Energy Charter Treaty—alternative energy production—feed-in tariffs—fair and equitable treatment—regulatory measures—legitimate expectations—relationship between EU law and investment treaties

CHARANNE B.V. v. SPAIN. SCC Case No. 062/2012. *At* http://www.italaw.com.
Stockholm Chamber of Commerce, January 21, 2016.

On January 21, 2016, an arbitral tribunal (Tribunal) adopted its award in *Charanne B.V. v. Kingdom of Spain*, a case administered by the Stockholm Chamber of Commerce.[1] This is the first award of the approximately thirty investment arbitrations currently pending against Spain that arose from its recent revocation of incentives for companies to use renewable energy sources in generating electricity. The award affords the first insight into how arbitrators evaluate the expropriation and fair and equitable treatment claims against the Spanish regulations adopted in 2010. In deciding on jurisdiction and the merits together, the Tribunal also clarified for the first time that arbitration provisions in investment treaties are fully effective between member states of the European Union (EU) even when they were adopted after the EU treaties entered into force for them.

The claimants in this dispute were a Netherlands corporation, Charanne B.V., and a Luxembourg corporation, Construction Investments S.A.R.L. The two companies held 18.6583 percent and 2.8876 percent, respectively, of the Spanish-registered Grupo T-Solar Global S.A. (T-Solar), which owned thirty-four solar power plants. The claimants filed a request for arbitration against Spain on May 7, 2012, under the 1994 Energy Charter Treaty (ECT),[2] claiming approximately US$10 million in damages for losses allegedly resulting from certain regulatory measures adopted by the Spanish government. In 2007 and 2008, two regulations, Royal Decrees (or RDs) 661/2007 and 1578/2008, established a generous feed-in tariff system payable to solar energy producers that supplied electricity into the general grid, which reduced the need for conventional energy production. This generous system was curbed in 2010, when the government adopted two regulations that negatively affected claimants' situation. RD 1565/2010 eliminated the electricity producers' right to a guaranteed tariff after the twenty-sixth year of operation (later extended to the thirtieth year) and required solar energy producers to install mechanisms to protect the general grid from drops in voltage. Legislative Decree (or LD) 14/2010 limited the maximum number of hours during which the producers could feed electricity into the general grid and imposed a toll on them for access to the grid. The companies contended that the two regulations effectively constituted an indirect expropriation of their investments in T-Solar and a breach of the fair and equitable treatment standard, and that LD 14/2010 violated their right to an effective means of recourse.

Spain raised four objections to the Tribunal's jurisdiction. First, it alleged that the dispute was moot because a subsequent regulation (LD 9/2013, adopted on July 12, 2013) had repealed the entire feed-in tariff system, including the 2010 modifications. As a consequence,

[1] Charanne B.V. and Construction Investments S.A.R.L. v. Kingdom of Spain, SCC Case No. 062/2012 (Jan. 21, 2016), *at* http://www.minetur.gob.es/es-es/gabineteprensa/notasprensa/2016/Paginas/index.aspx (search for "Charanne"; then follow link "Se resuelve") [hereinafter Award] (Spanish and Eng. trans.). For the Dissenting Opinion of Prof. Dr. Guido Santiago Tawil, see *id.* (Spanish only). Quotes from the Award and the dissent below, including internal citations in the text, are taken from the Tribunal's translations. The Award and Tawil dissent, together with unofficial English translations, and all other arbitrations cited below, are available at http://italaw.com.

[2] Energy Charter Treaty, Dec. 17, 1994, 2080 UNTS 95.

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there was no actual dispute about the validity, effects, and contents of those rules (paras. 188–93). The Tribunal dismissed this objection on the basis that, even if the 2010 regulations had been effectively annulled in 2013, they had at least temporarily affected the claimants' energy investments in Spain (paras. 452–54).

Second, Spain argued that the claimants' concerns about the 2010 regulations had already been addressed to the Spanish Constitutional and Supreme Courts, and to the European Court of Human Rights, which precluded the Tribunal from revisiting the issue (*electa una via*). In rejecting this argument under ECT Article 26(2), the Tribunal noted that, for the bar to apply, the prior complainants to a domestic court must be the same entities that started the investment arbitration (para. 408). Charanne and Construction Investments were only minority shareholders in T-Solar, one of the domestic complainants against the 2010 regulations. But even though they belonged to the same group of companies, the Tribunal required "substantial identity" between the companies, which was not the case (*id.*). Therefore, the prior complaints did not constitute a valid bar to the Tribunal's jurisdiction (para. 410).

