Novenergia v. Kingdom of Spain, the ECT and the ECJ: Where to now for intra-EU ECT claims?

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There has been much comment about recent awards in Energy Charter Treaty ('ECT') arbitrations concerning investors' claims against Spain and other EU states regarding renewable energy projects . The fortunes of investors and states have waxed and waned over the last few years, but overall it seemed that investors faced a considerable hurdle. In recent weeks, the rollercoaster ride has accelerated, with *Novenergia v. Kingdom of Spain*, SCC Case No. 063/2015, giving hope to investors, and EC Decision 2017/C 442 ('the Decision') and the European Court of Justice's ('ECJ') decision in Case C-284/16 *Slovak Republic v. Achmea BV* apparently dashing those hopes.

Background

In the mid-2000s, many EU states encouraged foreign investors to undertake renewable power projects, particularly solar energy. Legislation offered incentives such as specified feed-in tariffs for lengthy periods and no limit on energy generation/distribution.

The global economic crash made such schemes became unbearably costly, and relevant legislation was repealed or amended. Those legislative changes undermined or even destroyed the profitability of investments predicated on the basis of the existing legislative frameworks. Consequently, many investors brought arbitration claims under the ECT, which protects foreign investments in the energy sector of signatory states from expropriation and unfair treatment.[fn]At the time of writing, for example, around 30 ECT claims against Spain are underway[/fn]

Charanne, Eiser, Isolux* and *Blusun

In 2016 and 2017, four awards were made in respect of claims by investors from one EU state against another EU state: *Charanne v. Spain*[fn]*Charanne B.V. and Construction Investments S.á.r.l v. Kingdom of Spain* (SCC Case No. V 062/2012)[/fn]; *Eiser v. Spain*[fn]*Eiser Infrastructure Limited and Energia Solar Luxembourg Sarl v. Kingdom of Spain* (ICSID Case No.ARB/13/36)[/fn]; *Isolux Netherlands, BV v. Kingdom of Spain*[fn]*Isolux Netherlands, BV v. Kingdom of Spain* (SCC Case No. V 2013/153)[/fn] and *Blusun v. Italy*[fn]*Blusun S.A., Jean-Pierre Lecorcier and Michael Stein v. Italian Republic* (ICSID Case No. ARB/14/3)[/fn]. The awards displayed some consistency in that:

1. They rejected submissions by the respondents, and the European Commission ('EC') via amicus curiae briefs, that the tribunals lacked jurisdiction to hear ECT claims between an EU member state and an investor from another EU state.[fn]Similar arguments have been heard, and dismissed, in other cases, e.g. *RREEF Infrastructure v. Kingdom of Spain* (ICSID Case No. ARB/13/30)[/fn] Broadly the arguments were that:

(a) As the EU itself is a signatory of the ECT and both parties are from the EU, Article 26(1) ECT was not fulfilled i.e. the claimant was not from an “Area” of “another Contracting Party”;
(b) The ECT impliedly included a disconnection clause, barring EU states from applying the ECT inter se; and
(c) EU law is an independent legal system taking precedence over other international law and domestic law, which provides an exclusive source of legal rights and remedies for intra-EU relations, including investor protection. The tribunal must apply EU law in reaching its decision. Therefore, the courts of the EU are the only appropriate jurisdiction to apply and enforce EU law.

The tribunals dismissed those arguments, holding that:
(i) individual EU states are also individual signatories to the ECT and the parties are of different nationalities;
(ii) the plain wording of the ECT did not allow for an implied disconnection clause; and
(iii) the claims are based on the provisions of the ECT, not EU law; the ECT expressly gives the tribunal exclusive jurisdiction; and there is no clash between ECT protections and EU law which would require a decision by the ECJ.

2. The tribunals accepted that fair and equitable treatment protections such as that in Article 10(1) ECT do not prevent a state from amending its regulatory regime, unless (i) it has given specific assurances to keep that regime in place for the lifetime of the investment (such as a contractual ‘stablisation clauses’); and/or (ii) such changes are disproportionate to the aim of the legislative changes, and fail to take due regard to investors’ legitimate expectations, formed before such reforms were mooted.

However, the awards also differed on some key issues:

3. The only award in favour of an investor was *Eiser*. This distinguished the 2010 amendments to Spain’s solar incentives regime[fn]The focus of the claim in Charanne.[/fn] from the more extensive 2013/14 reforms. The tribunal held that Article 10(1) ECT entitled the claimants to expect that Spain would not revise the regime upon which their investments were based to such a degree that all value in them was lost. Those legitimate expectations were based on the 2007 legislation and Spain’s further conduct in 2010-2011. The 2013/14 reforms amounted to a “total and unreasonable change” in violation of those legitimate expectations. The tribunal awarded the claimants damages of €128m.

4. When considering the circumstances in which a state may have breached Article 10(1) by modifying its regulatory framework, the *Blusun* tribunal rejected the tripartite criteria in *Charanne* (public interest, unreasonableness and disproportionality). The tribunal concluded that “in the absence of a specific commitment”, a state has no obligation to grant or maintain subsidies, but any modification should be done “in a manner which is not disproportionate to the aim of the legislative amendment, and should have due regard to the reasonable reliance interests of recipients who may have committed substantial resources on the basis of the earlier regime.”

