

Energy Charter Treaty: International Trends Relating to Energy Dispute Resolution



## Energy Charter Treaty: international trends relating to energy dispute resolution

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This article is part of the Energy and Natural Resources Global Guide.

It aims to provide an overview of the Energy Charter Treaty and international trends relating to energy dispute resolution in particular, the background of the ECT; investment protection; dispute resolution and arbitration under the ECT and the future of the ECT.

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The beginning of 2016 saw a sharp decline in oil prices, which fell to almost US\$30 per barrel (compared to US\$100 per barrel almost 18 months ago). The effects of tumbling oil prices continue to be felt, particularly in an economy where oil exports accounted for an average 75% in 2014 to 2015, and oil revenues contributed almost 30% to the GDP.

In the early 1990s, the European states were in need of energy resources which the former Soviet states were able to provide. This resulted in the European Energy Charter Declaration (later solemnised as the Energy Charter Treaty (ECT)). Investments in the energy sector are largely promoted by a common framework established under the ECT. The changing economy has led to a shift of focus towards renewables, which in turn has generated positive interest among the state bodies.

While the oil and gas-led economies are still experiencing the financial distress that plunging oil prices have caused, the crucial enabling role played by the energy sector cannot be underestimated. The energy sector affects employment, growth and development on a larger scale than is usually conceded. The Abu Dhabi-based International Renewable Energy Agency (IRENA) released a market analysis that supported existing 2030 clean energy targets. If these targets are met in the Gulf Co-operation Council (GCC), green jobs will dominate the power sector to the tune of 210,000 direct jobs, with the majority expected to be in the solar photovoltaic power system industry in the United Arab Emirates (UAE) and Saudi Arabia (according to a published media statement).

In essence, the energy sector remains one of the prime focuses in the UAE. This article examines the international trends relating to dispute resolution in wake of the ECT.

### Background to the ECT

Signed in 1995, the ECT (which follows from the non-binding European Energy Charter Declaration 1991) is binding in nature. It is one of the primary international regulations in the energy sector. The ECT is the only binding multilateral treaty that specifically addresses government interactions and co-operation on a joint platform within the energy sector. The ECT's objective is to (*Article 2, ECT*):

*"...promote long-term co-operation in the energy field, based on complementarities and mutual benefits, in accordance with the objectives and principles of the Charter".*

52 countries (the EU and Euratom) are signatories to the ECT. The UAE and most of the other GCC countries have assumed "observer" status and have not signed the ECT or the International Energy Charter of 2015. The ECT's scope is limited to the energy sector. It focuses on several key considerations including investment protection, provisions on trade, transit of energy, energy efficiency and environmental protection, and dispute resolution.

## Investment protection

The ECT has gained favour due to its provisions relating to protection of foreign investment. Investment protection is discussed under Part III of the ECT, which aims to reduce the risks associated with investments by foreign state bodies. The investment protection provisions of Part III of the ECT (post-investment phase) apply to investments of investors. Article 1 defines "investment" and "investor". An investor is either a:

- Natural person with citizenship, nationality or permanent residence in a contracting party (that is, a state or regional economic integration organisation that has consented to be bound by the ECT under its applicable law).
- Company or other organisation organised under the law applicable in that contracting party.

Investment is any kind of asset associated with an economic activity in the energy sector, which is owned or controlled directly or indirectly by an investor, and includes:

- Tangible and intangible, and movable and immovable property and any property rights such as leases, mortgages, liens and pledges.
- A company or business enterprise, or shares, stock or other forms of equity participation in a company or business enterprise, and bonds and other debt of a company or business enterprise.
- Claims to money and claims to performance under a contract having an economic value and associated with an investment.
- Intellectual property.
- Returns.
- Any right conferred by law or contract, or by virtue of any licences and permits granted under law, to undertake any economic activity in the energy sector.

"Economic activity in the energy sector" means economic activity concerning exploration, extraction, refining, production, storage, land transport, transmission, distribution, trade, marketing or sale.

Each contracting party must encourage and create stable, equitable, favourable and transparent conditions for investors of other contracting parties to make investments in its area (*Article 10(1), ECT*). These conditions include a commitment to give investments of investors of other contracting parties fair and equitable treatment at all times. These investments must also be given protection and security, and no contracting party can in any way impair by unreasonable or discriminatory measures their management, maintenance, use, enjoyment or disposal. Investments must not be given treatment less favourable than that required by international law, including treaty obligations. Each contracting party must observe any obligations it has entered into with an investor or an investment of any other contracting party.