Third, Spain alleged that the real investors behind Charanne and Construction Investments were Spanish citizens, who could not benefit from the ECT's provisions in a case against Spain. The Tribunal held that ECT Article 1(7) provides for protection if the company is constituted in accordance with the legislation of the state party. Since there was no dispute about the legality of Charanne's and Construction Investments' incorporation, and the Tribunal had no reason to believe that the claimants had committed any fraud so as to invoke the Tribunal's jurisdiction, the arbitrators dismissed this preliminary objection (paras. 412–17).

Spain also argued that any decision on this matter by the Tribunal would be incompatible with the Spanish Constitution and public order (para. 418). The Tribunal observed that its task was to apply the ECT and not Spanish constitutional law, although it recognized that considerations of Spanish public order might influence its interpretation of the relevant rules (paras. 420–22). The Tribunal further held that Spain had not discriminated against foreigners with regard to access to the courts of justice because the ECT governed access to international arbitration, which was different from the exercise of judicial powers by Spain (para. 423).

Fourth, Spain alleged that the dispute was an intra-EU matter subject to the exclusive jurisdiction of the European Court of Justice. On this point, the Tribunal assessed the parties' arguments in three steps. First, it noted that the existence of the European Union did not extinguish the statehood of its member states (paras. 427–32). Second, the Tribunal affirmed that the "implicit disconnection clause" enshrined in Article 267 of the Treaty on the Functioning of the European Union,[3] applicable to disputes between EU member states, does not apply to disputes between private parties and EU member states (para. 438). As a third and final step, the Tribunal stated that the ECT dispute resolution mechanism, that is, investment arbitration pursuant to ECT Article 26(4), is compatible with EU law, especially Article 344 of the Treaty on the Functioning of the European Union (para. 444). The Tribunal noted that an investigation was pending against Spain before the European Commission for alleged violation of the rules on state aid, which includes the system of remuneration for renewable energy. According to the Tribunal, if the Commission found a violation of the state aid rules, problems might arise

[3] Consolidated Version of the Treaty on the Functioning of the European Union, Dec. 13, 2007, 2012 O.J. (C 326) 47.

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about the validity of the arbitral award (para. 449). Since that case was still pending, however, the Tribunal could not take it into account in resolving the dispute before it.

Turning to the merits, the Tribunal addressed the claimants' claims about expropriation, the right to effective means of recourse against government measures, and the fair and equitable treatment standard.

As for expropriation, the claimants alleged that, by adopting the regulations in question, Spain had effectively deprived them of the value of the returns from their shares in the local subsidiary. They alleged that their return for the solar energy plants installed pursuant to RD 1578/2008 had been reduced by about 10 percent, from 9.41 percent to 8.48 percent, and their return for those pursuant to RD 661/2007 by about 8.5 percent, from 7.36 percent to 6.72 percent (para. 284). The Tribunal clarified that Charanne's and Construction Investments' holdings were in shares, as defined by ECT Article 1(6)(b), not in returns, as defined by ECT Article 1(6)(e) and alleged by the claimants (para. 459). As a consequence, the Tribunal stated, the claimants could ask the Tribunal to evaluate the reduction in their income from the shares only as the respective share value, and not as affecting any rights to specific returns from those shares in the future (para. 460).

The Tribunal analyzed the claimants' allegations in accordance with the widely accepted view among investment arbitration tribunals that, for a finding of indirect expropriation under ECT Article 13, the effects of the measure concerned must amount to a deprivation of property or destruction of the value of the investment (para. 464). The Tribunal noted that the reduction in returns from the claimants' shares was less than 10 percent, and that the claimants themselves had admitted that their investments still yielded positive returns. These considerations led the Tribunal to conclude that the economic and financial impact of the Spanish governmental measures had not been sufficiently severe as to constitute an indirect expropriation (paras. 466–67).

The Tribunal also dismissed the allegation by the claimants, based on ECT Article 10(12), that Spain had not granted them effective means to appeal against LD 14/2010. They contended that the only reason the government had changed the feed-in tariff regulation by legislative decree was to avoid public debate and the filing of administrative appeals (para. 469). But the Tribunal noted that legal recourse is available against a Spanish LD through the filing by an ordinary judge of a question of unconstitutionality to the Constitutional Court or the bringing of an administrative claim for damages against the responsible public body (para. 471). Such legal recourse sufficed for the purposes of ECT Article 10(12), because international law does not require states to provide for a specific form of legal recourse but only for such legal recourse, as in this case, as would allow for some sort of constitutional control—be it direct or indirect—and for compensation for damage (para. 472).