The awards indicated the difficulties of establishing actionable legitimate expectations of stability in the absence of a stabilisation clause. Even the one result in favour of an investor, Eiser, is being challenged via annulment proceedings.[fn]Spain has applied for annulment for a failure to state reasons and a manifest excess of power, based upon the finding of a breach of Article 10(1) in circumstances where the tribunal held that Spain had a sovereign right to amend its legislation and had made no commitments as to a stable regulatory environment. Spain’s application also alleges that the claimant’s nominated arbitrator breached his obligation of independence and impartiality by failing to disclose a longstanding relationship with the claimants' valuation experts.[/fn]

Novenergia v. Kingdom of Spain

However, in February 2018, the tribunal in *Novenergia v. Spain* ordered Spain to pay €53 million to Novenergia, a Luxembourg fund which had invested in photovoltaic plants in Spain. The award was significant in that adopted a more expansive approach to investor claims than in the previous cases (including *Eiser*).

Novenergia's claim related to the same 2013/14 reforms as in *Eiser* and *Isolux*. As in the previous awards, the tribunal confirmed that Article 10(1) ECT does not create an independent obligation to provide stable investment conditions. The key question is whether the investor has legitimate expectations of stability.

Contrary to *Charanne*, however, the tribunal held that such expectations "arise naturally from undertakings and assurances" given by the state. These do not need to be specific undertakings and/or contractual stabilisation clauses – state conduct or statements which objectively create such expectations (irrespective of whether the state intended to create them) are sufficient. Novenergia was entitled to form legitimate expectations as to the 2007 regime based on statements by officials to Spain's Congress of Deputies, as well as Spain's marketing documents which, the tribunal said, constituted "bait".

As in *Eiser*, the tribunal held that Spain's 2013/2014 reforms, which replaced the 2007 regime with a new regime guaranteeing only a 'reasonable rate of return', were a "radical and unexpected" departure from the 2007 regime. At the time of its investment decision, Novenergia had a legitimate expectation that the 2007 regime would remain relatively stable.

While Novenergia's investments had not been destroyed by the 2013 reforms,[fn]In fact, they were still achieving a reasonable rate of return[/fn] going further than *Esier*, the tribunal held that it was sufficient that Novenergia could show "quantifiable prejudice" compared with its position when it initially made its investment. The tribunal found that the 2013/14 reforms had a "significant damaging economic effect" on Novenergia's plants, decreasing revenues by 24% – 32%, and awarded damages accordingly.

Enter the EC

One might think that the tide has turned in favour of investors. However, two interventions from EU institutions seem to have swung the pendulum in the other direction:

(a) In Decision 2017/C 442, published on 10 November 2017, the EC attacked ECT claims brought by investors against Spain (and other EU states). Spain had established the 2007 regime, and reformed it, without obtaining prior approval from the EC. That constituted the granting of state aid without first notifying the EC, and under EU law investors cannot form legitimate expectations with regard to such schemes. The applicable law of the dispute must be EU law as each party was or was from an EU state; and since "the principle of fair and equitable treatment [in the ECT] cannot have a broader scope than the [EU] law notions of legal certainty and legitimate expectations in the context of a state aid scheme", no investor could form legitimate expectations with regard to the Spanish 2007 regime and its reforms.

The Decision went on to criticise the concept of the ECT claims, stating that the EC considers that "any provision that provides for investor-State arbitration between two Member States is contrary to [European] Union law…Union law provides for a complete set of rules on investment protection…Member States are hence not competent to conclude bilateral or multilateral agreements between themselves". The Decision concluded that "[f]or those reasons, ECT does not apply to investors from other Member States initiating disputes against another Member States".

Finally, the Decision stated that if an arbitral tribunal awarded an investor compensation in respect of losses caused by Spain's reform of the Special Regime, that would constitute state aid; and if Spain paid such an award, it would require EC approval. For good measure, the Decision stated that "this Decision is part of Union law, and as such also binding on Arbitration Tribunals, where they apply Union law. The exclusive forum for challenging its validity are [sic] the European Courts".[fn]The Decision was considered in the *Novenergia* award and dismissed as irrelevant, since the tribunal held that they were not applying EU law, but rights arising under the ECT.[/fn]

(b) In March 2018, the ECJ handed down its judgment in the *Achmea* case, holding that investor-state arbitration clauses in intra-EU BITs are not compatible with EU law. However, it is not clear whether this affects intra-EU ECT claims. The *ratio decidendi* appears to be that EU member states cannot derogate from the provisions of EU instruments, especially the Treaty on the Functioning of the EU, which provide for the primacy of EU law and the necessity for it to be tested in the courts of member states, by reference to the ECJ if necessary. However, in contrast to the Netherlands and Slovakia BIT which is the subject-matter of *Achmea*, the EU itself is a signatory to the ECT, and hence it can be argued that it has agreed to claims under the ECT being determined by the arbitration mechanism specified in the ECT. The EU clearly has the power to enter into arbitration agreements – c.f. the EU's free trade agreements with third parties.

Nevertheless, the Decision and the *Achmea* judgment make it likely that any attempt to enforce an ECT award in an EU state will be resisted, e.g. under Article V(2) of the New York Convention (dispute not capable of settlement by arbitration/contrary to public policy). Investors may of course try to enforce outside the EU.

Where to now?

It remains to be seen if claimants will press ahead with their outstanding ECT claims against Spain and other EU states; or whether fresh claims will be commenced in another forum (and if so, what and where?). However, the Decision and *Achmea* may not necessarily be the death-knell for intra-EU ECT arbitrations that they might seem at first glance.

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