Kluwer Arbitration Blog

Naturgy v. Colombia: Considerations on Police Powers and a Setback from Urbaser?

Paola Patarroyo (Esguerra Asesores Jurídicos) · Tuesday, June 29th, 2021

On 12 March 2021, a tribunal issued an award in the case of *Naturgy v. Colombia* (ICSID Case No. UNCT/18/1) under the Colombia-Spain BIT (2005) (the "BIT"). The decision is the first in a wave of four decisions decided in the first half of 2021 in favor of Colombia. *Naturgy* is noteworthy for its engagement with debates on the police powers doctrine and the jurisdiction of arbitral tribunals over counterclaims by States against investors.

The Facts

The tribunal, composed by Stephen Drymer, Alexis Mourre and Eric Schwartz, analyzed a dispute concerning the takeover of Electricaribe (an electricity company operating in the Caribbean region of Colombia) by the national authority regulating public utility services. The intervention occurred in 2016 after a series of government measures attempting to balance the financial situation of the company. Pursuant to Law 142 of 1994, that regulates public utilities, the State can take temporary control of public utilities as a "preventive" measure in certain cases. Some of the situations include when the company can no longer provide services with the quality and continuity required if such service is indispensable to preserve public or economic order, to avoid serious damage to users or third parties, and if the company has suspended or might suspend payment of its obligations.

Naturgy claimed that through these measures its property in Electricaribe was expropriated and that Colombia violated the fair and equitable treatment clause of the BIT.

Colombia argued that intervention in the company was a valid exercise of its police powers, that the requirements for takeover under domestic law were met, and that the intervention was justified.

The Decision on the Merits: Colombia Used its Police Powers

The tribunal started from the premise that States are not obliged to pay compensation to investors for damages arising out of regulatory actions taken in good faith, and Article 11(2) of the BIT does not prevent a Contracting Party from "adopting or maintaining measures destined to preserve public order."

The award concluded that Colombia legitimately exercised its police powers because the requirements for takeover under Law 142 of 1994 were met. The takeover was justified by Electricaribe's financial distress, the danger of the disruption of service, and a 'systemic risk' that the company could no longer comply with its financial duties to purchase energy in the national market (¶ 468). Hence, the Tribunal decided that Colombia's takeover was not an expropriation and Colombia accordingly did not owe compensatory damages to the claimant.

The tribunal also dismissed the FET claim, finding that that the takeover was not a disproportionate decision. The government's actions included hiring external advisors to prepare financial indicators to establish Electricaribe's economic condition. Additionally, the company had the opportunity to request the revision of the decision as an administrative recourse. The request for reconsideration was rejected and Electricaribe did not file an appeal to the decision which confirmed the company's intervention (¶ 504).

No Jurisdiction over Counterclaims

Colombia filed counterclaims requesting compensation for the claimant's mismanagement of Electricaribe. It alleged that this mismanagement meant that "Colombia was forced to channel [funds] into the Company" to maintain its operations during the intervention, and produced a negative impact in regional development, lower tax revenues from Electricaribe and the reduction in the value of Colombia's shareholding in the company. (¶ 582).

The tribunal analyzed its jurisdiction over such counterclaims under the applicable BIT and the scope of consent given by the parties. The Treaty's dispute settlement clause, article 10(2) covers: "[a]ll disputes regarding investments that may arise between one of the Contracting Parties and an investor of the other Contracting Party *regarding issues governed by this Agreement*…". The tribunal recalled the absence of admissibility rules for counterclaims under the UNCITRAL Rules and followed the two-step approach in *Saluka*, to confirm that counterclaims (i) could fall within the tribunal's jurisdiction; and (ii) were within the dispute resolution provisions of the applicable treaty (¶ 600).

Colombia argued that the tribunal had jurisdiction over the counterclaims since the BIT covers "all disputes", and that there was a "reasonable" connection between the investor's claims and the State's counterclaims as required by article 19(3) of the UNCITRAL Rules of 1976 (¶ 590). As the Treaty requires disputes to be "regarding issues governed by [the BIT]", Colombia argued that because article 10(9) includes domestic law as one of the applicable laws, the investor's duties under domestic law were implicitly "regulated by the treaty," and thus under the tribunal's jurisdiction (¶ 620).

The tribunal concluded that article 10(2) of the BIT, read together with the other sections of the same article, indicated a specific scope of consent and did not provide grounds for counterclaims.