The claimants further alleged that Spain had infringed the fair and equitable treatment clause of ECT Article 10(1) because the detrimental modification of the feed-in tariff regime by the 2010 regulations had violated the companies' legitimate expectations. The Tribunal agreed that a state generates legitimate expectations when it engages with an investor through a direct legal relationship—for example, a stabilization agreement— or when it adopts general legislation creating specific obligations to the benefit of an investor (paras. 489–92). But it rejected the claimants' allegation that, at the time of the investment, Spain had made a specific commitment giving rise to legitimate expectations that the 2007 and 2008 decrees would not be modified (para. 494). None of the evidence considered by the Tribunal—the Spanish policy

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documents, the government's presentations to attract investment in the solar energy sector, the Spanish rules on the feed-in tariff— granted investors specific assurances that the legislation would not be modified (para. 511).

As regards proportionality, the Tribunal concluded that the 2010 regulations had not substantially changed the legislative framework for solar energy production in Spain (paras. 517–40). But the arbitrators recognized that their holding that the proportionality principle had not been violated was limited to their analysis of the 2010 regulations. They indicated that other tribunals should not automatically extend this holding to the 2013 regulations, which had further dismantled the feed-in system for alternative energy (para. 542).

The Tribunal considered the claimants' contention that the state had violated their right not to be subjected to retroactive regulations as essentially a different formulation of the argument about fair and equitable treatment—that the regulations should have remained unaltered. This argument was dismissed because the 2010 regulations had not been retroactive but, rather, had immediate effect on current situations (paras. 543–49). The Tribunal explained that no principle of international law prevents a state from adopting regulations with immediate effect on ongoing situations, absent a specific obligation undertaken by the state, for example through a contract (para. 548).

With respect to the costs of the arbitration, even though it had ruled against the claimants on all counts, the Tribunal required the claimants to pay only half of Spain's capped legal costs of 1 million euros, among other expenses, because the state had unsuccessfully raised complex issues of jurisdiction (paras. 562–66).

Arbitrator Guido Santiago Tawil attached a partial dissent to the award,[4] which argued that Spain's 2010 regulations had in fact violated the claimants' legitimate expectations. The Spanish government had given several specific promises and assurances that it would not modify the regulations, such as in Article 44(3) of RD 661/2007 (Tawil, arb., diss. op., para. 6). Tawil further maintained that the inclusion in the public register of solar installations under Article 14 of RD 661/2007 created expectations in investors that the feed-in tariffs would not be modified (*id.*, para. 9).

* * * *

This decision is the first investment arbitration award in an intra-EU dispute involving investors from long-standing EU member states, namely, the Netherlands and Luxembourg (member states since 1958), and Spain (a member state since 1986), for alleged violations of investment protections adopted in the 1994 ECT, which entered into force after the states joined the European Union.

Until now, intra-EU investment arbitrations have dealt with disputes only on the basis of investment treaties that were already in force at the time of the respondent state's accession. Arbitral tribunals interpreting these treaties in light of EU law have looked to Article 344 of the Treaty on the Functioning of the European Union, which establishes the exclusive jurisdiction of the Court of Justice over disputes between states involving EU law. But they have

[4] *See supra* note 1.

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consistently held that Article 344 does not apply to investment arbitration because these disputes are between a private party and a state.[5] This position seems reasonable because, if the Article 344 argument had any viability, all the judgments between private parties and states rendered by the European Court of Human Rights would be without effect, since they, too, may apply EU law. The latter court—like the investment arbitration tribunals—has reaffirmed its jurisdiction, holding EU member states responsible in situations where EU law or state practice in compliance with EU law violated the European Convention on Human Rights.[6]

The Tribunal in the present case arrived at the same conclusion, even though the EU legal system was already in force when the investment treaty entered into force. The Tribunal drew an analogy with domestic courts, which also could not apply EU law if they followed Spain's interpretation of Article 344, claiming that any dispute related to EU law must be settled by EU courts. In this context, the Tribunal recalled *Eco Swiss China Time Ltd v. Benetton International BV*,[7] which confirmed the validity of commercial arbitration even though the arbitrators may have to apply EU law (para. 443). Within this broader context, it seems sensible for the Tribunal to have rejected Spain's allegations, supported by the European Commission, that the intra-EU arbitration was incompatible with the EU judicial system. The award thus constitutes another setback for the European Commission, which has been trying to exercise more control over member states' investment arbitrations and to defer those disputes to the EU tribunals.[8]

