL CHAMBER OF COMMERCE INTERNATIONAL COURT OF ARBITRATION (ICC)**
- **STOCKHOLM CHAMBER OF COMMERCE (SCC)**

Before a Claimant initiates the proceedings, usually there is a cooling-off period where the parties should try to reach a mutual agreement. For example, the BIT between the Netherlands and Peru provides:

"Any dispute between one Contracting Party and a national of the other Contracting Party, concerning an investment of the latter in the territory of the former, shall, if

possible be settled amicably. If such a dispute cannot be settled within a period of 3 months from the date either party requested amicable settlement, each Contracting Party hereby consents to submit any legal dispute arising[to arbitration].”[42]

Generally, this cooling-off period will begin after the investor sends a “trigger letter” to the highest authorities of the host state, such as the head of state or the minister of the ministry dealing with the investment. The letter will briefly state the facts and the nature of the dispute and request the host state to enter into negotiations. If the negotiations are not successful, sometimes because the host state will not answer the request, the investor can start the procedure.

d) Relationship BIT- ECT

Even though the goal of this thesis is to deal with ECT, it should include a few remarks about the relationship among them. Both of them are instruments designed for the protection and enhancing international investment. Sometimes they do legislate the same provisions and the risk of parallel proceedings may appear. However, some essential differences separate them. The ECT is a specialised treaty for investment disputes in the energy sector, whereas the BITs cover any dispute including energy disputes. They may both offer an investor-state arbitration clause but the ECT contains (Art.17) a denials of benefits provision that could be an obstacle for the arbitral procedure, whereas BITs do not include provisions like this. Therefore, it is arguable that an investor should initiate the arbitral proceedings under the BIT provisions in order to avoid such problems. In addition, an investor could seek redress under the BIT in order to bypass the precedent of the previous rulings of the provisions under the ECT. During my research for this subject, I came up with questions that need to address since there is not a concluding regime in the arbitration community about the parallel proceedings. Is it possible for a tribunal to examine simultaneously allegations of breach of the ECT and BIT provisions? My thought is negative about this. The reason is the legal basis which a tribunal acquires its jurisdiction. An ECT tribunal derives its legitimacy under Art. 26, whereas a BIT tribunal is constituted under an article of the BIT. This means that an ECT tribunal cannot find a violation of a BIT and backwards. Due to the above, a respondent could

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[41] See UNCTAD “*Bilateral Investment Treaties in the Mid- 1990s*”, 1998, p. 56

[42] See Bilateral Investment Treaty between the Netherlands and Peru

easily object, which would end in denial of jurisdiction under one of the both instruments.

CHAPTER V: Cases

As previously mentioned, the investment protection regime of the ECT has been in force since 1998, but the number of awards rendered so far is rather limited. Due to the limited number of awards, it is not yet possible to identify any clear trends in ECT cases. However, in particular, the awards in Petrobart and Plama raise some jurisdictional issues of general interest, which will be discussed. As to the merits, the awards in Nykomb and Petrobart involve questions concerning the standard of compensation in case of other violations of the ECT than expropriation

I. Nykomb Synergetics Technology Holding AB v the Republic of Latvia

Summary[43]

Nykomb, a company with a Swedish nationality, bought a Latvian subsidiary (Windau) in order to participate in the business of supplying and producing electric power in the territory of Latvia. Windau in 1997 came into a contractual agreement with Latvenergo, which was possessed by the State and it was the only distributor and purchaser of electricity in the national grid. According to the agreement, the Latvian subsidiary had to build a power plant and on the other side, Latvenergo would buy the electric power from Windau at a price composed of two elements – the general tariff and a multiplier. Latvian laws defined both these elements. When the contract was signed the domestic law had a provision that a “double tariff” to be paid as remuneration the first eight years that the plant would function.

