The Energy Charter Treaty

An Overview

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1. INTRODUCTION

The purpose of this paper is to give an overview of the investment protection regime of the Energy Charter Treaty (the "ECT") and to comment on the arbitral awards rendered so far under the Energy Charter Treaty (the "ECT"). To date, fifteen cases have been brought to international arbitration by investors under the ECT.[1] Eleven of these cases are still pending[2] and two have been settled by the parties[3]. In two cases under the Rules of the Stockholm Chamber of Commerce – *Nykomb Synergetics Technology Holding AB v. the Republic of Latvia* and *Petrobart Limited v. the Kyrgyz Republic* – the respective arbitral tribunals have issued final awards on the merits. In the ICSID arbitration *Plama Consortium Limited v. Republic of Bulgaria*, the tribunal has issued an award on jurisdiction. Thus, decisions rendered on the investment protection provisions of the ECT are still rather limited in number, but these three awards nevertheless raise a number of issues of general interest regarding the application of the ECT.

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[1] AES Summit Generation Ltd. (UK subsidiary of US-based AES Corporation) v. Hungary (ICSID Case no ARB/01/4); Nykomb Synergetics Technology Holding AB (Sweden) v. Latvia (SCC- Case no 118/2001); Plama Consortium Ltd. (Cyprus) v. Bulgaria (ICSID Case no ARB/03/24); Petrobart Ltd, (Gibraltar) v. Kyrgyzstan (SCC-Case no 126/2003); Alstom Power Italia SpA, Alstom SpA (Italy) v. Mongolia (ICSID Case no ARB/04/10); Yukos Universal Ltd, (UK - Isle of Man) v. Russian Federation (UNCITRAL Arbitration Rules); Hulley Enterprises Ltd. (Cyprus) v. Russian Federation (UNCITRAL Arbitration Rules); Veteran Petroleum Trust (Cyprus) v. Russian Federation (UNCITRAL Arbitration Rules); Ioannis Kardossopoulos (Greece) v. Georgia (ICSID Case no ARB/05/18); Amto (Latvia) v. Ukraine (SCC); Hrvatska Elektropriveda d.d. (HEP) (Croatia) v. Republic of Slovenia (ICSID Case no ARB/05/24); Libananco Holdings Co. Limited (Cyprus) v. Republic of Turkey (ICSID Case no ARB/06/8); Azpetrol International Holdings B.V, Azpetrol Group B.V. and Azpetrol Oil Services Group B.V (Netherlands) v. Azerbaijan (ICSID Case no ARB/06/15); Cementownia "Nowa Huta" S.A, (Poland) v. Republic of Turkey (ICSID Case no ARB(AF)/06/2); Europe Cement Investment and Trade S.A. (Poland) v. Republic of Turkey (ICSID).

[2] Plama Consortium Ltd. (Cyprus) v. Bulgaria (ICSID Case no ARB/03/24); Yukos Universal Ltd. (UK - Isle of Man) v. Russian Federation (UNCITRAL Arbitration Rules); Hulley Enterprises Ltd. (Cyprus) v, Russian Federation (UNCITRAL Arbitration Rules); Veteran Petroleum Trust (Cyprus) v. Russian Federation (UNCITRAL Arbitration Rules); Ioannis Kardossopoulos (Greece) v. Georgia (ICSID Case no ARB/05/18); Amto (Latvia) v. Ukraine (SCC); Hrvatska Elektropriveda d.d. (HEP) (Croatia) v. Republic of Slovenia (ICSID Case no ARB/05/24; Libananco Holdings Co. Limited (Cyprus) v. Republic of Turkey (ICSID Case no ARB/06/8); Azpetrol International Holdings B.V, Azpetrol Group B.V. and Azpetrol Oil Services Group B.V (Netherlands) v. Azerbaijan (ICSID Case no ARB/06/15); Cementownia "Nowa Huta" S.A. (Poland) v. Republic of Turkey (ICSID Case no ARB(AF)/06/2); Europe Cement Investment and Trade S.A. (Poland) v. the Republic of Turkey (ICSID).

[3] AES Summit Generation Ltd. (UK subsidiary of US-based AES Corporation) v. Hungary (ICSID Case no ARB/01/4) and Alstom Power Italia SpA, Alstom SpA (Italy) v. Mongolia (ICSID Case no ARB/04/10).

2. OVERVIEW OF THE ENERGY CHARTER TREATY

2.1 *BACKGROUND*

In the early 1990s, various ideas were discussed on how to develop energy cooperation between Eastern and Western Europe. Russia and many of its neighbouring countries were rich in energy but in great need of investment to reconstruct their economies. At the same time, Western European countries were trying to diversify their sources of energy supplies to decrease their potential dependence on other parts of the world. There was, therefore, a recognized need to set up a commonly accepted foundation for energy cooperation between the states of the Eurasian continent. It was out of this need that the Energy Charter Process was born.[4]

The first formal step in the Energy Charter process was the adoption and signing of the European Energy Charter (the "EEC") in December 1991. The EEC was not a binding international treaty, but rather a political declaration of principles which the signatories declared themselves intent on pursuing. However, the EEC contained guidelines for the negotiation of what was later to become the Energy Charter Treaty (the "ECT") and a set of protocols.[5]

The ECT and the Energy Charter Protocol on Energy Efficiency and Related Environmental Aspects were signed in December 1994 and entered into force in April 1998. As of today, the ECT has been signed by 51 states and the European Union. The treaty has been ratified by 45 states and the European Union.[6] It is noteworthy that the Russian Federation has signed but not ratified the treaty. The Russian Federation has, however, accepted provisional application of the treaty.[7]

The ECT is a multilateral treaty with binding force, limited in its scope to the energy sector. The purpose of the ECT, as stipulated in Article 2, is to "*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*". It is the only binding multilateral instrument dealing with inter-governmental cooperation in the energy sector, and contains far reaching undertakings for the contracting parties. The ECT includes provisions regarding investment protection, provisions on trade, transit of energy, energy efficiency and environmental protection and dispute resolution.

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[4] *See e.g.* Graham Coop, The Energy Charter Treaty: More than a MIT, in C. Ribeiro (ed.), Investment Arbitration and the Energy Charter Treaty, p. 4–9.

[5] Bamberger, Linehan, Waelde, Chapter from Energy Law in Europe, edited by Roggenkamp Martha M, Ronne Anita, Redgwell Catharine, Inigo Del Guayo, The Energy Charter Treaty in 20●●: In a New Phase.

[6] The ECT has been signed by Albania, Armenia, Austria, Australia, Azerbaijan, Belarus, Belgium, Bosnia and Herzegovina, Bulgaria, Croatia, Czech Republic, Cyprus, Denmark, Estonia. European Communities, Finland, France, Georgia, Germany, Greece, Hungary, Iceland, Italy, Japan, Kazakhstan, Kyrgyzstan, Latvia, Liechtenstein, Lithuania, Luxembourg, Malta, Moldavia, Mongolia, Netherlands, Norway, Poland, Portugal, Romania, Russian Federation, Slovakia, Slovenia, Spain, Sweden, Switzerland, Tajikistan, The former Yugoslav Republic of Macedonia, Turkey, Turkmenistan, Ukraine, Uzbekistan, United Kingdom. Signatory States that have not yet ratified the ECT are Australia, Belarus, Iceland, Norway, Russian Federation.

[7] *See* section 5, *infra.*

2.2 *Investment Promotion and Protection*

The provisions of the ECT regarding foreign investments are considered to be the cornerstone of the treaty. The aim of the foreign investment regime is to create a "*level playing field*" for investments in the energy sector and to minimize the non-commercial risks associated with such investments. Under the ECT, a distinction is made between the pre-investment phase of making an investment and the post-investment phase relating to investments already made. While the provisions concerning the pre-investment phase primarily set up a "soft" regime of "best endeavour" obligations, the ECT creates a "hard" regime for the post-investment phase with binding obligations for the contracting states similar to the investment protection provisions of the North American Free Trade Agreement (NAFTA) and bilateral investment treaties (BITs).[8] The investment protection regime is discussed in more detail in section 3 below.

2.3 *Dispute Settlement*

Dispute settlement is regulated in Part V of the ECT (Articles 26–28). Article 26 of the ECT governs investment disputes between private investors and contracting states, and extends to investors a right to arbitration of such disputes (see section 4 below). Article 27 regulates resolution of state-to-state disputes between contracting parties concerning the application or interpretation of the ECT (not limited to matters of investments). The ECT also contains special provisions for the resolution of trade disputes (see section 2.4 below), a conciliation procedure for transit disputes (see section 2.5 below) and consultation procedures for competition and environmental disputes.[9]

2.4 *Trade*

The ECT's trade provisions, based on the trading regime of the GATT and the Trade Amendment to the ECT of 1998 (bringing the ECT into line with WTO rules and practises)[10], are founded on the principles of non-discrimination, transparency and a commitment to the progressive liberalisation of international trade.

Thus, the ECT introduces the trade provisions of GATT/WTO to the energy sector. The importance of this is that when the ECT entered into force in 1998, 19 of its members were not parties to the WTO. In 2006, 9 members were still non-parties to the WTO.

Disputes regarding compliance with the trade provisions under Article 29 and Article 5 are to be settled in accordance with the provisions for trade dispute settlement

[8] Cf. Bamberger, Linehan, Wälde, *op. cit.*

[9] For a general overview of the various dispute settlement mechanisms of the ECT, *see e.g.* L. Gouiffes, The Dispute Settlement Mechanisms of the Energy Charter Treaty, in C. Ribeiro (ed.), Investment Arbitration and the Energy Charter Treaty, p. 22–34.

[10] The Trade Amendment has, as of August 2006, been ratified by 30 states and the European Union.

in Annex D to the ECT. The dispute settlement mechanism set out in Annex D is modelled on the WTO panel model with certain modifications.

