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## Can a Breach of Constitutional Law of the Host State Nullify Investment Protection? The Case of *Energía y Renovación Holdings v. Guatemala*

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In investment arbitration, it is widely recognized that to benefit from the protection of an investment treaty, the investment must be legal. Tribunals assess this legality either because the treaty explicitly mandates it (e.g., [Ecuador-Sweden BIT](#)) or because the tribunal assumes this authority even if the treaty is silent (e.g., [Worley v. Ecuador](#)). In either case, determining legality often involves interpreting not just treaty provisions but also the domestic laws of the host state. If the investment is found to breach domestic laws, especially those of constitutional importance, tribunals may deny protection (e.g., [Fraport v. Philippines II](#)).

The dispute in *Energía y Renovación Holdings S.A. (“E&R”) v. Republic of Guatemala* (“Guatemala” or the “State”) before the International Centre for Settlement of Investment Disputes (“ICSID”) stands out, as it questions whether a mere breach of a constitutional provision is sufficient to declare an investment illegal. This article focuses specifically on the Tribunal’s treatment of this issue, in light of Guatemala’s jurisdictional objection, which asserted that the investment was illegal and therefore outside the scope of the Tribunal’s jurisdiction.

### The Dispute

E&R filed a claim under the [Free Trade Agreement between Central America and Panama](#) (“Free Trade Agreement”). The dispute arose from the alleged inaction of Guatemalan authorities in preventing attacks by third parties that adversely affected E&R’s hydroelectric projects in the San Mateo Ixtatán region. E&R argued that the inaction from the State constituted expropriation and breached the Treaty’s standards of fair and equitable treatment, full protection and security, and national treatment.

### Guatemala’s Jurisdictional Objection

Guatemala contended that E&R’s investment violated Article 123 of its [Constitution](#), which prohibits foreign entities from owning real estate in the border areas of Guatemala. The State claimed that although the properties were formally held by Guatemalan entities, the true controllers

were Panamanian. Furthermore, the State argued that E&R misrepresented its ownership during permitting process, thereby tainting the legality of the entire investment.

E&R countered that its Panamanian ties were transparent and known to the authorities. Moreover, it emphasized that most properties were exempt from the prohibition in Article 123, and that ownership restrictions applied only to territory, not to shares or permits. E&R also emphasized that the State had not annulled property titles or challenged the ownership structure domestically and had in fact renewed all the licenses of the project.

### **Decision on the Legality of the Investment**

The Tribunal analyzed the jurisdictional objection in the [final award](#). The analysis started with the Tribunal asserting that the legality of an investment is a requirement under the Treaty, even if not explicitly stated. The Tribunal analyzed Article 123 of the Guatemalan Constitution and concluded that the provision contains two distinct legal scenarios: (1) assets registered before March 1, 1956, may remain under the ownership of foreign entities; and (2) assets registered after that date may not be owned by foreign entities. Based on this the Tribunal determined that 69% of the investment assets were registered under the first condition and thus complied with the constitutional requirement. However, the remaining 31% were registered under the second condition, falling within the constitutional prohibition against foreign ownership. As a result, this portion of the investment was found to be in violation of Article 123.

However, the Tribunal concluded that Guatemala did not demonstrate the legal effects resulting from the breach of Article 123. It emphasized that the State was responsible for showing the consequences of such a violation—for instance, whether the investment became null and void *ipso jure*. Additionally, Guatemala did not initiate any legal action in domestic courts to challenge the investment's validity. Instead, the Tribunal found it had implicitly accepted it by renewing E&R's licenses.

The Tribunal ultimately concluded that, since Article 123 does not explicitly define the legal consequences of foreign ownership of property registered after March 1, 1956, interpreting its implications falls within the exclusive jurisdiction of the Guatemalan Constitutional Court. Expert testimony presented by E&R confirmed that the Constitutional Court had not previously issued an authoritative interpretation of this provision. As a result, the Tribunal acknowledged that the authority to interpret Article 123 lies solely with the Constitutional Court in any future proceedings that Guatemala may initiate.

Based on the foregoing, the Tribunal rejected Guatemala's jurisdictional objection.

