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IC Power v. Guatemala: Setting the Standard on Past Investments and Denial of Justice in Investment Claims

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The recently surfaced award in *IC Power Asia Development Ltd. v. Guatemala* dated 7 October 2020 reveals the reasoning of the Tribunal's majority in dismissing IC Power's claims on the merits. A majority of Albert Jan van den Berg (chair) and Raúl Vinuesa (Respondent's appointee) dismissed IC Power's claims on the merits, while Guido Santiago Tawil (Claimant's appointee) dissented.

The Tribunal acted under the UNCITRAL Rules and the dispute was brought under the Guatemala-Israel BIT (2006) (the "BIT"). Among the many legal issues analyzed by the Tribunal, this entry focuses on two main issues. On jurisdiction, the tribunal upheld jurisdiction even when the investment had been sold before the commencement of the arbitration. On the merits, the Tribunal reaffirmed that international law accords a high level of deference to the decisions of domestic courts and does not purport to have investment tribunals act as courts of appeal. Below we discuss these two issues, after a brief recollection of the factual background.[1)]

Background

In 2011, UK investment fund Actis LLP ("Actis") acquired the Guatemalan group Energuate from Unión Fenosa Internacional S.A. The Group included two Guatemalan electricity distribution companies (DEORSA and DEOCSA, together the "Companies"), a transmission company and a trading company. In May 2012, the Guatemalan Superintendence of Tax Administration (the "SAT" for its Spanish acronym) initiated an audit of the Companies due to a significant reduction in their tax collection (the "Audit"). The SAT identified that the Actis purchase transaction had caused irregular tax deductions in favor of the Companies. In 2015, Actis obtained two binding tax opinions, apparently solving the tax dispute. The SAT did not take the investigations further.

In January 2016, Energuate was acquired by Israeli company IC Power Asia Development Ltd. (the "Claimant") for a value of USD 265 million. On 13 July 2016, the SAT filed a criminal complaint against the Companies for tax fraud after reviewing the Audit due to a corruption scandal involving former SAT employees. The criminal court at issue granted the SAT's petition to enact provisional measures over Energuate's bank accounts, lifted only after Energuate paid the SAT around USD 75 million under protest.[2)] On 31 December 2017, IC Power closed the sale of its

stake at Energuate to a third party, while expressly retaining its rights to bring a treaty claim against Guatemala. Two months after the sale, IC Power filed a Notice of Arbitration (the "NOA") against Guatemala.

On Jurisdiction: A Voluntary Sale of the Investment Prior to the Commencement of the Arbitration Does Not Preclude Treaty Protection

Among the jurisdictional objections dismissed by the Tribunal was that Claimant did not have an "investment" under the BIT because it had sold its shares in the Companies prior to initiating the dispute. Guatemala relied on *David R. Aven, et.al. v. Costa Rica* to argue that an investor who disposes of ownership should not be eligible to seek investment protection unless "special circumstances" are present, *e.g.* a loss of the investment due to third-party or state actions. According to Guatemala, a voluntary sale of the investment due to market reasons would not meet this threshold. (Award, ¶¶ 355-356)

In turn, IC Power argued that the relevant date to assess jurisdiction should not be that of the NOA, but the date on which the alleged breach occurred. Claimant also emphasized that it had expressly reserved the right to pursue a treaty claim during the sale, and said retained right qualified as an investment under the BIT. Claimant relied on *El Paso v. Argentina* to point out that there is no rule of continuous ownership of the investment or otherwise expropriations would automatically bar investor's rights to bring any claim. Claimant distinguished its case from *David R. Aven* where the investor did not expressly retain any rights, and where the underlying treaty (the CAFTA-DR), unlike the BIT, required continuous ownership.

The Tribunal upheld jurisdiction. *First*, the Tribunal held that under the text of Article 1.1 of the BIT, an "*investment*" would have to be physically located in Guatemala or arise as a matter of domestic law, which was not the case of a treaty claim.[3)] Additionally, the Tribunal referred to *Axos Capital v. Kosovo* to clarify that treaty claims do not constitute investments *per se*.

Second, the Tribunal found that the text of the BIT was ambiguous and did not answer if a dispute could be submitted to arbitration in respect of a former investment that was sold prior to the commencement of the proceedings. The Tribunal sought answers from general international law and the practice of international tribunals.