2.5 *TRANSIT*

An important part of the ECT are the rules for facilitation of the transit of energy through the participating states. The transit regime is based on freedom of transit and the principle of non-discrimination. In addition to the existing transit provisions of the ECT, the participating states commenced negotiations in 2000 on the enhancement of these rules in the form of a Transit Protocol. However, due to differences in opinion between the Russian Federation and the European Union, the negotiation of such a protocol has not yet been concluded.[11]

"Transit", according to the ECT, is defined as "*carriage through the area of a Contracting Party, or to or from port facilities in its area for loading or unloading, of Energy Materials and Products originating in the area of another state and destined for the area of a third state, so long as either the other state or the third state is a Contracting Party*".[12] If a contracting party is listed in Annex N, "transit" also includes the carriage originated and destined for the same contracting party in cases where the products are transferred through the territory of another contracting party.

Article 7(1) establishes the principles of freedom of transit and non-discrimination. According to this provision "*each Contracting Party shall take the necessary measures to facilitate the Transit of Energy Materials and Products consistent with the principle of freedom of transit and without distinction as to the origin, destination or ownership of such Energy Materials and Products or discrimination as to pricing on the basis of such distinctions, and without imposing any unreasonable delays, restrictions or charges*".

According to Article 7(3) each contracting party undertakes that its provisions relating to transport of "Energy Materials and Products" and the use of energy transport facilities shall treat such materials and products in transit in no less favourable a manner than its provisions treat such materials and products originating in or destined for its own area.

The contracting parties have also undertaken not to place obstacles in the way of new capacities being established in the event that transit of "Energy Materials and Products" cannot be achieved on commercial terms by means of energy transport facilities. However, contracting parties are not under any obligation to accept new capacities when legislation on environmental protection, land use, safety, or technical standards provides otherwise.

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[11] Official website of the Energy Charter Secretariat, http://www.encharter.org/index.jsp?psk=1102&ptp=tDetail.jsp&pci=254&pti=26 (7 August 2006).

[12] Energy Materials and Products means, *inter alia*, nuclear energy, coal, natural gas, petroleum products, electrical energy and fuel wood.

Paragraph 6 of Article 7 contains the important provision that, a contracting party is not entitled to interrupt or reduce the existing flow of "Energy Materials and Products" in the event of a dispute over any matter arising from the transit, except where this is specifically provided for in a contract or other agreement governing such transit, or permitted in accordance with the conciliator's decision in accordance with paragraph 7 of Article 7. Paragraph 7 sets out the possibility of appointing a special conciliator, via the Secretary-General of the ECT, in the case of a dispute regarding the transit of Energy Materials and Products. However, the appointment of a conciliator is subject to the exhaustion of all relevant contractual or other dispute resolution remedies previously agreed between the parties to the dispute, or between entities subject to their control.

2.6 *Energy Efficiency*

Energy efficiency is regulated by the Energy Charter Protocol on Energy Efficiency and Related Environmental Aspects (PEEREA). PEEREA was signed together with the ECT in 1994 and entered into force in April 1998. PEEREA requires the participating states to create policies to improve the efficiency of energy use and to minimize its negative effects on the environment. The objectives of PEEREA are illustrated in the second paragraph of Article 1 of the PEEREA. These objectives include the promotion of "*energy efficiency policies consistent with sustainable development*", the creation of "*framework conditions which induce producers and consumers to use energy as economically, efficiently and environmentally soundly as possible, particularly through the organization of efficient energy markets and a fuller reflection of environmental costs and benefits*", and the fostering of "*co-operation in the field of energy efficiency*".

2.7 *The Institutions*

The governing and decision-making body for the Energy Charter Process is the Energy Charter Conference. The conference is an inter-governmental organization established by the ECT. All States that have signed or acceded to the ECT are members of the conference. The duties of the Energy Charter Conference are carried out by its Secretariat, which is composed of a Secretary-General and a staff consisting of various experts from the energy sector.

3. Investment Protection

3.1 *Introduction*

The investment protection provisions of the ECT are found in Part III of the ECT. The aim of the provisions is to establish equal conditions for investments in the energy sector and thereby limit the non-commercial risks connected with such investments.

The ECT separates two phases of investment protection and affords them different levels of protection. As indicated above in section 2.2, the provisions concerning the pre-investment phase primarily set up a "soft" regime of "best endeavour" obligations, whereas the ECT creates a "hard" regime for the post-investment phase with binding obligations for the contracting states similar to the investment protection provisions of the North American Free Trade Agreement (NAFTA) and bilateral investment treaties (BITs).[13]

3.2 *SCOPE OF PROTECTION*

The investment protection provisions of Part III of the ECT (post-investment phase) are applicable to *Investments of Investors.* "Investment" and "Investor" as referred to in the ECT are defined in Article 1.

An "Investor" is a natural person having the citizenship or nationality of, or is a permanent resident in, a contracting state in accordance with its applicable law, or a company or other organization organized in accordance with the law applicable in that contracting state.

"Investment" means every 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: (a) tangible and intangible, and movable and immovable, property, and any property rights such as leases, mortgages, liens, and pledges; (b) 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; (c) claims to money and claims to performance pursuant to a contract having an economic value and associated with an Investment; (d) Intellectual Property; (e) Returns; (f) any right conferred by law or contract or by virtue of any licences and permits granted pursuant to law to undertake any "Economic Activity in the Energy Sector".

"Economic Activity in the Energy Sector" means economic activity concerning the exploration, extraction, refining, production, storage, land transport, transmission, distribution, trade, marketing, or sale of "Energy Materials and Products" except those included in Annex NI, or concerning the distribution of heat to multiple premises.

The scope of protection pursuant to Part III of the ECT also delineates the right to arbitration under Article 26, since the Investor's right to arbitration is limited to disputes between a "Contracting Party" and an "Investor" of another "Contracting Party" relating to an "Investment" of the "Investor" in the Area of the first "Contracting Party".

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[13] T. Wälde, Investment Arbitration Under the Energy Charter Treaty – From Dispute Settlement to Treaty Implementation, Arbitration International, Vol. 12 No. 4 (1996), p.437.

3.3 *MINIMUM STANDARD OF INVESTMENT PROTECTION – ARTICLE 10(1)*

Article 10(1) sets out a number of basic principles for the treatment of foreign investments that are frequently found in BITs. Article 10(1) provides that:

> "each Contracting Party shall, in accordance with the provisions of this Treaty, encourage and create stable, equitable, favourable and transparent conditions for Investors of other Contracting Parties to make Investments in its Area. Such conditions shall include a commitment to accord at all times to Investments of Investors of other Contracting Parties *fair and equitable treatment*. Such Investments shall also enjoy the most constant *protection and security* and no Contracting Party shall in any way impair by *unreasonable or discriminatory measures* their management, maintenance, use, enjoyment or disposal. In no case shall such Investments be accorded treatment less favourable than that required by international law, including treaty obligations. Each Contracting Party shall *observe any obligations it has entered into* with an Investor or an Investment of an Investor of any other Contracting Party".

FAIR AND EQUITABLE TREATMENT

Whereas the first sentence of Article 10(1) is a general statement regarding the favourable investment climate that contracting parties are required to provide qualifying investments, the second sentence of Article 10(1) explains that such favourable conditions "*shall include a commitment to accord at all times to Investments of Investors... fair and equitable treatment*". This standard of "fair and equitable treatment" is derived from international law, and has, through its frequent application by tribunals in BIT and NAFTA arbitrations, become an important principle of investment protection. Although certain principles have developed in arbitral practice (good faith, protection of legitimate expectations, due process, proportionality etc[14]), the exact scope and meaning of fair and equitable treatment is not easily described in general terms. The application of the principle is often fact-specific and requires in-depth factual assessment as well as application of standards of good-government conduct.[15] As with any flexible standard, it is a challenge for counsel and arbitrators to establish sources for good-government conduct that are relevant and suitable in the context of an individual case. In the absence of such an approach, there is a risk that a case will be decided on the basis of the arbitrators' individual perceptions of what is fair and equitable in the circumstances of the case.

As indicated above, tribunals applying the principle of fair and equitable treatment have found it to include principles such as the protection of legitimate investor expectations with respect to the maintenance of a stable and predictable business and

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[14] *See e.g. MTD Equity San. Bhd. & MTD Chile S.A. v. Chile*, ICSID Case No. ARB/01/7 (Malaysia/Chile BIT), Award, 25 May 2004; *Waste Management, Inc. v. Mexico (Number 2)*, ICSID Case No. ARB(AF)/00/3 (NAFTA), Final Award, 30 April 2004; *CMS Gas Transmission Company v. Argentina*, ICSID Case No. ARB/01/8 (United States/Argentina BIT), Final Award, 12 May 2005; *Azinian, Davitian & Baca v. Mexico*, ICSID Case No. ARB(AF)/97/2 (NAFTA), Award, 1 November 1999; *Metalclad Corporation v. Mexico*, ICSID Case No. ARB(AF)/97/1 (NAFTA), Award, 30 August 2000; *Tecnicas Medioambientales Tecmed, S.A. v. Mexico*, ICSID Case No. ARB(AF)/00/2 (Spain/Mexico BIT), Award, 29 May 2003.

[15] Cf. T. Wälde, Investment Arbitration under the Energy Charter Treaty: An Overview of Key Issues, Transnational Dispute Management, vol. 1:2 (2004).

legal environment by the host government, the principle of transparency, the good-faith and abuse of rights principles, due process, proportionality and the prohibition on arbitrariness.[16] References to the prohibition on arbitrariness and requirements of transparency are frequently made within the general framework of due process, which must be observed by courts and authorities of the host state.

MOST CONSTANT PROTECTION AND SECURITY

The first part of the third sentence of Article 10(1) of the ECT provides that investments shall enjoy the "most constant protection and security". The precise meaning of this standard within the context of the ECT is somewhat unclear, but it has been argued that it includes – apart from police protection from riots and similar physical attacks on the investment – a duty of the state to protect the normal ability of the investor's business to function in a level playing field.[17]

DISCRIMINATION

The second part of the third sentence of Article 10(1) provides that the management, maintenance, use, enjoyment or disposal of investments is not to be impaired by "*unreasonable or discriminatory measures*". The reference to unreasonable or discriminatory measures links the standard laid down in the third sentence of Article 10(1) to the principle of fair and equitable treatment. Thus, there is a certain overlap between the two standards. In the first award ever issued under the ECT, *Nykomb Synergetics Technology Holding AB v. the Republic of Latvia*, the tribunal found that Latvia had breached its obligation under the ECT not to discriminate against the foreign investor by offering higher tariffs for electricity to other companies and failing to present any evidence as to why those companies should be treated differently (see section 6 below).

