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EU Law Showing its Teeth: The Annulment of Novenergia II v Spain

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The Court of Justice of the European Union (CJEU) ruled in *Komstroy* (C-741/19, Sept, 2021) that the dispute resolution mechanism of the 1994 Energy Charter Treaty (ECT) does not apply in intra-EU investment disputes. The ruling was interpreted by some as the beginning of the end of intra-EU investment arbitration. A recent decision by the Swedish appellate court (Svea Court of Appeal Case No. T 4658-18, Dec 2022) annulling the award in Novenergia II v Spain seems to speak in favour of this proposition.

It related to an ECT award rendered in favor of Luxemburg-based Novenergia II – Energy & Environment (SCA) (Novenergia) against the Kingdom of Spain. The case is another example of how a court of an EU Member State has interpreted the CJEU's case law to mean that investment arbitration awards rendered in intra-EU relations are to be considered as invalid. It is also shedding light on the issue to what extent (if any) investors can rely on due process principles to defend a challenge of an intra-EU investment award.

Facts of the Case

Novenergia purchased eight solar parks in Spain in 2007. During the period 2010–2014, Spain implemented regulatory changes that negatively impacted Novenergia's entitlement to receive subsidies on the energy production of the solar parks.

In 2015, Novenergia commenced arbitration against Spain in Sweden under the Arbitration Rules of the SCC Arbitration Institute (SCC Case V 2015/063). In the arbitration, Novenergia successfully argued that the regulatory changes effectuated by Spain amounted to a breach of Article 10.1 (fair and equitable treatment) of the ECT and was awarded EUR 53.3 million in damages.

Spain subsequently challenged the award before the Swedish appellate court relying on the CJEU's preliminary rulings in *Achmea* (C-284/16, Mar, 2018), *Komstroy*, and *PL Holdings* (C-109/20, Oct 2021). In summary, Spain argued that these cases demonstrate that the award had been rendered in violation of mandatory EU law. As a result, Spain requested, among other things, that the award should be declared invalid based on non-arbitrability or that the award is contrary to *ordre public*.

The Appellate Court's Assessment

The appellate court began by making general comments on the implications of *Achmea*, *Komstroy* and *PL Holdings*. It noted that, in *Komstroy*, the CJEU re-affirmed its conclusion in *Achmea* that an international agreement cannot infringe on the allocation of powers laid down by the Treaties of the EU and, consequently, the autonomy of the EU legal system.

The appellate court further stated that the proper interpretation of *Komstroy* is that Article 26.2 (c) of the ECT (i.e., the treaty's dispute resolution mechanism) is not applicable with respect to disputes between a Member State and an investor from another Member State. Consequently, Article 26 of the ECT does not give rise to a valid arbitration agreement between Novenergia and Spain. The court pointed to the following factors in support of its conclusion:

- The reasons underlying the *Komstroy* ruling are general in nature which has been confirmed by the CJEU in Opinion 1/20 dated 16 June 2022 concerning a request from Belgium for an opinion on the compatibility with EU law of the draft version of the modernized ECT.
- The CJEU's ruling in *Komstroy* was not limited in time. This means that the principles expressed therein applies to the ECT as from its entry into force.

The appellate court also referenced *PL Holdings*, where the CJEU held that Articles 267 and 344 of the TFEU "preclude national legislation which allows a Member State to conclude an ad hoc arbitration agreement" that mirrors an arbitration clause of an intra-EU bilateral investment treaty (BIT). The appellate court concluded that the CJEU's ruling in *PL Holdings* means that the parties lack the possibility to remedy the absence of a valid treaty-based arbitration agreement by concluding an arbitration agreement ad hoc.

For these reasons, the court found that Spain and Novenergia had been prevented from entering into an agreement to submit their dispute to arbitration and, therefore, declared the award invalid due to non-arbitrability, pursuant to Section 33 (1) of the Swedish Arbitration Act ((SFS) 1999:116).

Novenergia's Due Process Defense

In defense of Spain's challenge, Novenergia claimed that fundamental due process principles prevented the appellate court from annulling the award. It pointed to, among other things, the fact that Novenergia – in the event of annulment of the award – would be deprived of any possibility to pursue its damages claim against Spain.