First, the Tribunal differentiated the BIT from other treaties, pointing out that the former did not contain language entitling Contracting Parties to bring counterclaims. It emphasized that the *Saluka* tribunal did not suggest that the expression "all disputes" provides a general basis for jurisdiction over State's counterclaims, but that, in principle, it did not preclude the possibility in that case (¶ 604). The *Saluka* tribunal declined jurisdiction over the counterclaims as it considered that they were not "sufficiently closely connected with the subject matter of the [investor's]

original claim" (*Saluka*, ¶ 81). Moreover, other treaties, e.g., the Organisation of Islamic Cooperation Investment Agreement expressly include references to awards containing orders against investors for counterclaims (*Hesham*, ¶ 660).

Second, other sections of article 10 of the BIT, beyond section 2, were drafted specifically to refer to claims "from an investor," without references to a State's counterclaims (¶ 615). The Tribunal also concluded that, given the detailed treaty clause addressing dispute-settlement, it was at least doubtful that the contracting parties omitted references to counterclaims if they intended to extend an arbitral tribunal's jurisdiction to such claims (¶ 616). For example, article 10(4) referred to the grounds for a claim concerning treaty violations by a Contracting Party and the losses or damages suffered by the investor (¶ 617). Likewise, article 10 (10) referred to the impossibility of States to formulate as a defense that the investor received or will receive compensation from an insurance contract or guarantee for the losses suffered from BIT violations.

Finally, as article 10(2) of the Treaty covered investor-State disputes *regarding issues regulated by [the] Agreement*, the tribunal considered that the treaty did not regulate the management of the investment by the investor in a sector regulated by domestic law. Thus, it rejected Respondent's argument that the reference to domestic law in the applicable law would amount to a matter "regulated by the treaty" (¶ 620). The arbitrators considered that the dispute settlement clause in the treaty was precise enough to qualify the covered disputes, and the broad interpretation proposed by Respondent would "deprive the provision of any meaning" (¶ 619).

A Setback from *Urbaser* on the close connection test?

In 2016, the tribunal in *Urbaser v. Argentina* ruled that it had jurisdiction over counterclaims brought in relation to violations of the right to water for the lack of investments by the Claimants. However, the treaties in *Urbaser* and *Naturgy* had different language regarding the covered claims. In *Urbaser*, the Argentina-Spain BIT (1991) covered disputes "*in the sense of* the present Agreement", while the Colombia-Spain BIT referred to disputes "regarding issues *regulated by* the present Agreement."

Thus, the *Urbaser* tribunal interpreted the close connection test broadly by concluding that there was a manifest factual link between the investor's claims and the State's counterclaim as the claims were "based on the same investment, or the alleged lack of sufficient investment, in relation to the same concession" (¶1151).

The *Naturgy* tribunal considered that the necessary close connection test developed in *Saluka*, and *Paushok* was not proven. The tribunal concluded that the counterclaims concerned Electricaribe's operation being inconsistent with Colombian law, and the compensation sought by Colombia was "different in nature and based on different factual and legal grounds than the compensation sought by Claimants in the main claims" (¶ 623). Thus, unlike *Urbaser*, the same factual context would not suffice to determine that there was a connection between the investor's claims and the State's counterclaims.

Conclusion

The decision in *Naturgy v. Colombia* further developed the police powers doctrine and emphasized the possibility for States to take measures in highly regulated industries. It also engaged in the debate as to the jurisdiction of investment tribunals over counterclaims. There was a return to *Saluka* through a more restrictive interpretation of the close connection test, narrower than in *Urbaser* where a factual connection to the investment was deemed enough. The tribunal interpreted the requirement of a connection between claims and counterclaims to focus on the factual *and legal* basis of the claims to compensation, requiring counterclaims to be based on the treaty. However, while the tribunal held that it lacked jurisdiction over the counterclaim as raised, it signaled a way forward for States interested in bringing counterclaims, in terms of the drafting of treaties to establish consent and a comprehensive framework to allow claims ruled under such instruments.

This entry was posted on Tuesday, June 29th, 2021 at 8:56 am and is filed under Colombia, Counterclaims, Investment Arbitration, Latin America, Police Powers, Treaty Interpretation
You can follow any responses to this entry through the Comments (RSS) feed. You can leave a

response, or trackback from your own site.