UMBRELLA CLAUSE

The last sentence of Article 10(1) emphasises the principle of *pacta sunt servanda* by making it an obligation of each Contracting Party to "*observe any obligations it has entered into with an Investor or an Investment of an Investor of any other contracting party*". Thus, a breach of such an obligation covered by Article 10(1) may constitute a violation of a Contracting Party's obligations under the ECT. The precise scope of this so-called "umbrella clause" remains to be determined by tribunals applying the ECT. In particular, it is unclear as to whether it encompasses exclusively commercial conduct of state owned companies or is limited to conduct involving certain elements of government authority. Some tribunals applying similar clauses in BITs have attempted to draw a line

[16] *See* note 9 above.

[17] T. Wälde, Investment Arbitration under the Energy Charter Treaty; An Overview of Key Issues, Transnational Dispute Management, vol. 1:2 (2004).

excluding disputes which are exclusively or predominantly commercial in nature. However, even if such a distinction is accepted under the ECT, the difficult task remains of deciding what conduct is commercial, and what is governmental.[18]

It should be noted that Articles 26(3)(c) and 27(2) of the ECT allow for the contracting parties listed in Annex IA to exclude disputes covered by the umbrella clause from dispute resolution under Article 26 of the ECT.[19]

It could also be argued that the umbrella clause in Article 10(1), when read together with Article 22, may have far-reaching implications on, *inter alia*, commercial contracts for the sale of goods and the delivery of services where such contracts have been entered into by an investor and a legal entity controlled or owned by the host state. According to Article 22(1), a state enterprise of the host state "*...shall conduct its activities in relation to the sale of or provision of goods and services in its Area in a manner consistent with the Contracting Party's obligations under Part III of this Treaty*". In light of Article 10(1), assuming a wide interpretation of the umbrella clause, it could be argued that the host state may become responsible under the ECT (in addition to any liability of the state owned company under the commercial agreement) for a wide range of actions or omissions of state enterprises in the fulfilment of agreements for the sale of goods and delivery of services.

3.4 *MOST FAVOURED NATION TREATMENT*

The fourth sentence of Article 10(1) states that investments in no case shall be accorded "*treatment less favourable than that required by international law, including treaty obligations*"' and Article 10(7) provides that: "*Each Contracting Party shall accord to Investments in its Area of Investors of other Contracting Parties, and their related activities including management, maintenance, use, enjoyment or disposal, treatment no less favourable than that which it accords to Investments of its own Investors or of the Investors of any other Contracting Party or any third state and their related activities including management, maintenance, use, enjoyment or disposal, whichever is the most favourable.*"

Thus, according to Article 10(1), if another treaty to which the state hosting the investment is a party provides for better treatment of investments, this treatment must be "imported" into the ECT. The wording "treaty obligations", however, does not include decisions taken by international organizations or treaties entered into force before 1 January 1970, according to an Understanding in the Final Act of the Energy Charter Conference. Thus, stronger investment protections and guarantees contained in a bilateral investment treaty to which the host state is a party will be available to an investor, even if the investor's home state has not entered into a bilateral investment treaty with the host state.

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[18] *See e.g.* T. Wälde, Contract Claims under the Energy Charter Treaty's Umbrella Clause: Original Intentions versus Emerging Jurisprudence, in C. Ribeiro (ed.), Investment Arbitration and the Energy Charter Treaty, p. 205–236.

[19] Australia, Hungary and Norway have made such a reservation.

Article 10(7) expresses the principle of national, or most-favoured-nation (MFN) treatment. This treatment is afforded not only to the investments of investors but also to activities related to investments including management, maintenance, use, enjoyment or disposal.

The national treatment standard implies non-discrimination since the treatment of investments shall be "*no less favourable than that which it accords to Investments of its own Investors*". However, in comparison to WTO law or EU law, the concept of non-discrimination is less developed in investment law.[20]

Thus, most-favoured-nation treatment incorporates standards and rights contained in other treaties, or legislation, or beneficial treatment otherwise afforded to other investors into the protection offered to investors by the ECT.

Another interesting and important provision is Article 10(12) of the ECT. This provision stipulates that "*[e]ach Contracting Party shall ensure that its domestic law provides effective means for the assertion of claims and the enforcement of rights with respect to Investments, investments agreements, and investment authorizations*".

This provision was applied in the *Petrobart* case.[21]

3.5 *ARTICLE 13—EXPROPRIATION*

One of the most fundamental provisions of the investment protection regime of the ECT is Article 13, which deals with expropriation. Article 13(1), which resembles similar provisions of BITs and which confirms the principle of full compensation for expropriation, provides that:

> Investments of Investors of a Contracting Party in the Area of any other Contracting Party shall not be nationalized, expropriated or subjected to a measure or measures having effect equivalent to nationalization or expropriation (hereinafter referred to as "Expropriation") except where such expropriation is: (a) for a purpose which is in the public interest; (b) not discriminatory; (c) carried out under due process of law; and (d) accompanied by the payment of prompt, adequate and effective compensation.

Article 13(1) also provides that compensation must amount to the fair market value of the investment immediately before the expropriation, or impending expropriation, became known in such a manner as to affect the value of the investment. Interest at a commercial rate established from the date of expropriation until the date of payment is also included in the compensation.

The significance of the protection against expropriation is not primarily the protection against outright takings of investments by the host state, but rather the

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[20] C. Bamberger, J. Linehan, T. Waelde, Chapter from Energy Law in Europe, edited by Roggenkamp Martha M, Ronne Anita, Redgwell Catharine, Inigo Del Guayo, 'The Energy Charter Treaty in 2000: In a New Phase'.

[21] *See* Section 6, *infra*.

protections against "*measures having equivalent effect to nationalisation or expropriation*", i.e. various forms of indirect or creeping expropriation such as exorbitant regulations or confiscatory taxation that undermines the operation or enjoyment of the investment.

The effect of the protection provided by Article 13 is that irrespective of whether an expropriation is "lawful", i.e. carried out in accordance with the conditions set out in Article 13, or "unlawful", the investor is entitled to prompt, adequate and effective compensation. In the first case, compensation is a precondition for the lawfulness of the expropriation, and, in the latter case, compensation is equivalent to damages for the loss suffered by the investor as a result of the unlawful expropriation. Where an international treaty, such as the ECT, provides a standard of compensation for "lawful compensation", tribunals applying NAFTA or BITs, generally apply the same standard of compensation regardless of whether the expropriation is lawful or unlawful.[22]

3.6 *ARTICLE 17 – NON-APPLICATION OF PART III IN CERTAIN CIRCUMSTANCES*

In accordance with Article 17 of the ECT, each contracting party reserves the right to deny the advantages of Part III to an entity owned or controlled by investors of a state that is not a party to the ECT, if that entity has no substantial business activities in the area of the contracting party where it is organized. Furthermore, contracting parties can deny the advantages of Part III if it is established that the investment is an investment of an investor of a state that is not a party to the ECT, with which the host state does not maintain diplomatic relations, or as to which the host state upholds trade restrictions.

As has been evidenced by recent arbitral awards of tribunals established under the ECT, the interpretation of Article 17 raises difficult issues as to the meaning and effect of the provision (see section 6 below).

4. SETTLEMENT OF DISPUTES BETWEEN AN INVESTOR AND A CONTRACTING PARTY

4.1 *INTRODUCTION*

The right to arbitration of investment disputes set out in Article 26 is only one of the many dispute resolution mechanisms of the ECT. It is nonetheless arguably the most significant.

Article 26(1) covers: "*disputes between a Contracting Party and an* Investor *of another Contracting Party* relating to an Investment *of the latter in the Area of the former, which concern an* alleged breach of an obligation of the former under Part III". The definitions of these terms and thus the scope of the investor's right to dispute resolution in accordance with Article 26 have been described in section 2.2 above.

[22] A. Sheppard, The Distinction between Lawful and Unlawful Expropriation, in C. Ribeiro (ed.), Investment Arbitration and the Energy Charter Treaty, p. 169–199.

It should be emphasised that the right to arbitration, or other methods of dispute resolution, under Article 26 arises solely out of the ECT and is not subject to any requirement of exhaustion of local remedies, or any contractual dispute resolution mechanisms.

4.2 *AMICABLE SETTLEMENT*

In accordance with the first paragraph of Article 26, investment disputes (as defined above) must, if possible, be settled amicably. The investor may not submit a dispute for resolution in accordance with Article 26 until three months have elapsed from the date on which either party to the dispute requested amicable settlement. However, if a dispute cannot be settled amicably within three months, the dispute shall be resolved in a forum elected by the investor, as set forth in Article 26.

4.3 *THE INVESTOR'S CHOICE OF FORUM FOR DISPUTE RESOLUTION*

The investor has the choice of submitting an unresolved dispute covered by Article 26 to one of the following fora under Article 26(2)(a)-(c):

- the national court or administrative tribunals of the contracting party where the Investment was made,
- in accordance with a previously agreed dispute settlement procedure, or
- international arbitration.

Among the above three forms of dispute resolution, the right to international arbitration of investment disputes is by far the most important remedy available to investors for enforcing their rights under the ECT. According to Article 26(4), investors may elect any of the following forms of international arbitration:

- ICSID-arbitration (provided that both the host state *and* the investor's state have ratified the ICSID Convention);
- arbitration under the ICSID Additional Facility Rules (where either the host state *or* the home state of the foreign national, but not both states, have ratified the ICSID Convention);
- a sole arbitrator or *ad hoc* arbitral tribunal established under the UNCITRAL Arbitration Rules; or
- arbitral proceedings under the Arbitration Institute of the Stockholm Chamber of Commerce.

Thus, pursuant to Article 26(3)(a) each contracting party gives "*unconditional consent to the submission of a dispute to international arbitration or conciliation in accordance with the*

provisions of this article." This unconditional consent implies that a state cannot withdraw its consent, or withdraw from the ECT, upon the request of an investor to commence arbitral proceedings. The state's consent is irrevocable and its withdrawal would not be legally effective. In the case of a withdrawal from the ECT, the contracting party remains bound to honour its investment protection obligations for a period of 20 years following the effective date of its withdrawal, according to Article 47 of the ECT.