In short, Novenergia relied on the following legal arguments in support of its defense:

- Annulling the award based on the CJEU's rulings in *Achmea* and *Komstroy* would contradict public international law as it would constitute a retroactive revision of the provisions of the ECT. This would violate the 1950 European Convention on Human Rights (ECHR), which has been incorporated into Swedish law.
- Annulling the award would violate Novenergia's right to: (i) a fair trial according to Article 6 of the ECHR; (ii) protection of property as per Article 1 of Protocol No. 1 to the ECHR; and (iii) the principle of proportionality imbedded in EU law.

The appellate court rejected Novenergia's defense. In summary, it relied on the following reasons:

- It is clear from the CJEU's reasoning in *PL Holdings* that the CJEU foresaw – and even presupposed – that its preliminary ruling would mean that the award in question could not be upheld. There is no reason to assume that the CJEU took a different approach as to arbitral awards rendered under the ECT. Against this background, it should also be presumed that the CJEU's interpretation of the ECT conforms to the ECHR.
- Sweden is obligated under public international law to ensure – on a case-by-case basis – that the rights included in the ECHR are not violated. In this respect, the evidence relied on by Novenergia does provide some support for the allegation that a claim under the ECT would now be considered time-barred if brought before the Spanish courts. This notwithstanding, Novenergia has, against Spain's denial, failed to prove that Novenergia – in the event a damages claim was brought against Spain under the ECT – would be denied recourse to the judicial system. Under these circumstances, Novenergia has failed to prove: (i) that an annulment of the award would have the consequences alleged by it and (ii) that Novenergia's rights under the ECHR and its first Protocol would be violated.

An Uphill Battle for Investors

Both *PL Holdings* and *Novenergia* demonstrate that investors defending intra-EU investment awards in Sweden face an uphill battle. The CJEU's ruling in *PL Holdings* was prompted by a challenge initiated in Sweden by Poland against two awards rendered in favor of PL Holdings based on a BIT concluded by Poland with Belgium and Luxemburg. In December 2022, the Swedish Supreme Court (where the challenge was pending) annulled both awards based on the CJEU's ruling, finding the BIT's dispute resolution clause contrary to EU law.

The appellate court's judgment in *Novenergia* was rendered only one day before the Swedish Supreme Court's judgment in *PL Holdings*. Despite similar fact-patterns, the appellate court and the Swedish Supreme Court did not rely on the same legal grounds for declaring the respective awards invalid. The appellate court used Section 33 (1) (non-arbitrability) whereas the Swedish Supreme Court cited Section 33 (2) (violation of *ordre public*).

The Swedish Supreme Court also differed in respect of its assessment of the investor's due process defense. Both courts did concede that the CJEU's interpretation of EU law may be disregarded in the event of a "serious" and "unambiguous" violation of the ECHR. However, as opposed to the appellate court in the *Novenergia* case, the Swedish Supreme Court did not assess whether the legal system of the host-State (in that case Poland) satisfied basic due process requirements. Instead, it took an even more restrictive approach stating that "[t]o the extent the Polish legal system has such flaws in terms of rule of law that PL Holdings contends, taking necessary remedial measures is a task for the Polish judicial system in consultation with CJEU (where applicable)."

Notwithstanding the difference in the approaches taken by the two courts, the bottom line, however, remains the same – any intra-EU arbitral award rendered in an arbitration seated in Sweden is susceptible to invalidity challenges with a high likelihood of success. As noted in the introduction, this is hardly surprising given the firm position taken by the CJEU on these issues. What the outcomes of *Novenergia* and *PL Holdings* also show is that an investor relying on due process arguments as a defense against a challenge of an intra-EU award has a very challenging –

albeit perhaps not insurmountable – obstacle to overcome.

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This entry was posted on Tuesday, March 7th, 2023 at 8:46 am and is filed under Achmea, CJEU, Energy Charter Treaty, Intra-EU BITs, Intra-EU Investment Arbitration, Sweden
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