This award is also the first decision about the dismantling of the incentives for the renewable energy sector in Spain that started in 2010, on the verge of the economic crisis in that country. It came even before the European Commission has completed its investigation of the allegations of illegal state aid, and the Tribunal did leave open whether the award would be enforceable if the Commission found a violation of EU competition law. The Tribunal did not evaluate the whole cluster of regulations adopted by Spain, but only those of 2010. While they started the dismantling of the incentives, later regulations eventually had a stronger impact on them.[9] The Tribunal expressly clarified that its decision was limited to the impact of the 2010

[5] Electrabel S.A. v. Republic of Hungary, ICSID Case No. ARB/07/19, Decision on Jurisdiction, Applicable Law, and Liability, para. 4.151 (Nov. 30, 2012); Achmea B.V. v. Slovak Republic [formerly Eureko B.V. v. Slovak Republic], PCA Case No. 2008-13, Award on Jurisdiction, Arbitrability and Suspension, para. 276 (UNCITRAL Oct. 26, 2010); Eastern Sugar BV (Netherlands) v. Czech Republic, SCC Case No. 088/2004, Partial Award, paras. 119–25 (Mar. 27, 2007).

[6] See, for instance, the judgments by the European Court of Human Rights in *Matthews v. United Kingdom*, 1999-I Eur. Ct. H.R. 251, paras. 26–54; *Cantoni v. France*, 1996-V Eur. Ct. H.R. 1614, paras. 28–34. In *Bosphorus Airways v. Ireland*, the European court even stated that the member states remained responsible when they merely executed rules of EU law without taking any regulatory action on their own. Bosphorus Hava Yollari Turizm ve Ticaret Anonim Şirketi v. Ireland, 2005-IV Eur. Ct. H.R. 107, paras. 135–38.

[7] Case C-126/97, Eco Swiss China Time Ltd v. Benetton Int'l NV, 1999 ECR I-3055.

[8] The European Commission has initiated infringement procedures against several EU member states for not having terminated their intra-EU bilateral investment treaties. *See* European Commission Press Release IP/15/5198, Commission Asks Member States to Terminate Their Intra-EU Bilateral Investment Treaties (June 18, 2015), *at* http://europa.eu/rapid/press-release_IP-15-5198_en.htm. The Commission is even leaning against investment arbitration tribunals altogether, instead proposing the establishment of permanent tribunals composed of a larger number of judges. *See, e.g.*, Eur. Comm'n, Transatlantic Trade and Investment Partnership, ch. II, sec. 3, subsec. 4, Art. 9: Tribunal of First Instance (draft text Sept. 2015), *at* http://trade.ec.europa.eu/doclib/docs/2015/september/tradoc_153807.pdf.

[9] Such a measure was, notably, LD 9/2013, which repealed RD 661/2007 and RD 1578/2008.

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regulations and did not mean that the same result would occur if all the regulations adopted since 2010 were taken into account.

The claimants' strongest argument was that the abrupt changes in legislation had violated the fair and equitable treatment standard by thwarting the investors' legitimate expectations stemming from the previous legal framework on feed-in tariffs. The Tribunal required strict evidence that Spain had promised not to change the legal framework created under the relevant 2007 and 2008 decrees, and that the 2010 regulations fit within the general legislative framework on electricity, that they were not irrational or arbitrary, and that they had been adopted in the public interest (paras. 533–35).

This approach is consistent with the reasoning adopted in some other investment arbitrations. The cases of *Parkerings-Compagniet v. Lithuania* and *El Paso Energy International Co. v. Argentina* recognized wide latitude for state regulatory action, unless a specific contract existed or the regulation was changed "unfairly, unreasonably or inequitably" or even "total[ly]."[10] In essence, the regulation had to guarantee to the investor that the regime would not be changed.[11] Such an analysis is necessarily fact specific. In the present case, the Tribunal balanced the elements in the regulation that assured the investor of regulatory stability—in particular, because the regulation set specific prices for a thirty-year period and beyond—against general statements that Spain promoted renewable energy by allowing investors "reasonable" returns and a long-term perspective on their investments. The majority interpreted the prices payable for the feed-in tariffs as only one possible aspect of the favorable renewable energy policy. The government could change the incentives, as long as the measures continued to adhere to a favorable policy on renewable energy. Since the claimant companies lost only 10 percent and 8.5 percent of their revenue, the Tribunal's assessment was probably justified.