However, according to Article 26(3)(b), the consent to international arbitration of the contracting parties listed in Annex ID, is subject to the limitation that where the investor previously has submitted the dispute to the national courts of the host state or under another previously agreed dispute settlement procedure it may not then pursue international arbitration in respect of the same dispute. Almost half of the contracting parties have made such a "fork in the road" reservation. Furthermore, as described above in section 2.3, according to Article 26(3)(c), the contracting parties listed in Annex IA have limited their consent with respect to disputes arising under the umbrella clause in the last sentence of Article 10(1).[23]

4.4 *Applicable Law*

Article 26(6) provides that an arbitral tribunal established under paragraph 26(4) shall decide the issues in dispute in accordance with the ECT and the rules and principles of international law.

4.5 *Local Companies Controlled by Foreign Investors*

As regards the nationality of an investor, Article 26(7) ECT states that a legal entity which has the nationality of the contracting party to the dispute, but before the dispute between it and the contracting party arose, the local party was controlled by investors of another contracting party, the local party shall be treated as a "national of another Contracting State" for the purpose of Article 25(2)(b) of the ICSID Convention, and a "national of another State" for the purpose of Article 1(6) of the Additional Facility Rules. Hence, if the majority of shares of an investor of the same nationality as the host state are controlled by investors of another contracting state, the investor is to be viewed as an investor of another contracting party for purposes of establishing "diversity" jurisdiction for an arbitral tribunal constituted under the ICSID Rules or the ICSID Additional Facility Rules. Accordingly, the ECT creates a possibility for "local companies", which are owned or controlled by investors of another contracting party, to request international arbitration under the ECT against their "home states", and benefit from the investor protection of the ECT which may be more favourable than the protection available under national law. Difficult questions of parallel proceedings may arise, however, if claims under the ECT are brought simultaneously against the host state by the local company and its foreign shareholder.

[23] Australia, Hungary and Norway have made such a reservation.

5. PROVISIONAL APPLICATION OF THE ECT

5.1 *PROVISIONAL APPLICATION OF TREATY OBLIGATIONS*

Provisional application of a treaty means that treaty obligations are given effect prior to a state's formal ratification or accession to a treaty. The reasons for introducing the concept of provisional application may include, *inter alia*, that the treaty is urgently required to be implemented before it has been ratified, that the negotiators are certain that the treaty will obtain the required domestic approval for ratification, or that there is a desire to circumvent political or other obstacles to the entry into force of a treaty.[24]

The Vienna Convention on the Law of Treaties 1969 (the "Vienna Convention") explicitly allows for provisional application of treaties. Article 18 of the Vienna Convention imposes the obligation on a state to refrain from acts which would defeat the object and purpose of a treaty when the treaty has been *signed*, or when the state has expressed its consent to be bound by the treaty pending its entry into force. In addition, Article 25 of the Vienna Convention provides that a "*treaty or a part of a treaty is applied provisionally pending its entry into force if: (a) the treaty itself so provides; or (b) the negotiating states have in some other manner so agreed*" (emphasis added).

Article 45, in its entirety, reads as follows:

"PROVISIONAL APPLICATION

(1) Each signatory agrees to apply this Treaty provisionally pending its entry into force for such signatory in accordance with Article 44, to the extent that such provisional application is not inconsistent with its constitution, laws or regulations.

(2) (a) Notwithstanding paragraph (1) any signatory may, when signing, deliver to the Depositary a declaration that it is not able to accept provisional application. The obligation contained in paragraph (1) shall not apply to a signatory making such a declaration. Any such signatory may at any time withdraw that declaration by written notification to the Depositary.

(b) Neither a signatory which makes a declaration in accordance with subparagraph (a) nor Investors of that signatory may claim the benefits of provisional application under paragraph (1).

(c) Notwithstanding subparagraph (a), any signatory making a declaration referred to in subparagraph (a) shall apply Part VII provisionally pending the entry into force of the Tr[illegible] for such signatory in accordance with Article 44, to the extent that such [illegible]onal application is not inconsistent with its laws or regulations.

(3) (a) Any signatory may terminate its provisional application of this Treaty by written notification to the Depositary of its intention not to become a Contracting Party to the Treaty. Termination of provisional application for any signatory shall take effect upon the expiration of 60 days from the date on which such signatory's written notification is received by the Depositary.

[24] A. Michie, Journal of Conflict & Security Law (2005), vol. 10 No. 3, 'The Provisional Application of Arms Control Treaties', p. 346–347.

(b) In the event that a signatory terminates provisional application under subparagraph (a), the obligation of the signatory under paragraph (1) to apply Parts III and V with respect to any Investments made in its Area during such provisional application by Investors of other signatories shall nevertheless remain in effect with respect to those Investments for twenty years following the effective date of termination, except as otherwise provided in subparagraph (c).

(c) Subparagraph (b) shall not apply to any signatory listed in Annex PA. A signatory shall be removed from the list in Annex PA effective upon delivery to the Depositary of its request therefore.

(4) Pending the entry into force of this Treaty the signatories shall meet periodically in the provisional Charter Conference, the first meeting of which shall be convened by the provisional Secretariat referred to in paragraph (5) not later than 180 days after the opening date for signature of the Treaty as specified in Article 38.

(5) The functions of the Secretariat shall be carried out on an interim basis by a provisional Secretariat until the entry into force of this Treaty pursuant to Article 44 and the establishment of a Secretariat.

(6) The signatories shall, in accordance with and subject to the provisions of paragraph (1) or subparagraph (2)(c) as appropriate, contribute to the costs of the provisional Secretariat as if the signatories were Contracting parties under Article 37(3). Any modifications made to Annex B by the signatories shall terminate upon the entry into force of this Treaty.

(7) A state or Regional Economic Integration Organization which, prior to this Treaty's entry into force, accedes to the Treaty in accordance with Article 41 shall, pending the Treaty's entry into force, have the rights and assume the obligations of a signatory under this Article."

Article 45 of the ECT resulted in the provisional application of the treaty by all signatory states between December 1994 and its entry into force in April 1998, unless a member state expressly declared that it was unable to apply the ECT provisionally. After April 1998, the provisional application was restricted to those signatory states which had not yet ratified the treaty. In the Russian Federation, for example, the ratification procedure commenced with the introduction of the project in the State Duma in 1996. Parliamentary hearings began in 1998, but the Duma postponed ratification several times due to ongoing negotiations and disputes about the Transit Protocol to the Energy Charter Treaty. When signing the ECT in 1994, the Russian Federation did not register a declaration of non-application according to Article 45(2). Therefore, the Russian Federation applies the ECT on a provisional basis within the framework of Article 45.[25]

5.2 *THE RELATIONSHIP BETWEEN INTERNATIONAL LAW AND MUNICIPAL LAW*

A crucial aspect of Article 45 is its first paragraph, which provides for provisional application by a signatory state "to the extent that such provisional application is not

[25] In the three arbitrations pending against the Russian Federation referred to in footnote 1, *supra*, the Russian Federation has argued that the ECT is not provisionally applicable to it. The tribunals sitting in these cases will thus in due course address this issue.

inconsistent with its constitution, laws or regulations." This provision seems to give national law priority over the treaty as long as it is applied provisionally. The language could be interpreted in two ways, *viz.* (i) provisional application itself must not be inconsistent with municipal law and/or (ii) the substantive provisions of the treaty must not be inconsistent with substantive provisions of municipal law.

With respect to the Russian Federation, this article will briefly address the first issue.

The constitution of the Russian Federation assigns the right to negotiate and conclude international treaties to the President (Article 86(b)), but leaves their ratification to the Federal Assembly (State Duma and Council of the Federation – Articles 71, 105, and 106(d)). The concept of "provisional application" is not dealt with in the relevant provision of Article 15 of the Constitution.

> "(4) Generally accepted principles and rules of international law and international treaties of the Russian Federation shall be an integral part of its legal system. If an international treaty of the Russian Federation establishes rules, other than provided for by the law, the rules of the international treaty shall be applied."

The details concerning international treaties are regulated by the 1995 Federal Law on International Treaties of the Russian Federation. Article 23 of the 1995 Federal Law expressly deals with the provisional application of international treaties in the Russian Federation:

> 1. An international treaty or part of a treaty may, before its entry into force, be applied by the Russian Federation provisionally if such has been provided for in the treaty or if an arrangement was reached concerning this with the parties who have signed the treaty.
>
> 2. Decisions concerning the provisional application by the Russian Federation of an international treaty or part thereof shall be adopted by the agency which adopted the decision to sign the international treaty in the procedure established by Article 11 of the present Federal Law.
>
> If an international treaty, the decision concerning consent to the bindingness of which for the Russian Federation is subject in accordance with the present Federal Law to adoption in the form of a Federal Law, provides for the temporary application of the treaty or part thereof or an arrangement concerning this has been reached with the parties in any other way, it shall be submitted to the State Duma within a period of not more than six months from the date of the commencement of the provisional application thereof. By a decision in the form of a Federal Law in the procedure established by Article 17 of the present Federal Law for the ratification of international treaties, the period of provisional application may be extended.
>
> 3. Unless provided otherwise in an international treaty or the respective States agree otherwise, the provisional application by the Russian Federation of a treaty or part thereof shall terminate upon informing the other States which provisionally are applying the treaty of the intention of the Russian Federation not to become a participant of the treaty. "

It follows from the foregoing that Russian law acknowledges and accepts provisional application of treaties *per se.* In this respect, Russian law is thus consistent with Article 45(1) of the ECT.

5.3 *Termination and Opting out of Provisional Application of the ECT*

According to Article 45(2) of the ECT, any signatory state may, when signing the ECT, declare that it is not able to accept provisional application. In such a case, neither a signatory that makes the declaration, nor investors of that signatory state, may claim the benefits of provisional application. Australia, Iceland and Norway made such declarations when they signed the ECT, and as per 20 April 2006 the ECT is not yet in force for those countries. The Russian Federation has not delivered a declaration pursuant to Article 45(2) of the ECT.