## Dispute resolution

### Arbitration under the ECT

Article 26 of the ECT provides a dispute resolution mechanism. An investor (*see above, Investment protection*) of a contracting party can bring a claim against another contracting party relating to an investment in that other party's area, if the dispute qualifies under Article 26(1) of the ECT. This Article provides that the dispute must concern an alleged breach of the other contracting party's obligations under Part III. These disputes must, if possible, be settled amicably. If amicable and mutual settlement fails and a consultation period of three months passes, the parties can address the matter either (*Article 26(2)(a) to (c), ECT*):

- Before the courts or administrative tribunals of the contracting party where investments were made.
- In accordance with any applicable, previously agreed dispute settlement procedure.

Generally speaking, the ECT does not set out:

- The manner in which a dispute must be addressed.
- The amount of compensation.
- Provisions relating to liquidated damages.
- Provisions which a bilateral treaty may generally address.

These provisions are therefore usually agreed between the parties based on prior dealing and market trends.

### **Modes of international arbitration**

Article 26(c) of the ECT allows investors to resort to international arbitration under Article 26(4) of the ECT. Investors can choose one of the following modes of international arbitration:

- Arbitration before the International Centre for Settlement of Investment Disputes (ICSID), established under the Convention on the Settlement of Investment Disputes between States and Nationals of other States 1965 (ICSID Convention). This is applicable only if both parties to the dispute are parties to the ICSID Convention.
- The ICSID established, under the rulings governing the Additional Facility for the Administration of Proceedings by the Secretariat of the Centre, that where the contracting party of the investor or the contracting party to the dispute, but not both, is a party to the ICSID Convention.
- Arbitration administered by a sole arbitrator or ad hoc arbitration tribunal established under the Arbitration Rules of the United Nations Commission on International Trade Law (UNCITRAL).
- Arbitral proceedings before the Arbitration Institute of the Stockholm Chamber of Commerce.

The wide choice has led to countries' increased willingness to be a signatory to the ECT. Being a signatory allows greater flexibility in terms of procedures.

### **Nature of consent**

Each contracting party should give unconditional consent to the submission of a dispute to international arbitration or conciliation (*Articles 26 and 27, ECT*). This unconditional consent implies that a state cannot withdraw from the ECT, on the request of the investor to commence arbitral proceedings.

A contracting party remains bound to honour its investment protection obligations for 20 years following the effective date of a withdrawal from the ECT (*Article 47, ECT*).

The consent to international arbitration of the contracting parties listed in Annex ID is limited. Where the investor has previously submitted the dispute to the national courts of the host state or under another previously agreed dispute settlement procedure, it cannot then pursue international arbitration in respect of the same dispute (*Article 26(3) (b), ECT*).

In addition, consent given under Article 26(3) of the ECT together with the investor's written consent given under Article 26(4) satisfies the requirement for (*Article 26(5), ECT*):

- The parties' written consent to a dispute for the purposes of Chapter II of the ICSID Convention under the "additional facility rules".
- Written agreement for the purposes of Article II of the UN Convention on the Recognition and Enforcement of Foreign Arbitral Awards 1958 (New York Convention).
- Written agreement for the purposes of Article 1 of the UNCITRAL Arbitration Rules.

Any arbitration under Article 26(5) of the ECT must, at the request of any party to the dispute, be held in a state that is a party to the New York Convention. Claims submitted to arbitration under the ECT are considered to arise out of a commercial relationship or transaction for the purposes of Article I of the New York Convention.

### Applicable law, award and nationality

Arbitration must be held in accordance with the provisions of the ECT and the applicable rules and principles of international law (*Article 26(6), ECT*). A tribunal established under Article 26(4) of the ECT decides the issues in dispute.

Where amicable resolution of a dispute is not possible within three months from the date on which either party to the dispute requested amicable settlement, the investor party to the dispute can invoke provisions contained in Article 26(2) of the ECT. This involves a referral of the matter to the courts or administrative tribunals of the contracting party to the dispute in accordance with either:

- Any applicable, previously agreed dispute resolution process.
- Provisions contained within Article 26(4) of the ECT.

Investors must (where both parties are parties to the International Centre for Settlement of Investment Disputes (ICSID)) provide a written consent to submit the dispute to the ICSID (*Article 26(5), ECT*).