Nonetheless, Latvia’s legislator body passed a new law in 1998 and a dispute began the moment the construction was finished, in 1999. The new provision rejected the “double tariff” and applied a 0,75 tariff. The Swedish company Nykomb, which was the investor in our case, had the right to initiate under the provisions of the ECT

[43] The full text of the award is available in K Hober, “Investment Arbitration in Eastern Europe: In Search of a Definition of Expropriation”(Juris Net, LLC, Huntington 2007) Appendix 11. For a complete analysis of the case, see Hober, “Investment Arbitration in Eastern Europe 202; and T Walde and K Hober, ‘The First Energy Charter Award’ (2005) 22J Int’l Arb 83–103

arbitral proceedings and this happened. The claims were: the refusal to pay the double tariff breaches the provisions of FET, discriminatory behaviour and others. The total amount that the investor argued as damages from the tariff difference reached 12,8 million US dollars. The arbitral tribunal after examining the domestic law and the contractual agreement reached at a decision that for the first 8 years the state-owned company was obliged to pay the double tariff. In addition, the arbitral tribunal decided that the act of non-payment the double tariff was attributable to the state of Latvia and it was an arbitrary and discriminatory measure since the same company had paid to two other Latvian companies the double tariff. According to the previous said, the tribunal concluded that Latvia violated the article 10 par.1 of the ECT that prohibits measures of discrimination, and it rendered its award on merits for 2,4 million US dollars. Furthermore, it decided that Latvia had to pay the double tariff amount for the next 8 years.

Comments

The case is noteworthy due to its environmental character which separates it from many others disputes that arose through investment treaties. In addition, the first ECT case is outstanding because the investor decided to invest in a subsidiary, which was organised by the domestic law of the host state.

This case discusses the matter of damages from the company that is the investor and concludes that the investment may have more damages than the investor may. As the tribunal said: *"[I]t is clear that the higher payments for electric power would not have flowed fully and directly through to Nykomb. The money would have been subject to Latvian taxes etc., would have been used to cover Windau's costs and down payments on Windau's loans etc., and disbursements to the shareholder would be subject to restrictions in Latvian company law on payment of dividends. An assessment of the Claimant's loss on or damage to its investment based directly on the reduced income flow into Windau is unfounded and must be rejected*". Although Nykomb tried to justify its claims on the theory of the economic unity of the parent investor and the investment (this term was introduced at the ICJ Barcelona Traction judgment) the tribunal rejected the theory and reduced the amount to the 1/3 of the difference.

It is clear that the arbitral tribunal chose the road of a compromise decision, so both parties of the dispute could be satisfied. As Jonas Wetterfors[44] quote "*There is no substantial reasoning for this quite surprising and "settlement-like" decision in the award, other than the conclusion of the Tribunal that damages suffered by the parent are "apparently not identical" to those suffered by the domestic investment.*"

II. Petrobart Ltd. (Gibraltar) v. Kyrgyzstan

Summary[45]

The arbitration concern the company "Petrobart Ltd" of Gibraltar and the state of Kyrgyzstan Kyrgyz based on a sales contract between Petrobart and the Kyrgyz state-owned company KGM for the purchase by the investor of 200,000 tonnes of gas condensate.

Petrobart initially delivers gas five times but got a compensation only for the first two due to the severe economic situation of KGM. Petrobart tried to solve the dispute in the domestic Bishkek Court, where it a judgment of debt for the amount of US$ 1.5 million. However, the Vice Prime Minister of the Kyrgyz Republic "demanded" the Bishkek Court not to apply the decision for three months. At the same time, he issued a decree of changing the structure of the KGM, by relocating its assets to another state- owned companies. Furthermore, KGM declared bankruptcy and there were not any assets for the investor to apply the judgment. Subsequently, Petrobart decided to initiate arbitral proceedings under the provisions of the ECT against the Kyrgyz Republic. The claim was that the acts of the Vice Prime Minister and the decree breached the provision of article 10 par.1 of stable, equitable and favourable conditions. The two parties came to an agreement for arbitration procedure only on written submissions.

After rejecting jurisdictional challenges, the arbitral tribunal stated that the Kyrgyz Republic was obliged to organise the KGM structure in a way that would protect the rights of Petrobart according to the ECT. Specifically, the act of the Vice Prime Minister had a detrimental impact on the judgment application. The Tribunal, hence

[44] Jonas Wetterfors is Partner at Hellstrom & Partners

[45] The full text of the award is available online at "http://www.energycharter.org/what-we-do/dispute-settlement/investment-dispute-settlement-cases/4-petrobart-ltd-gibraltar-v-kyrgyzstan/"

concluded that the Kyrgyz Republic violated Article 10(1) and Article 10(12) of the Treaty.