Any signatory may also terminate its provisional application of the ECT by written notification to the depository of the ECT of its intention not to become a contracting party to the ECT according to Article 45(3) of the ECT.[26]

There is thus an express opting-out provision in Article 45(2) of the ECT. It is still arguably unclear, however, as to whether an ECT signatory is *obliged to declare* that it is not able to accept provisional application in the event that its legislation is in conflict with the substantive provisions of the ECT. Moreover, it is unclear as to whether an ECT signatory, without making any such declaration, is entitled to rely on the condition contained in the provisional application provision of Article 45(1), i.e., that provisional application not be inconsistent with its constitution, laws or regulations.

Assuming that an ECT signatory would be entitled not to make an "opting-out declaration", it could prove extremely difficult to pass judgement on the extent to which the provisions of the ECT are inconsistent with a particular signatory's constitution, laws or regulations.

5.4 *Provisional application without limitation?*

Although provisional application of a treaty, as the term indicates, is intended to be temporary pending the entry into force of the treaty, it may well be that – in relation to a specific signatory state – such provisional application continues past the general entry into force of the treaty, where such signatory state, for whatever reason, has not ratified the treaty. The Russian Federation – being a signatory to the ECT that has not yet ratified the treaty – continues to apply the ECT provisionally within the framework of Article 45(1), even though the ECT entered into force in April 1998.

One question which arises in this situation is whether the period of provisional application of a treaty may be indefinite or whether it is limited in time.

Article 25(2) of the Vienna Convention – regulating the provisional application of treaties – provides that:

> Article 25 Provisional application
> 2. Unless the treaty otherwise provides or the negotiating States have otherwise agreed, the provisional application of a treaty or a part of a treaty with respect to a State shall be

[26] A similar situation arose in the Petrobart case, *see* Section 6.2.2, *infra*.

terminated if that State notifies the other States between which the treaty is being applied provisionally of its intention not to become a party to the treaty.

This provision is reproduced almost verbatim in Article 23(3) of the 1995 Federal Law on International Treaties of the Russian Federation.

Thus, neither Article 25 of the Vienna Convention nor Article 23 of the Russian law stipulate any express limitation in time for the period of provisional application. Instead, both provisions envisage that provisional application will come to an end either through the entry into force of the treaty, or by express termination through a notification by a signatory to the other States between which the treaty is being applied provisionally of its intention not to become a party to the treaty.

Based on the wording of the two provisions, it would seem that - if a treaty provides for provisional application - the period of provisional application will be limited only if so expressly stated in the treaty. This was the case, for instance, with the OSCE Open Skies Treaty 1992, which provided that certain of its provisions were to be provisionally applied and that this provisional application was to be effective for a period of 12 months from the date on which the treaty was opened for signature.[27]

If provisional application is not limited in time, such application may be terminated by a party to the treaty. Both Article 25(2) of the Vienna Convention and Article 23(2) of the Russian law make it clear that such termination must be explicit and that each other party applying the treaty provisionally must be notified of such termination. If this is not done, the treaty will continue to apply provisionally.

Article 45 of the ECT does not provide any express limitation in time for the provisional application of the Treaty. According to Article 45, provisional application of the ECT will come to an end either through the entry into force of the ECT for such signatory, or through the express termination of the provisional application. Such termination shall be in the form of a written notification to the Depository.

Furthermore, Article 45(3)(b) of the ECT provides that, even if provisional application is terminated, the obligation of the signatory to apply Parts III and V with respect to investments made during such provisional application shall nevertheless remain in effect with respect to those investments for twenty years following the effective date of termination.

Consequently, unless terminated in accordance with Article 45(3)(a) by the signatory, provisional application of the ECT continues without any limitation in time.

Russian law thus acknowledges and accepts the provisional application of treaties *per se*. Article 45(1) of the ECT is thus consistent with Russian law in this respect. It would also seem that provisional application of the ECT continues without any limitation in time.

[27] See Anthony Aust, Modern Treaty Law and Practice, Cambridge University Press (Cambridge 2000), p. 139–141.

5.5 *Provisional Application and Arbitration*

As regards the ECT, an important question is whether private parties may rely on the right to arbitration under Article 26 during the provisional application regime. Provisional application is a well-established method for giving immediate effect to treaties. The issue of provisional application in favour of private parties obtaining arbitration rights against states has not, however, been previously addressed. One view is that private parties should be able to do so, in particular since the underlying rationale of the ECT is to gain maximum effectiveness and given its binding character; in addition international arbitration plays a very important role in the investment protection scheme provided by the ECT. Moreover, no exception has been carved out for arbitration despite the numerous, often very carefully crafted, exceptions and opt-outs in the ECT. Accordingly, the better view is perhaps that Article 26 of the ECT is to be applied provisionally under the regime of Article 45 in the same manner as any other provision of the ECT.

6. Awards Rendered

As previously mentioned, the ECT's investment protection regime has been in force since 1998, but the number of awards rendered so far is rather limited. Eleven out of the fifteen cases that so far have been brought to international arbitration under Article 26 are still pending, and to date only one award on jurisdiction (*Plama Consortium Limited v. Republic of Bulgaria*) and two final awards (*Nykomb Synergetics Technology Holding AB v. the Republic of Latvia* and *Petrobart Limited v. the Kyrgyz Republic*) have been issued under the ECT. Both *Nykomb* and *Petrobart* were arbitrations under the Rules of the Stockholm Chamber of Commerce, whereas *Plama* is an ICSID arbitration.

Due to the limited number of awards, it is not yet possible to identify any clear trends in ECT cases. However, in particular the awards in *Petrobart* and *Plama* raise some jurisdictional issues of general interest, which will be discussed in section 6.2 below. As to the merits, the awards in *Nykomb* and *Petrobart* involve questions concerning the standard of compensation in the case of violations of the ECT other than expropriation. Like many BITs, the ECT does not contain any provisions on the standard of compensation to be applied in such cases. This issue will be discussed in section 6.3 below.

6.1 *Brief Introduction to the Cases*

6.1.1 Nykomb Synergetics Technology Holding AB v. the Republic of Latvia[28]

Nykomb v. the Republic of Latvia concerned a dispute regarding the purchase of power by the state-owned Latvian company, Latvenergo, and the Latvian company Windau, a wholly owned subsidiary of the Swedish company, Nykomb. In 1997

[28] The full text of the award is available in K. Hobér, Investmenat Arbitration in Eastern Europe: In search of a Definition of Expropriation (Juris Net, LLC, Huntington 2007), Appendix 11. For an analysis of the case see Hobér, Investment Arbitration in Eastern Europe, p. 202; and T. Wälde and K. Hobér, The First Energy Charter Award, Journal of International Arbitration, Vol. 22, No. 2 (2005), pp. 83–103. The author of this article represented Nykomb in the arbitration.

Latvenergo and Windau entered into several agreements for the construction of power plants in Latvia. Pursuant to the agreements Latvenergo undertook to purchase surplus electric power, i.e. electricity not used for its own consumption, at a tariff which was twice the average electric power sale tariff approved by the Public Utilities Commission of the Republic of Latvia (the "Double Tariff).

The first plant was ready for operation on 17 September 1999, but Latvenergo refused to purchase the surplus electric power from the plant at the Double Tariff. Due to Latvenergo's refusal Windau was not able to start its production until 28 February 2000. After that time Latvenergo purchased surplus electric power from Windau at 75 percent of the average tariff, i.e. at a tariff which is lower than the average tariff.

In the arbitration Nykomb argued that Windau was entitled to the Double Tariff, since one of the contracts stipulated that the purchase price for surplus energy was to be determined in accordance with the Latvian Law on Entrepreneurial Activities in the Energy Sector. At the time when Windau signed the agreements, this law provided that power plants with a certain capacity were entitled to the Double Tariff. Latvia, on the other hand, argued that Windau only was entitled to 75 percent of the average tariff in accordance with the new Energy Law, which had entered into force after Windau and Latvenergo concluded their agreements.

Nykomb claimed that Latvenergo's refusal to pay the Double Tariff with reference to the new Energy Law, which deprived Windau of its right to the Double Tariff referred to in the agreement, constituted a regulatory taking having effect equivalent to expropriation (Article 13(1)). Nykomb also claimed that such refusal by Latvenergo to pay the double tariff constituted discriminatory measures, since Latvenergo were paying two other companies (SIA "Latelektro-Gulbene" and Joint Stock Company "Liepājas Siltums") the Double Tariff for its surplus electric power.

The tribunal found that there was no taking of Windau or its assets, no interference with the shareholder's rights or with the management's control over and running of the enterprise. It therefore concluded that the refusal to pay the Double Tariff did not qualify as expropriation, or the equivalent thereof, under the ECT.[29] However, as to Nykomb's discrimination claim, the tribunal found that Latvia had breached its obligation under Article 10(1) of the ECT not to discriminate by offering double tariffs to other companies and failing to present any evidence as to why those companies should be treated differently.[30]

6.1.2 PETROBART LIMITED V. THE KYRGYZ REPUBLIC[31]

The arbitration between Petrobart Ltd of Gibraltar and the Kyrgyz Republic concerned a sales contract between Petrobart and the Kyrgyz state owned company KGM for the purchase by the latter of 200,000 tonnes of gas condensate.

[29] Nykomb v. Synergetics Technology Holding AB v. the Republic of Latvia, section 4.3.1.
[30] Nykomb v. Synergetics Technology Holding AB v. the Republic of Latvia, section 4.3.2.(a).
[31] The full text of the award is available in K. Hobér, *op. cit.*, Appendix 12.

Petrobart delivered five shipments of gas but was only paid for the first two. At the same time as Petrobart turned to domestic courts for recourse, Kyrgyz authorities – as part of a reform of the system for supply of oil and gas in the Kyrgyz Republic – took certain measures that made it impossible for Petrobart to enforce its rights under the contract. The measures included a decision by the Kyrgyz authorities to privatize KGM, and to transfer its assets, but not its liabilities (including monies owed to Petrobart), to a new company as well as a request by the Vice Prime Minister of the Kyrgyz Republic who – referring to KGM's critical financial standing – asked the chairman of a Kyrgyz court that previously had rendered a judgment in favour of Petrobart, to assist in granting a stay of the enforcement of the judgment against KGM. Enforcement was stayed by the court referring to the letter of the Vice Prime Minister, and before the period of stay of execution ended, KGM was declared bankrupt, which meant that enforcement of the judgment was no longer possible.