Nevertheless, this finding might be more difficult to reach with respect to other companies that, by relying on the relevant decrees, had assumed a higher business risk and lost a larger share of returns than the Charanne and Construction Investments claimants. In such situations, an arbitral tribunal might rule in favor of the investor, basing its award on precedent that demanded a higher standard from the state than the *Parkerings-Compagniet* or *El Paso Energy* tribunals, among others. For instance, in *Metalclad Corp. v. Mexico* and *Técnicas Medioambientales Tecmed, S.A. v. Mexico*,[12] the arbitral tribunals required a stable and coherent legal framework, and in *Tecmed* the tribunal even stated that the investor must "know beforehand any and all rules and regulations that will govern its investments . . . to be able to plan its investment."[13] In *PSEG Global Inc. v. Turkey*, the tribunal rejected the claimants' arguments on breach of the fair and equitable treatment standard because the state and the investor had made no explicit agreement that would guarantee regulatory stability; the state had not attracted that investor specifically to make the flawed investment; and the state had not violated the good

[10] Parkerings-Compagniet AS v. Republic of Lithuania, ICSID Case No. ARB/05/8, Award, para. 332 (Sept. 11, 2007); and El Paso Energy Int'l Co. v. Argentine Republic, ICSID Case. No. ARB/03/15, Award, para. 374 (Oct. 31, 2011); respectively.

[11] *El Paso Energy Int'l Co.*, *supra* note 10, para. 374. See also, implicitly, *Continental Cas. Co. v. Argentine Republic*, ICSID Case No. ARB/03/9, Award, para. 261 (Sept. 5, 2008).

[12] Metalclad Corp. v. United Mexican States, ICSID Case No. ARB(AF)/97/1, Award, para. 99 (Aug. 30, 2000); Técnicas Medioambientales Tecmed, S.A. v. United Mexican States, ICSID Case No. ARB(AF)/00/2, para. 154 (May 29, 2003).

[13] *Tecmed*, *supra* note 12, para. 154.

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faith principle.[14] Yet, in spite of this apparently correct conduct by the state, the tribunal in *PSEG Global Inc.* did find a violation of the fair and equitable treatment standard because, among other reasons, the state had continuously changed the law applicable to the investment.[15] This finding might be successfully applied to the 2010 modifications of the solar energy regulations in Spain, or at least to the whole group of changes adopted between 2010 and 2013. In addition, in the context of complex economic sectors such as solar energy production, which need specialized technology to comply with regulatory requirements, frequent legislative changes can be especially damaging because of increased regulatory compliance costs.

In the present case, the Tribunal analyzed the normative elements of the fair and equitable treatment standard in its reasoning, but from its reiteration of the reduced economic impact of the measures on claimants' economic performance, the award conveys the impression that the Tribunal had performed a sound economic analysis to infer the disproportion between the financial impact and the claimants' international law claims. As indicated above, however, other tribunals called to evaluate the Spanish legislative changes in the renewable energy sector may not follow the same reasoning, especially if claimants allege a greater impact on their returns from the 2010 regulations. This decision demonstrates the continuing uncertainty surrounding the fair and equitable treatment and expropriation standards, and it shows that tribunals, while considering the legal elements that constitute these standards, also weigh material or equitable justice.

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Universal jurisdiction to enforce—torture as crime against humanity—duty to investigate—crimes committed in foreign country—limiting principles—lack of presence of accused

NATIONAL COMMISSIONER OF THE SOUTH AFRICAN POLICE SERVICE v. SOUTHERN AFRICAN HUMAN RIGHTS LITIGATION CENTRE. 2014 (12) BCLR 1428 (CC).
Constitutional Court of South Africa, October 30, 2014.

On October 30, 2014, the South African Constitutional Court (Court) ruled that the South African Police Service (SAPS) was obligated, by virtue of both domestic and international law, to investigate allegations that torture (as a crime against humanity) had been committed in Zimbabwe by the Zimbabwean police against citizens of Zimbabwe.[1] Such an investigation could proceed, the Court stated, even though no individuals suspected of committing the alleged crime were in fact present on South African territory because Zimbabwe had proved unwilling or unable to conduct the investigation itself, because a reasonable possibility existed that the investigation would find relevant evidence, and because the possible presence of suspects in South Africa in the future could not be discounted. The decision articulates a broad,

[14] PSEG Global Inc. v. Republic of Turkey, ICSID Case No. ARB/02/5, Award, paras. 242–45 (Jan. 19, 2007); *see also* Award, paras. 476–539 (analyzing the same concepts in its consideration of the legitimate expectations standard).

[15] *PSEG Global Inc.*, para. 250.

[1] Nat'l Comm'r of S. Afr. Police Serv. v. S. Afr. Human Rights Litig. Ctr., 2014 (30) ZACC 1 (CC), 2014 (12) BCLR 1428 (CC), *available at* http://www.saflii.org/za/cases/ZACC/2014/30.html.

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