The arbitral tribunal held that replacement of assets from KGM to the other companies influenced Petrobart and there was a strong relationship between the breach of ECT and the investor's damage. The tribunal, though, faced with the problem of estimating the damages, because the submissions did not include satisfactory data for the calculation. The arbitral tribunal went on to assess the loss according to UNIDROIT Principles, with a starting point the debt judgment. However, it rejected the claims for legal expenses during the domestic legal proceedings and for lost profits that were not proved efficiently.

The Republic of Kyrgyz objected the award at the Svea Court of Appeal in Stockholm. Nonetheless, the Court of Appeal with its decision on 19 January 2007 upheld the award.[46]

Comments

One of the main issues of jurisdiction in Petrobart case was the matter of Gibraltar as an investor under the ECT provisions. During the signing of the ECT by the United Kingdom, there was a declaration under Article 45(1) that the provisional application of the treaty should apply to the United Kingdom of Great Britain and Northern Ireland and to Gibraltar. Yet, when the ECT was ratified by the UK, in the instrument of ratification referred that the ratification was in respect of the United Kingdom of Great Britain and Northern Ireland, the Bailiwick of Jersey and the Isle of Man, leaving Gibraltar outside of the scope. The tribunal, therefore, had to define whether Gibraltar was or was not a member of the ECT even though it wasn't in the instrument of ratification. The tribunal stated that there was an issue of interpretation and it had to be solved via a '*rather formal approach based on the wording of the Treaty'*, and noted that *'according to the text of the Treaty provisional application ceases if it is terminated either by a special notification under Article 45(3)(a) of the Treaty or by transition from provisional application to a corresponding and final legal commitment resulting from the entry into force of the Treaty. It could indeed be expected that the United Kingdom, if it wished the provisional application of the*

[46] See case No T 5208-05 The Republic of Kirgizistan v Petrobart Ltd (Svea Court of Appeal, Judgment of 19 January 2007

Treaty to Gibraltar to be terminated as a result of a ratification not including Gibraltar, should have made this clear by making a notification in line with Article 45(3)(a) or a declaration in some other form in connection with the ratification. In the Arbitral Tribunal's opinion, the fact that the ratification, for political or other reasons, did not include Gibraltar does not justify the conclusion that the United Kingdom intended to revoke the application of the Treaty to Gibraltar on a provisional basis'[47].In other meaning, the tribunal concluded that Gibraltar was protected under the ECT despite the instrument of ratification that did not include it. The fact that it was not there, it does not mean that it was a legal commitment for Gibraltar, meaning terminating the application in relation to Gibraltar.

In conclusion, the arbitral tribunal found a robust link among the breach of the ECT and the damage experienced by the investor Petrobart. The tribunal concluded that the total amount of damage would be more limited if there was no illegal interference by the State. It added though that it would be difficult in any case to recover the whole amount of money of the KGB. However, the arbitral tribunal denied the allegation for damages on the ground of the request of the Vice Prime Minister of non-application of the domestic decision.

III. Plama Consortium Limited v Republic of Bulgaria[48]

Plama Consortium Limited (from now on 'Plama') is a company with the Cypriot nationality, which made an investment in a Bulgarian company, Nova Plama, that had in its possession an oil refinery in Bulgaria. The investor Plama claimed that Bulgaria hindered the operation of the oil refinery in a manner that was inappropriate, breaching international law obligations under both the Energy Charter Treaty and the Cyprus Bulgaria BIT.