With reference to the above, the tribunal found that the Kyrgyz Government was liable for certain breaches of the ECT, specifically by virtue of its failure to provide fair and equitable treatment by transferring assets from KGM to the above mentioned new company to the detriment of KGM's creditors, including Petrobart (Article 10(1)); and by intervening in court proceedings regarding the stay of execution of a final judgment to the detriment of Petrobart (Article 10(12)).[32]

The award was challenged by the Kyrgyz Republic before the Svea Court of Appeal in Stockholm. The Court of Appeal, however, in a decision dated 19 January 2007 upheld the award.[33]

6.1.3 PLAMA CONSORTIUM LIMITED V. REPUBLIC OF BULGARIA (ICSID CASE NO. ARB/03/24) – DECISION ON JURISDICTION[34]

Plama Consortium Limited ("Plama") is a Cypriot company, which purchased an equity interest in a Bulgarian company. Nova Plama, owning 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 Energy Charter Treaty and the Cyprus-Bulgaria BIT.

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 BIT. The BIT claims will not be dealt with any further in this paper.[35]

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[32] Petrobart Limited v. the Kyrgyz Republic, p. 76.

[33] Judgment of Svea Court of Appeal, 19 January 2007, *The Republic of Kirgizistan v. Petrobart Ltd*, Case no. T 5208-05.

[34] The full text of the award is available *e.g.* at http://www.investmentclaims.com/decisions/Plama-Bulgaria-Jurisdiction-8Feb2005.pdf.

[35] The Cyprus-Bulgaria BIT only provided for jurisdiction with regard to claims of expropriation. Since Plama's claim concerned other alleged breaches of the Cyprus-Bulgaria BIT, Plama tried to rely on the MFN-clause in the Cyprus-Bulgaria BIT to be able to invoke the dispute resolution clauses in other Bulgarian BITs, which gave investors the option to pursue dispute resolution for all breaches of the treaty. However, the tribunal found that the MFN treatment obligation contained in the Cyprus-Bulgaria BIT did not extend to Plama the protection of dispute

(footnote continued on next page)

6.2 *Jurisdictional Issues*

6.2.1 Nykomb

Nykomb did not raise very many jurisdictional issues, but certain findings of the tribunal may nevertheless be briefly noted.

Investment

In the arbitration, Latvia argued that the contract between Latvenergo and Windau for the purchase of electric power, upon which Nykomb's claims were based, was a commercial contract and as such not protected by the ECT. Latvia contended that the ECT only applies to investment contracts within the meaning of the ECT, and that Nykomb's claims, which were based on a commercial contract, were outside the scope of the ECT.

The tribunal found that the purchase contract could not be regarded as purely commercial. Moreover, according to the tribunal, neither could the action to refuse payment of the double tariff under the contract be considered as purely commercial. As for the objection that the purchase contract was not an investment contract within the meaning of the ECT, the tribunal found that it suffices to note that a contract for provision of energy for eight years "*clearly falls within the Treaty's definition of an investment in Article 1 of the Treaty*".[36]

Retroactive Application

Latvia also argued that Nykomb was seeking to apply the treaty retroactively since the contract between Windau and Latvenergo had been concluded before the entry into force of the ECT. The tribunal, however, rejected the argument that retroactive application had been asserted finding that the alleged breaches had occurred after the entry into force of the ECT.[37]

6.2.2 Petrobart

Investment

One of the jurisdictional issues in *Petrobart* was whether Petrobart had made an "investment" in the Kyrgyz Republic for the purposes of the ECT. In an earlier

resolution provisions set out in other Bulgarian investment treaties. The tribunal emphasised that it is a well-established principle, both in domestic and international law that the parties to an arbitration must clearly express their agreement to arbitrate, and that *"doubts as to the parties' clear and unambiguous intention can arise if the agreement to arbitrate is to be reached by incorporation by reference"* such as through an MFN clause (see Plama Consortium Limited v. Republic of Bulgaria, p. 63, para. 199).

[36] Nykomb v. Synergetics Technology Holding AB v. the Republic of Latvia, section 4.3.3.(d).

[37] Nykomb v. Synergetics Technology Holding AB v. the Republic of Latvia, section 4.3.3.(a).

UNCITRAL arbitration between the same parties, a different tribunal had ruled that Petrobart's sales contract with KGM did not qualify as a foreign "investment" under the Foreign Investment Law of the Kyrgyz Republic.

The tribunal in the ECT arbitration stressed that the term "investment" must be interpreted in the context of each particular treaty in which the term is used,[38] and that the question therefore was whether Petrobart's right under the contract to payment for goods delivered under the contract constituted an investment within the definition provided by the ECT.[39] Article 1(6)(c) of the ECT provides that assets constituting an investment shall include "*claims to money and claims to performance pursuant to contract having an economic value and associated with an Investment*". The tribunal found that the wording of Article 1(6)(c) presented certain ambiguities and pointed to the logical problem that the term "Investment" is not only the term to be defined, but is also used as part of the definition. The tribunal concluded that "*this means that the definition is in reality a circular one which raises a logical problem and creates some doubt about the correct interpretation.*"[40]

Instead the tribunal based its jurisdiction on Article 1(6)(f), which provides that an asset constituting an investment shall also include "*any right conferred by law or contract or by virtue of any licences and permits granted pursuant to law to undertake any Economic Activity in the Energy Sector*". "Economic Activity in the Energy Sector" is in Article 1(5) defined as "*economic activity concerning the exploration, extraction, refining, production, storage, land transport, transmission, distribution, trade, marketing, or sale of Energy Materials and Products except those included in Annex NI, or concerning the distribution of heat to multiple premises.*" It was not disputed in the arbitration that the gas condensate, which Petrobart sold according to the sales agreement, constituted "Energy Materials and Products" within the meaning of the ECT. With reference to the above, the tribunal found that "*a right conferred by contract, to undertake an economic activity concerning the sale of gas condensate is an investment according to the Treaty [ECT]. This must also include the right to be paid for such a sale.*"[41]

The decision of the tribunal to the effect that Petrobart's claim for payment under the sales agreement constituted an investment within the meaning of the ECT was not challenged by the Kyrgyz Republic in the above-mentioned application for the setting aside of the award before the Svea Court of Appeal.

Applicability of the ECT with regard to Gibraltar

Another jurisdictional issue was whether the ECT was applicable with respect to investors of Gibraltar. When the United Kingdom signed the ECT, it made a declaration

[38] Petrobart Limited v. the Kyrgyz Republic, p. 69.
[39] Petrobart Limited v. the Kyrgyz Republic, p. 71.
[40] Petrobart Limited v. the Kyrgyz Republic, p. 72.
[41] Petrobart Limited v. the Kyrgyz Republic, p. 72.

under Article 45(1) that the provisional application of the treaty should extend to the United Kingdom of Great Britain and Northern Ireland and to Gibraltar. However, when the United Kingdom ratified the ECT, it was specified in the instrument of ratification, that the ratification was in respect of the United Kingdom of Great Britain and Northern Ireland, the Bailiwick of Jersey and the Isle of Man. Gibraltar was not mentioned in the instrument of ratification.[42] The tribunal therefore had to determine whether the ECT applied to Gibraltar despite the non-inclusion of Gibraltar in the instrument of ratification. The tribunal found that such problem of interpretation had to be resolved through a "*rather formal approach based on the wording of the Treaty*", and noted that "*according to the text of the Treaty provisional application ceases if it is terminated either by a special notification under Article 45(3)(a) of the Treaty or by transition from provisional application to a corresponding and final legal commitment resulting from the entry into force of the Treaty. It could indeed be expected that the United Kingdom, if it wished the provisional application of the Treaty to Gibraltar to be terminated as a result of a ratification not including Gibraltar, should have made this clear by making a notification in line with Article 45(3)(a) or a declaration in some other form in connection with the ratification. In the Arbitral Tribunal's opinion, the fact that the ratification, for political or other reasons, did not include Gibraltar does not justify the conclusion that the United Kingdom intended to revoke the application of the Treaty to Gibraltar on a provisional basis.*"[43]

In other words, the tribunal found that the instrument of ratification, which – with respect to the United Kingdom of Great Britain and Northern Ireland (not including Gibraltar) – transformed the provisional application of the ECT into a final legal commitment, should not be interpreted as a termination of the provisional application in relation to Gibraltar.

This issue was part of the Kyrgyz Republic's above-mentioned challenge of the award before the Svea Court of Appeal. In the challenge proceedings, the Kyrgyz Republic argued that the tribunal exceeded its mandate by finding that the ECT applied provisionally to Gibraltar. The Court of Appeal, however, held that the Tribunal had not exceeded its mandate. The Court found that since there is no provision in the ECT which governs the situation where the ECT has been ratified with regard to a territory not corresponding to the territory covered by the provisional application, it could have been expected that the United Kingdom would have made it clear that the ECT no longer applied to Gibraltar, had this been the intention. With reference thereto, the Court found that the Tribunal had been correct in finding that Gibraltar was still covered by the provisional application of the ECT.

Article 17 of the ECT

The Kyrgyz Republic also argued that Petrobart, according to Article 17(1) ECT,

[42] Petrobart Limited v. the Kyrgyz Republic, p. 62.
[43] Petrobart Limited v. the Kyrgyz Republic, p. 62–63.

should be denied the protection of the investment protection provisions of Part III of the ECT, since Petrobart was owned or controlled by nationals of a non-contracting party to the ECT, and since Petrobart had no substantial business activities in Gibraltar. The tribunal, however, relied upon information provided by Petrobart showing that it was managed by an English company and that this company handled many of Petrobart's strategic and administrative matters. The tribunal found that this information rebutted the allegations that Petrobart was owned or controlled by nationals of a state other than the UK and that Petrobart did not have substantial business in the UK.[44]

The tribunal did not specifically address the question of whether non-application in certain circumstances of Part III as provided for in Article 17 goes to the jurisdiction of the tribunal or constitutes a defence on the merits of the case. However, the reference by the tribunal to Article 10(2) of the Rules of the Arbitration Institute of the Stockholm Chamber of Commerce, regarding the time when jurisdictional objections should be made, indicates that the tribunal viewed Article 17 as a jurisdictional defence. The distinction is of importance, since matters of jurisdiction may be open for review by local courts at the place of arbitration (or an ICSID *ad hoc* committee) on the grounds that the tribunal has exceeded its jurisdiction.