### **The Dissenting Opinion**

Dissenting opinions are relatively rare in investment arbitration, particularly in proceedings under the ICSID Convention (*see* [here](#)). Studies on the subject suggest this rarity is tied to a strong disincentive: arbitrators who issue dissenting opinions may be less likely to receive future appointments (*see* [here](#)). In practice, few arbitrators appear willing to jeopardize their prospects by stepping outside a unanimous decision.

Despite this trend, one of the arbitrators (“Dissenting Arbitrator”) issued a [dissenting opinion](#), expressing his disagreement with the majority’s reasoning—especially its treatment of the jurisdictional objection in the award. According to the Dissenting Arbitrator, it was impossible for Guatemala to initiate legal proceedings in domestic courts, as the State only became aware of the alleged illegality upon the commencement of the investment arbitration. Furthermore, the Dissenting Arbitrator maintained that Guatemala renewed the licenses and permits solely because E&R concealed the fact that the true owners were Panamanian nationals, not Guatemalan.

The Dissenting Arbitrator further argued that, had the Tribunal determined the legal consequences of breaching Article 123, such an interpretation would not have conflicted with any potential future rulings by Guatemalan courts. This was particularly true as no legal proceedings have been initiated at the national level by Guatemala. Lastly, to the Dissenting Arbitrator, any interpretation of such article would have applied solely within the context of the international dispute. Therefore, the award would not contradict any future domestic decisions.

Based on these arguments, the Dissenting Arbitrator concluded that it had enough reasons to dissent from the conclusions made by the majority of the Tribunal.

### **Is a Constitutional Breach Sufficient to Render an Investment Illegal?**

This is not the first time a tribunal has been asked to rule on a jurisdictional objection based on the alleged illegality of an investment under a State’s constitution. In recent years, ICSID tribunals—particularly in cases involving Latin American jurisdictions—have considered similar arguments. These cases highlight an emerging trend in which States invoke constitutional provisions not only as part of the factual or regulatory context, but as the central basis for asserting that an investment was made in violation of domestic law, thus rendering it ineligible for treaty protection.

For example, in *Álvarez and Marín v. Panama*, the respondent argued that the investment was unlawful because it violated Article 127 of the Panamanian Constitution, which designated the area where the investment was made as protected territory. The tribunal sided with the State, applying a structured, four-part test. It found that Panama had successfully demonstrated that:

1. the constitutional provision clearly prohibited investment in the protected territories;
2. the provision served a legitimate and significant public interest—namely, the protection of sensitive national territories;
3. domestic law explicitly established the legal consequence of such a violation, declaring the resulting real state titles null and void *ipso jure*; and
4. the Panamanian authorities had taken immediate legal action before national courts to enforce this consequence and establish the illegality of the titles and, therefore, the illegality of the investment.

This analysis was later applied in *Lee-Chin v. Dominican Republic*, reinforcing its credibility as a useful standard for assessing claims of illegality based on alleged breaches of constitutional law provisions

While the majority of the Tribunal in *E&R v. Guatemala* did not explicitly adopt the four-part test, its reasoning suggests that it implicitly applied similar criteria. This is evident from its conclusion

that Guatemala failed to meet key elements of the test—particularly its inability to demonstrate the legal consequences of the alleged constitutional breach and its failure to initiate timely legal proceedings at the domestic level. Accordingly, the Tribunal’s decision appears to be consistent with the criteria applied in previous ICSID comparable cases.

## Conclusion

In summary, recent trends show that tribunals require more than a claim of constitutional breach to declare an investment illegal. The party raising the objection based on a constitutional violation must demonstrate that:

1. a specific constitutional provision conflicts with the investment;
2. the constitutional provision serves a compelling public interest;
3. the constitution or other domestic law clearly stipulates the legal consequences of its violation, as tribunals are not to assume possible consequences through interpretation; and
4. the State has taken prompt and concrete legal steps to enforce those consequences.

In the absence of these key elements, tribunals are unlikely to uphold jurisdictional objections based on the alleged illegality of the investment. This recent trend, adopted by ICSID tribunals, represents an emerging position that could be considered a standard moving forward, especially since none of these awards have been subject to annulment to date.

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