On 8 February 2005 the first decision of the tribunal concerning the jurisdiction concluded that it had jurisdiction only under the ECT provisions but not under the Cyprus- Bulgaria BIT.[49] In its award on the merits, the tribunal accepted Bulgaria's

[47] Petrobart Limited v. The Kyrgyz Republic, SCC Case No. 126/2003
[48]The full text of the award is available at http://www.italaw.com/cases/857
[49] The Cyprus-Bulgaria BIT only provided for jurisdiction with regard to claims of expropriation. Since Plama's claim concerned other alleged breaches of the Cyprus-Bulgaria BIT, Plama tried to rely on the MFN clause in the Cyprus-Bulgaria BIT to be able to invoke the dispute resolution clauses in other

factual allegation that Plama was guilty of misrepresentation. The next award on the merits, the tribunal found that Plama failed to present the facts since, during the negotiations for the purchase, Nova Plama thought that there were two owners of Plama. However, the private individual of Plama did nothing to inform the buyer. This attitude was contrary to provisions of Bulgarian law and public international law. The tribunal quoted that the ECT should be read in a manner persistent with the goal of enhancing respect for the rule of the law and stated the introductory note to the ECT that reads: *'[t]he fundamental aim of the Energy Charter Treaty is to strengthen the rule of law on energy issues [...]'*.

In addition, the tribunal stated that Plama's conduct was inconsistent with the principle of good faith that is part of domestic law and one of the general principles of international law. In the tribunals' thoughts, the principle of good faith incorporates responsibility for the investor to furnish the host state all the applicable and significant information regarding the investor and the investment. Even though the tribunal could not give the effect of the provisions of the ECT to Plama, it went on to examine the contentions that were presented during the procedure. After the inquiry, the tribunal concluded that the investor's claims on the merits were declined in any occasion because of the high-risk of the project.

Comments

The Tribunal concluded that the investment breached Bulgarian law and public international law, including the principle of good faith and the principle of *auditor propriam turpitudinem allegans.* The second principle is interpreted as "noone should gain profit from a wrong act attributed to himself". According to this case, means that the contractor presents false evidence during the negotiations of the contract, hence it cannot bring his claims under this contract. As Elizabeth Whitsitt[50] quoted: "*Similar to the adage originating in the English courts of equity that "he who comes to equity*

Bulgarian BITs, which gave investors the option to pursue dispute resolution for all breaches of the treaty. However, the tribunal found that the MFN treatment obligation contained in the Cyprus-Bulgaria BIT did not extend to Plama the protection of dispute resolution provisions set out in other Bulgarian investment treaties. *The tribunal emphasised that it is a well-established principle, both in domestic and international law that the parties to an arbitration must clearly express their agreement to arbitrate, and that 'doubts as to the parties' clear and unambiguous intention can arise if the agreement to arbitrate is to be reached by incorporation by reference' such as through an MFN clause* (see Plama Consortium Limited v Republic of Bulgaria 63 [199]).

[50] Elizabeth Whitsitt is assistant Professor at the Law School of University of Calgary

must come with clean hands", the Tribunal's decision affirms that if investors want to seek refuge under international treaties, honesty is the best policy."

CONCLUSION

The road of investment arbitration as settling a dispute experienced a boost during the 21st century. The critical voices about the non-predictability of the cases, the pro-investor regime or the pro-State one, still exist, however, the awards have shown a balance, fair and consistent environment. It is certainly true that the absence of a permanent court (like the domestic court) ensuring consistency and predictability, makes it more difficult accomplish those targets.

In the future ECT is predicted to deal with issues of general interest that will attract the publicity, like the famous Yukos case. Even though States did not concern the ECT as an efficient way of dealing with disputes, this is changing the last few years and the cases that are pending for the award have increased.

I will conclude this Thesis with a few thoughts on how to improve international arbitration mechanism:

- States have to take a more active role in clarifying the meaning of existing treaty obligations. In future treaties, they must ensure that treaty provisions are clearly drafted to address the jurisprudential divides – for example by either clearly specifying that MFN applies or does not apply to dispute settlement.
- With respect to tribunals, one proposal I would like to quote is the participation of the investor's home state. The ECT was signed by the government and it would be beneficiary to look for the real meaning of the provisions. However, the host-state has to give its consent for such an inquiry cause the dispute is among an investor company.Therefore, if this is too ambitious the tribunal should go through the agreements between the State parties regarding the interpretation or subsequent practice that would be helpful for each pending case.

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