Curiously, the Kyrgyz Republic did not argue before the Swedish Court of Appeal in the above-mentioned challenge of the award, that a misapplication of Article 17 would constitute an excess of mandate by the Tribunal. The question whether the non-application in certain circumstances of Part III as provided for in Article 17 goes to the jurisdiction of the tribunal or constitutes a defence on the merits of the case was therefore not determined by the Court of Appeal. Rather, the Kyrgyz Republic initially argued that the tribunal exceeded its mandate by not scrutinizing the ownership and status of Petrobart in greater detail. This claim, however, appears subsequently to have been withdrawn.

Res Judicata

The case also involved matters of *res judicata* and *estoppel* in relation to a previous UNCITRAL arbitration under the Foreign Investment Law of the Kyrgyz Republic previously initiated by Petrobart against the Kyrgyz Republic regarding the same investment. In the UNCITRAL arbitration, a different tribunal had ruled that Petrobart's sales contract with KGM did not qualify as a foreign "investment" under the Foreign Investment Law of the Kyrgyz Republic. With reference hereto. The Kyrgyz Republic argued in the present proceedings under the ECT that the decision of the tribunal in the UNCITRAL arbitration should operate to bar such proceedings on grounds of *res judicata*. The tribunal, however, rejected the *res judicata* defence on the grounds that (i) the two arbitrations were based on different arbitration clauses, *viz.*, the first clause in the Foreign Investment Law and the second in the ECT, and (ii) the first arbitration dealt

[44] Petrobart Limited v. the Kyrgyz Republic, p. 63.
[45] Petrobart Limited v. the Kyrgyz Republic, p. 64–66.

with investments under Kyrgyz law and the second with alleged violations of the ECT.[45] For similar reasons, the initiation of the first proceedings without simultaneously initiating the ECT proceedings did not prevent Petrobart – on grounds of *estoppel* – from later initiating ECT proceedings based on the same factual allegations.[46]

6.2.3 PLAMA

Burden of proof

In Plama, the tribunal discussed the burden of proof with regard to jurisdictional requirements, and adopted the test previously advocated by Judge Higgins in her separate opinion in the *Oil Platforms Case*.[47] In such case Judge Higgins held that:

> the only way in which, in the present case, it can be determined whether the claims of [Claimant] are sufficiently plausibly based upon the 1955 Treaty is to accept pro tem the facts as alleged by [Claimant] to be true and in that light to interpret Articles I, IV and X for jurisdictional purposes, that is to say, to see if on the basis of Iran's claims of fact there could occur a violation of one or more of them.[48]

She also held that:

> the Court should... see if, on the facts as alleged by [Claimant], the [Respondent's] actions complained of might violate the Treaty articles (§ 33) ... Nothing in this approach puts at risk the obligation of the Court to keep separate the jurisdictional and merits phases... and to protect the integrity of the proceedings on the merits... what is for the merits, (and which remains pristine and untouched by this approach to the jurisdictional issue) is to determine what exactly the facts are, whether as finally determined they do sustain a violation of ...[the treaty] and if so, whether there-is a defence to that violation... In short it is at the merits that one sees 'whether there really has been a breach'.[49]

The tribunal concluded that it did not understand Judge Higgins' approach to be controversial and stated that it would apply such approach to the jurisdictional issues in dispute in the present arbitration.[50]

Investment

In its objection to jurisdiction, Bulgaria argued that Plama had not made an "Investment", as defined in the ECT. Bulgaria claimed that Plama had misrepresented or wilfully failed to disclose its true ownership to the Bulgarian authorities in violation of Bulgarian law. Accordingly, the consent of Bulgaria's Privatization Agency to

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[46] Petrobart Limited v. the Kyrgyz Republic, p. 66–68.
[47] Islamic Republic of Iran v. United States of America, 1996, ICJ Reports.
[48] Islamic Republic of Iran v. United States of America, para. 32.
[49] Islamic Republic of Iran v. United States of America, para. 34.
[50] Plama Consortium Limited v. Republic of Bulgaria, p. 36, para. 119.
[51] Plama Consortium Limited v. Republic of Bulgaria, p. 38, para. 126.

Plama's purchase of shares in the local company was null and void under Bulgarian law. Therefore, Plama had failed to make a valid investment.[51]

The tribunal found that as for the application of the definitions of "Investor" and "Investment" in the ECT, it is irrelevant who owns or controls the claimant, and that "*applying Judge Higgins' approach to disputed facts, the Tribunal must accept, pro tem, the investment as alleged by the Claimant; and on this ground alone, the Tribunal decides that Bulgaria's submission fails*".[52] The tribunal also found that as Bulgaria's commitment to arbitrate was based on the ECT and not on the agreement to purchase the shares, the agreement to arbitrate remained effective even if the parties' agreement regarding the purchase of Nova Plama was arguably invalid because of misrepresentation by the Claimant.[53]

Article 17 of the ECT

Bulgaria also argued that its consent to submit disputes to arbitration under Article 26(1) of the ECT was expressly limited to disputes concerning an alleged breach of an obligation arising under Part III of the ECT. Part III contains Article 17, which reserves to a contracting party, the right to deny advantages of that Party to "*a legal entity if citizens or nationals of a third state own or control such entity and if that entity has no substantial business activities in the Area of the Contracting Party in which it is organized*". Bulgaria claimed that by denying to the claimant, in accordance with Article 17(1), the protections afforded by Part III, Bulgaria's consent to submit disputes concerning alleged breaches of obligations under Part III, did not provide a basis for jurisdiction in the case.[54]

In its assessment of the parties' arguments, the tribunal agreed with Bulgaria that the jurisdiction of the tribunal under Article 26 ECT is limited to the host state's obligations under Part III of the ECT. However, the tribunal found, with reference to the wording of Article 17(1), that "*each Contracting Party reserves the right to deny the advantages of this Part [Part III]*" and that when interpreted in good faith in accordance with its ordinary contextual meaning such denial applies only to advantages under Part III. The tribunal concluded that "*it would therefore require a gross manipulation of the language to make it refer to Article 26 in Part V of the ECT.*"[55]

The tribunal noted that a contracting state can only deny the advantages of Part III if the specific criteria of Article 17(1) are satisfied. The tribunal further noted that the question of whether such criteria are met could raise wide-ranging, complex and highly controversial disputes, as in the present case, and that in the absence of Article 26 as a remedy available to the parties, the tribunal questioned how such disputes could ever be

[52] Plama Consortium Limited v. Republic of Bulgaria, p. 38-39, para. 128.
[53] Plama Consortium Limited v. Republic of Bulgaria, p. 39, para. 130.
[54] Plama Consortium Limited v. Republic of Bulgaria, p. 14, para. 32.
[55] Plama Consortium Limited v. Republic of Bulgaria, p.45–46, para. 147.
[56] Plama Consortium Limited v. Republic of Bulgaria, p. 46, para. 149.

decided.[56] The tribunal concluded that it would be a "*license for injustice*" and that "*the Contracting State invoking the application of Article 17(1) is the judge in its own cause*", if arbitration under Article 26 would not be available to the investor for the purpose of determining whether the conditions of Article 17(1) have been met.[57]

The tribunal also addressed certain other issues concerning Article 17. The tribunal considered whether Article 17 in itself provided sufficient notice to the investor that it could not enjoy the protection of the ECT (assuming the criteria for its application are satisfied) or whether further notice was required. Given the wording of Article 17(1) ("*reserves the right to deny*"), the tribunal took the view that interpretation of Article 17(1) of the ECT in accordance with Article 31(1) of the Vienna Convention[58] required that the right of denial be actively exercised by the contracting state.[59]

Since Bulgaria had not issued such notice until after Plama made its request for arbitration and not until four years after Plama made its investment, the tribunal also had to determine whether such notice applied retrospectively or only prospectively. Once again invoking Article 31(1) of the Vienna Convention, stressing in particular the objects and purpose of the ECT, the tribunal concluded that the exercise by a contracting party of its right under Article 17(1) should not have retrospective effect since this would not be consistent with the purpose of the ECT "*to promote the long term co-operation in the energy field*". The tribunal pointed out that such unexercised right could lure putative investors with legitimate expectations only to have those expectations at a much later date retrospectively denied and that the investor could not plan in the long-term for such an effect.[60]

6.2.4 CONCLUDING REMARKS ON JURISDICTION

Article 17 of the ECT

As mentioned above, there are still too few arbitral awards under the ECT to draw any general conclusions regarding jurisdictional issues arising under the ECT. It is interesting to note, however, that both *Petrobart* and *Plama*, involved the application of Article 17, be it as a jurisdictional defence, or as a defence on the merits.

In the *Plama* award, the Tribunal had to determine two issues regarding the application and interpretation of Article 17. The *first* was whether Article 17 goes to the jurisdiction of the tribunal or whether it goes to the merits. The tribunal in *Plama* dismissed Bulgaria's argument that the applicability of Article 17 would affect the

[57] Plama Consortium Limited v. Republic of Bulgaria, p. 47, para. 149.

[58] Article 31(1) of the Vienna Convention reads: "*a treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose*".

[59] Plama Consortium Limited v. Republic of Bulgaria, p. 49–50, para. 155–158.

[60] Plama Consortium Limited v. Republic of Bulgaria, p. 50–53, para, 159–165.

jurisdiction of the tribunal, whereas the Tribunal in *Petrobart* did not make any express decision on whether Article 17 was a jurisdictional or merits issue.

The *second* issue in relation to Article 17 that arose in *Plama* was whether the provision in itself means that treaty protection is excluded as soon as the conditions in 17(1) are fulfilled, or whether an additional express notice by the state to the investor prior to the occurrence of the allegedly wrongful acts is required. The tribunal in *Plama* considered such an additional notice to be necessary, whereas the Tribunal in *Petrobart* did not expressly determine this issue.

Thus, the cases discussed in this contribution show that there is, for the time being, no general approach to the application of Article 17. Only time will tell whether such a general approach will ever emerge.

