Kluwer Arbitration Blog

World Arbitration Update: Taking Stock of the ECT Modernization Process – Fit for the 21st Century?

Nazly Duarte (Georgetown University Law Center) · Saturday, November 19th, 2022

The **Second Edition of the World Arbitration Update (WAU)** took place from September 26 to September 30, 2022. This post highlights the panel on "***Taking Stock of the ECT Modernization Process: Fit for the 21st Century?".*** The panel was moderated by WAW Co-founder **José Antonio Rivas** (Xtrategy LLP/Georgetown Law). He was joined by **Daniela-Olivia Ghicajanu** (Georgetown University), **Lukas Stifter** (Chair, Modernisation Group – Energy Charter Treaty), **Nikos Lavranos** (International Dispute Resolution Arbitrator & Mediator, NL-Investmentconsulting), and **Marinn Carlson** (Partner and Co-leader of the Trade and Advocacy practice, Sidley Austin).

Quo vadis, ECT?

Ms. Ghicajanu opened the discussions by providing a general overview of the Energy Charter Treaty ("ECT"). The ECT is a multilateral trade and investment treaty which has been in force since 1998 and which provides a binding international legal framework for energy cooperation (initially between 54 Contracting Parties, among which the European Union ("EU") and EURATOM are also included in their own capacities. Ms. Ghicajanu highlighted that, at the moment, the ECT is the most used investment agreement globally with some 150 arbitral proceedings having been initiated under the treaty to date.

Ms. Ghicajanu also walked the audience through the highly discussed ECT modernization process, which, in her opinion, was a necessity due, *inter alia*, to (i) the inconsistent interpretation and application of the ECT provisions by tribunals, national courts and recently the Court of Justice of the European Union (CJEU) climate change and net zero goals. Furthermore, amendments were needed because the ECT did not include a disconnection clause that expressly excluded the application of the treaty in intra EU disputes. The term disconnection clause is commonly used to refer to a provision in a multilateral treaty allowing "*certain parties to the treaty not to apply the treaty in full or in part in their mutual relations, while other parties remain free to invoke the treaty fully in their relations with these parties*" (*See* Report on the Consequences of the so-called "Disconnection Clause" in International Law in General and for Council of Europe Conventions, containing such a Clause, in Particular, at 3). ECT modernization efforts and related topics have been discussed extensively on the Blog previously.

The overview concluded with comments that could be drawn on later in the panel discussion, including the latest developments in domestic courts regarding the ECT application (*See Mainstream Renewable Power and others v. Germany*, *RWE v. Netherlands*, and *Uniper v. Netherlands*) and the tension between the principles of supremacy and primacy of the EU law and principles of international public law.

ECT Modernization Process

While the ECT modernization process discussions started in 2017, the first negotiation only started until 2020. The ECT Reform negotiations ended in June 2022. Mr. Stifter explained that the core of the negotiations for the ECT modernization were focused on the amendments that the ECT needed to align the treaty with the Paris Agreement.

Some of the highly discussed topics during the negotiations were (i) the definition of Economic Activity in the energy sector (*See* article 1.6 of the ECT) and how that Economic Activity concerns to "Energy Materials and Products", (ii) the definition of 'Investor' and the necessity of including a substantial business requirement, and (iii) the definition of 'Investment' and its prospective compliance with the laws of the home state.

Similar to ISDS reform discussions in other fora, transparency, security for costs, third party funding, damages and frivolous claims were the main topics discussed during the negotiations of the ISDS provisions in the ECT. In particular, he noted that the provisions related to frivolous claims and third-party funding obligations were inspired by the ICSID Rules. Furthermore, Mr. Stifter held that the umbrella clause in the ECT will now be limited to concrete breaches and must be exercised through the government authority authorized for such purposes. Lastly, it is noteworthy that the negotiations clarified a long-standing issue regarding which ECT provisions (if any) should not apply among members of the Regional Economic International Organisation ("REIO") by concluding, *inter alia*, that article 26 of the amended ECT shall not apply to REIO members.

Thought Provoking Questions around the ECT Modernization Process

Mr. Rivas asked Mr. Lavranos about his perspective on the ECT modernization process. Mr. Lavranos noted that in the leaked text of the ECT Working Document there are no transition periods or cut off gates for the application of article 26 of the ECT which leaves the door open to possible retroactivity. Therefore, if article 26 of the ECT, as worded in the ECT Working Document, enters into force, it is worth questioning whether the awards of concluded cases under the current ECT provisions could be fully enforced and recognized in and outside of the EU. Retroactive application of article 26 of the ECT is a latent risk and European Court jurisprudence suggests that a retroactive application is a possibility, as happened in the *Achmea* ruling, for example.

Moreover, a valid question for ongoing or future cases is whether investors would have legitimate expectations, from a rule of law perspective, on the recognition and enforcement of awards. If cases are concluded after the ECT amended provisions have entered into force, EU domestic courts might not recognize these awards – even if they are ICSID awards – possibly arguing public order

reasons. Nonetheless, Mr. Lavranos noted that ICSID awards, generally speaking, should provide a stronger legal basis for enforcement before domestic courts, at least outside the EU, e.g., in the *Micula* case, the UK Supreme Court held, *inter alia*, that "*arbitration awards under the ICSID Convention should be enforceable in the courts of all Contracting States and with the same status as a final judgment of the local courts in those States* (…)" (at para. 70). However, non ICSID awards might pose a problem, possibly, due to the public order exception under the New York Convention.

ECT Going Forward

Ms. Carlson started her intervention by mentioning that the entire ECT modernization process was made in a remarkably short time for a multilateral agreement. She pointed out that the *Komstroy* case, which is relevant for the ECT modernization process discussion, does not involve an intra-EU ECT dispute, but a dispute involving a non-EU State and a third country investor. Mr. Rivas mentioned that in some cases, such as *Komstroy*, the Court of Justice of the EU (CJEU) have not relied on the Vienna Convention on the Law of Treaties, but on the EU law supremacy principle over an apparent conflicting international norm.

It is likely that the recognition and enforcement of awards of cases conducted under the current provisions of the ECT would be pushed to the United States, the United Kingdom or any other jurisdiction outside the EU, for instance, Turkey. However, US courts, might be hesitant to apply article 26 of the ECT retroactively. Opposing recognition or enforcement of awards in non-EU domestic courts by retroactively relying on ISDS provisions and EU laws might be a tall order (*See* the Micula saga as previously covered on the Blog).

Ms. Carlson questioned whether countries that withdrew the ECT like Italy -that is now under the sunset clause- would get the benefits of all the amendments and improved treaty provisions to the ECT or whether they would have to defend their disputes under the "former" ECT provisions.

Closing Remarks

Until today Netherlands, Spain, and Poland have signaled their intent to withdraw from the ECT and, more recently, France, Slovenia, and Germany have also announced that they would withdraw the treaty. Now that the ECT reform has been concluded, its outcome features various aspects such as the increase in the level of investment protection, the seeming end of intra-EU applications under the ECT, as well as the strengthening of environmental and social provisions. However, when assessing the outcome of the amended ECT, the current political landscape in the EU should be taken into consideration.

Commercial arbitration cases in the energy sector are likely to increase, and since the EU is looking to foster the investment in renewable energies, a key question is whether investors are -or not- better off the ECT. Finally, how EU and non-EU domestic courts would reconcile the regional principles of supremacy and autonomy of EU law with the principles of public international law, remains to be seen.

The complete the video of the panel is available here.

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