In relation to enforcement and execution of awards, the investor can request for arbitration proceedings to be held in a state which is party to the New York Convention (*Article 26 (5) (b), ECT*). These claims are considered to arise out of a commercial relationship or transaction as defined under Article I of the New York Convention.

Awards issued under these procedures are final and binding (*Article 26(8), ECT*).

If an investor is a body corporate from the contracting party that is allegedly in breach of its obligations, but was controlled by investors from another contracting party before the dispute arose, it is treated as the national of that other contracting party for the purposes of Article 25(2)(b) of the ICSID Convention (*Article 26(7), ECT*).

### Disputes over application or interpretation

Any dispute between the contracting parties relating to application or interpretation of the ECT must be settled through diplomatic channels (*Article 27, ECT*). If a dispute is not settled under Article 27(1) within a reasonable time frame, it may be submitted to an ad hoc tribunal under Article 27(2). Article 27(3) provides how the tribunal must be constituted.

### Cases

The number of cases before the arbitration bodies relating to ECT are limited. The number of cases under the ECT grew, with the total number of cases reaching 93 as at May 2016. The increase in the number of cases was largely due to Spain's decision to reduce incentives and tariffs for solar projects retrospectively. This decision resulted in 16 joint cases by groups of investors under the ICSID rules.

As at May 2016, there are 30 cases against Spain, six against the Russian Federation, six against Italy, five against the Republic of Turkey, seven against the Czech Republic, five against the Republic of Kazakhstan and five against Hungary.

A leading case before the ICSID is *Case No. ARB/03/24 Plama Consortium Limited v Republic of Bulgaria*. Plama Consortium Limited (Plama) (a Cypriot company) purchased an equity interest in Nova Plama (a Bulgarian company), that owns an oil refinery in Bulgaria. Plama claimed that Bulgaria interfered with the operation of the oil refinery in a manner that was inconsistent with Bulgaria's international law obligations under both the ECT and the Bulgaria-Cyprus BIT Bilateral Investment Treaties 1987.

In its decision on jurisdiction of 8 February 2005, the tribunal retained jurisdiction to consider the merits of Plama's argument that Bulgaria had breached the ECT, while determining that it did not have jurisdiction under the Cyprus-Bulgaria Treaty. The tribunal held that on grounds of merit, Bulgaria's allegations against Plama on misrepresentation were admissible. The plan to get the refinery to yield a profit did not work for reasons which were not attributable to any unlawful actions of Bulgaria (*ibid* 92 [305]).

## Outlook for the ECT

The ECT is comparatively new but the number of registered matters have been increasing. The Energy Charter Secretariat had 51 registered claims in 2014, compared to 93 in 2016. The ECT provisions could also increase the chances of settlement between the parties. For example, in *Slovak Gas Holding BV, GDF International SAS and E.ON Ruhrgas International GmbH v Slovak Republic* (ICSID Case No. ARB/12/7), following appointment of three arbitrators in August 2012, the parties requested the Tribunal in December 2012 to suspend the proceedings. The Tribunal suspended the proceedings until June 2013. Under mutual negotiations and understanding, the parties managed to record the settlement within 30 days and submitted the settlement agreement before the Tribunal under Rule 43(2) of the ICSID. On 19 March 2013, the Tribunal rendered its award embodying the parties' settlement.

Australia, Belarus (provisional applicant), Iceland, Norway and Russia have signed the ECT but have not ratified it. There have been cases where jurisdictions have chosen to withdraw from arbitration under investment treaties which pose a challenge to the ECT's framework and ICSID's powers to adjudicate in these cases. The ECT's future and outlook looks positive, but governing bodies including ICSID's powers in terms of adjudication and preventing states from withdrawing, are some of the key areas that need attention.

### Contributor profiles

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#### Recent transactions

- Acting on large number of transactions within the energy, mining and oil and gas sectors.
- Advising on the acquisition of mines in the UAE, Oman, Australia and India.
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- Acting on acquisition of other companies engaged in the energy sector including power distribution, oil and gas.

**Languages.** English, Urdu, Hindi.

#### Publications

- Musataha Agreements Under UAE Law.
- Foreign Direct Investment in India.
- Share Pledge for Commercial Facilities.
- New UAE Commercial Companies Law - Detailed Insight and Review.
- Hotel Management Agreements in the UAE.



- Cross Border Crime and Extradition.
- Private Joint Stock Companies and UAE Law.
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- Doing Business in Iraq.
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### Resource information

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