The Tribunal started its analysis by pointing to the broadly accepted rule that jurisdiction must be assessed at the date on which the proceedings are commenced and that this rule is subject to derogation, *e.g.* a claimant whose investment has been expropriated and who brings an expropriation claim. Additionally, the Tribunal found that the aforementioned rule is not absolute, and *special circumstances* may justify extending treaty protection to a claimant who *voluntarily* disposed of an investment prior to commence arbitration (relying on *David R. Aven)*. On this point, the Tribunal clarified that s*pecial circumstances need not be exceptional*, but it meant that there must be a valid reason for a claimant to bring a claim that it would otherwise be unable to bring.

Furthermore, the Tribunal reaffirmed that the text of the BIT controlled, and here, the BIT did not include any requirement of continuous ownership of the investment.

Interestingly, the Tribunal clarified that the retention of treaty claims has to be qualified to allow

investors to bring future disputes: (a) the retention must be absolute (in the sense that the new owner of the investment is barred from bringing the same treaty claim based on the same facts); and (b) claimant must have fulfilled the treaty's requirements for a qualifying investor and qualifying investment at some point prior to the commencement of the arbitration.

On these grounds, the Tribunal found that IC Power was eligible to seek Treaty protection of its retained Treaty claims. In their analysis, the Tribunal reaffirmed the rule introduced in *David R. Aven* and expanded its application to allow investors to bring claims after the voluntarily disposal of the investments so long as there is a qualified retention of treaty claims. This heightened standard sheds a light for investors that are seeking to divest their investment and fear not being able to hold treaty rights in the future. However, investors must first abide by the text of the applicable treaty at issue, since it may include a mandatory continuous ownership requirement.

On the Merits: Conduct of Local Courts Can only Generate International Responsibility under the Standard of Denial of Justice

IC Power argued that Guatemala had breached the FET standard in Article 2(2) of the BIT through a breach of legitimate expectations, arbitrary conduct, breach of procedural fairness and due process, and lack of transparency. Claimant's claims arose from the SAT's decision to initiate criminal proceedings and submit seizure orders against the Companies in alleged disallowance of the binding tax opinions and without exhausting administrative proceedings under Guatemalan law. Claimant also claimed a breach of FET in relation to the criminal court's decision in granting seizure orders. Guatemala denied all these allegations.

The majority of the Tribunal held that the local criminal court's action could only give rise to a breach of the BIT under the standard of denial of justice, an allegation that Claimant did not raise. The Tribunal recalled that international law accords a *high level of deference* to the decisions of domestic courts and does not purport to have investment tribunals act as courts of appeal. Simply put, the Tribunal did not want to second-guess determinations that had been made at the local level, which the majority found reasonable under the circumstances.

The Tribunal resorted to the standard set out in *Robert Azinian, et. al. v. Mexico* to identify different instances of denial of justice: *e.g.* refusal to entertain a suit, undue delay in the issuance of a decision, seriously inadequate administration of justice or clear and malicious misapplication of the law. In addition, the exhaustion of local remedies has also been regarded as one of the main grounds for denial of justice, as set in *Loewen v. United States* and revived in *Jan de Nul N.V. et. al. v. Egypt*. The Tribunal characterized Claimant's allegations within the paradigms of denial of justice in *Azinian*, concluding that they could not entertain Claimant's claim on arbitrariness (under a FET breach) because Claimant did not claim denial of justice.

The Tribunal's analysis and majority decision on this particular point reinforce the predominant position of the international community with respect to the interplay between local courts and international tribunals: international law imposes a *particularly high threshold* for conduct of the judiciary to give rise to international responsibility through denial of justice. This balance seems to play a crucial role in delimiting the role of international tribunals in disputes that involve decisions from local courts. However, the predominance of this position remains to be tested in future cases involving denial of justice claims, in particular those in which the alleged conduct does not only

entail decisions from the judiciary, but also governmental actions; or those in which arbitrariness derives from the alleged misuse of the judiciary.

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References

?1 The award on this case became public recently in the context of enforcement proceedings in the United States. Guatemala was awarded more than USD 1.8 million on legal and arbitration costs. At the time of this publication, the dissenting opinion remains unpublished.

?2 The criminal proceeding remains open and unresolved.

?3 Israel – Guatemala BIT (2006), "Article 1: Definitions I. For the purposes of the present Agreement: (a) 'Investments' shall mean any kind of assets, implemented in accordance with the legislation of the Contracting Party in whose territory the investment is made including, but not limited to: (…)".

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