Provisional Application

In *Petrobart*, the provisional application of the ECT in relation to Gibraltar was determined. Further issues regarding the provisional application are likely to arise in the future, since both Belarus and the Russian Federation are signatories who apply the ECT provisionally in the sense that they have signed the ECT without submitting a declaration that it is not able to accept provisional application in accordance with Article 45(2).

Investment

As is frequently the case in BIT arbitrations, the tribunals in all three arbitrations discussed above had to determine objections by the State-party to the effect that the investor had not made an "Investment" protected by the ECT. As evidenced by the award in *Plama*, the determination of such issues may involve questions of what issues properly belong to the Tribunal's decision on jurisdiction and what issues should be left for the determination of the merits.

6.3 *COMPENSATION STANDARDS*

The ECT (like most BITs as well as NAFTA), does not contain any provision or language, addressing the issue of compensation in case of violation of investment protection provisions (fair and equitable treatment, non-discrimination etc) other than expropriation. In this context, it may be of interest that the awards in both *Nykomb* and *Petrobart* dealt with the issue of compensation for violations of Article 10 of the ECT.

6.3.1 NYKOMB

As mentioned in Section 3.1.1 above, the tribunal in *Nykomb* found that Latvia had breached its obligation under Article 10 of the ECT not to *discriminate* against foreign

investors by offering the so-called "double tariff" to certain other companies but not to Nykomb's Latvian subsidiary, Windau, and by failing to present any evidence as to why those companies should be treated differently.

As to the standard of compensation applicable in the event of such discrimination, the tribunal noted that the principles of compensation set forth with respect to expropriation in Article 13(1) of the ECT were not applicable to the assessment of damages or losses caused by violations of Article 10. The tribunal found that "*the question of remedies to compensate for losses or damages caused by the Respondent's violation of its obligations under Article 10 of the Treaty must primarily find its solution in accordance with established principles of customary international law. Such principles have authoritatively been restated in The International Law Commission's Draft Articles on State Responsibility adopted in November 2001*".[61]

The tribunal further noted that according to Articles 34 and 35 of the ILC Draft Articles, restitution was the primary remedy. However, with respect to the case before it, the tribunal found that restitution was a suitable remedy primarily where the state had instituted actions directly against the investor. Where the actions were directed against an investor's subsidiary, the tribunal found instead that the appropriate remedy should be compensation for the losses or damage inflicted on the investor's investment.[62]

Nykomb claimed damages corresponding to the difference between the "double tariff" and the tariff that had actually been paid to Windau. However, the tribunal decided not to give Nykomb the full difference between the two sets of tariffs because the higher payments would not have gone directly to Nykomb. The tribunal stated that "*the money would have been subject to Latvian taxes etc., would have been used to cover Windau's costs and down payments on Windau's loans etc., and disbursements to the shareholder would be subject to restrictions in Latvian company law on payment of dividends*".[63]

Taking into account the requirements of causation, foreseeability and the reasonableness of the result as applicable under customary international law, the tribunal nevertheless found that the reduced earnings of Windau constituted the best available basis for the assessment also of Nykomb's losses. The tribunal came to the conclusion that a discretionary award of one third of the estimated loss in purchase prices of electricity up to the time of the award would serve as a reasonable basis for quantifying Nykomb's assumed losses up to the time of the award.[64]

As regards Nykomb's alleged losses on delivery of electric power to Latvenergo for

[61] Nykomb v. Synergetics Technology Holding AB v. the Republic of Latvia, Stockholm International Arbitration Review, 2005:1, p. 104–105.

[62] Nykomb v. Synergetics Technology Holding AB v. the Republic of Latvia, Stockholm International Arbitration Review, 2005:1, p. 105–108.

[63] Nykomb v. Synergetics Technology Holding AB v. the Republic of Latvia, Stockholm International Arbitration Review, 2005:1, p. 105.

[64] Nykomb v. Synergetics Technology Holding AB v. the Republic of Latvia, Stockholm International Arbitration Review, 2005:1, p. 107.

the remainder of the eight year contractual period, the tribunal considered this potential loss too uncertain and speculative to form the basis for an award of monetary compensation. The tribunal, however, considered it to be a continuing obligation of Latvia to ensure payment of the double tariff for electrical power delivered under the contract for the rest of the eight year contractual period. The tribunal, therefore, ordered Latvia to fulfil its obligation to pay the double tariff for future deliveries during the remainder of the contractual period.[65]

6.3.2 PETROBART

In *Petrobart*, the tribunal found that the Kyrgyz Republic had violated its obligations under Articles 10.1 and 10.12 of the ECT (see section 4.2.1 above). With reference to the *Chorzów Factory Case* and to ILC's Draft Articles on State Responsibility, the tribunal found that Petrobart had suffered damage as a result of the Kyrgyz Republic's breaches of the ECT and that Petrobart had, as far as possible, to be placed in the financial position in which it would have found itself, had the breaches not occurred.[66]

Petrobart essentially claimed compensation for (i) the unpaid invoices for gas condensate actually delivered by Petrobart to KGM; and (ii) loss of profit with regard to the remaining deliveries under the contract.

The tribunal found that due to the troublesome financial situation of KGM, KGM would probably not have survived irrespective of the breaches of the ECT committed by the Kyrgyz Republic.[67]

The tribunal nevertheless found that the transfer by the Kyrgyz Republic of substantial assets belonging to KGM to other state entities caused substantial damage to KGM's creditors, including Petrobart. Due to the inadequacy of the information submitted by the parties, the tribunal found that the damage suffered by Petrobart could not be established with precision. The tribunal therefore found it necessary to make a general assessment based on its appreciation of the situation as a whole. In making such assessment, the tribunal found that the Kyrgyz Republic "*as responsible for the transfer and lease of KGM's assets, shall compensate Petrobart for damage which the Arbitral Tribunal estimates at 75% of its justified claims against KGM*".[68]

With regard to Petrobart's claim for lost profit, the tribunal found that there remained a great deal of uncertainty as to the consequences of the breakdown of the business relations between Petrobart and KGM. The tribunal therefore concluded that

[65] Nykomb v. Synergetics Technology Holding AB v. the Republic of Latvia, Stockholm International Arbitration Review, 2005:1, p. 108.
[66] Petrobart Limited v. the Kyrgyz Republic, p. 77–78.
[67] Petrobart Limited v. the Kyrgyz Republic, p. 81.
[68] Petrobart Limited v. the Kyrgyz Republic, p. 83–84.
[69] Petrobart Limited v. the Kyrgyz Republic, p. 86–87.

Petrobart had not established that it was entitled to compensation for loss of future profits.[69]

6.3.3 Concluding remarks regarding compensation

Since most of the respective tribunals' findings regarding damages in *Nykomb* and *Petrobart* are rather fact specific, only limited conclusions can be drawn from such cases. It should be noted, however, that in the absence of express provisions on the standard of compensation, the tribunals in both cases relied upon customary international law. This is consistent with the findings of other tribunals awarding compensation for violations of the standards of, *inter alia*, fair and equitable treatment, non-discrimination under BITs and NAFTA.[70] Guidance is usually sought from the ILC Articles on State Responsibility which in turn build on the principles laid down in the *Chorzów Factory* case. This is, however, only the first step in that it establishes the *standard* of compensation. As stated in Article 31 of the ILC Articles the standard is "full reparation".

When it comes to the *method* of establishing and calculating "full reparation", customary international law does not provide much guidance. The cases discussed above – as well as the above mentioned BIT and NAFTA cases – illustrate that the method chosen depends on, and varies with, the circumstances of each individual case, including, *inter alia*, the nature of the violation of the fair and equitable treatment standard and the type and nature of the investment in question. Sometimes the starting point might be the amount actually invested. In other cases, it might be more appropriate to focus on lost future profits as established by using the DCF method.

An additional observation that may be made is that it would seem that the issue of causality has the potential of creating more problems in this context than in relation to compensation for expropriation. One possible explanation is that violation of, *inter alia*, the fair and equitable treatment standard and the non discrimination standard do not automatically result in the elimination of the investment, as is mostly the case with expropriation, but rather results in a decline in the business in question, or some other negative consequence for the business. The difficulty is to determine the extent to which this is caused by the violation of the fair and equitable treatment standard.

For instance in *Nykomb*, where the investment – the local subsidiary Windau – was still in operation and the contract for delivery of electric power was still in force between Windau and Latvenergo, the tribunal made a clear distinction between the damage suffered by Nykomb and the damage suffered by Windau. The tribunal only awarded damages to compensate Nykomb for the loss that it had actually suffered, and not for losses suffered by Windau. Nykomb's damage was quantified as a proportion of the

[70] See e.g. *MTD Equity Sdn. Bhd. and MTD Chile S.A. v. Republic of Chile*, ICSID Case No. ARB/01/7, Award of 25 May 2004; *CMS Gas Transmission Company v. The Argentine Republic*, ICSID Case No. ARB/01/8, Award of 12 May 2005; *Azurix Corp v. The Argentine Republic*, ICSID Case No. ARB/01/12, Award of 14 July 2006; *S.D. Myers, Inc. v. Canada*, 8 ICSID Reports (2005) 18; *Marvin Feldman v. Mexico*, ICSID Case No. ARB(AF)/99/1, Award 16 December 2002.

earnings that would have been generated by Windau had there not been any breach of the treaty. In other words, the tribunal estimated the dividends that would have been collected by Nykomb from its subsidiary, rather than establishing a reduction of the value (if any) of Nykomb's shares in Windau.

7. Concluding Remarks

My observations and conclusions with regard to *Nykomb*, *Petrobart* and *Plama* have already been made in relation to the issues of "jurisdiction" and "compensation", and shall not be repeated here. It is striking, however, and probably a manifestation of the fact that the ECT still is a rather young and "untested" investment protection treaty, that the mere three awards that have been made to date involve so many issues of general interest.

It is likely that future ECT awards will also involve issues of general interest for the application of the ECT. In this regard it may be noted that after a somewhat "slow start" for the investment protection regime of the ECT, investors have now started to discover the treaty. Nine new arbitrations under the ECT were registered during 2005 and 2006, compared to four during the period 1998–2004. With increasing investor awareness of the treaty, we are likely to see a continued steady stream of cases during the coming years.