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Investment arbitration as a possible remedy for investments affected by Bulgaria's suspension of the south stream pipeline project

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We recently learnt of the surprising news that Bulgaria has suspended construction on the South Stream pipeline in its territory, which would have serious consequences cancelling the entire project. This pipeline was due to bring gas from Russian sources to southern and central Europe along the Black Sea seabed and through the Balkans. As for the organization of the company involved, it is owned by a Dutch holding company with Gazprom holding 51% of the share capital.

Bulgaria claims to have made this decision after lengthy consultations with the European Union authorities and has given the following reasons for the suspension. Firstly, this new construction project would violate EU regulations on energy and the environment. Secondly, that the project did not comply with European regulations on the adjudication of public contracts. And finally, that the agreements signed by Bulgaria with the owners and builders of the pipeline are also in breach of EU laws. All this reasoning is highly debatable and would require lengthy analysis that is beyond the scope of this article.

Where we do want to focus now is on the legal mechanisms which, in the absence of a negotiated political solution, the investors

harmed by the Bulgarian Government's decision could use to protect their interests. In this regard we must remember that Bulgaria, Holland and the Russian Federation are signatories to the Energy Charter Treaty signed in Lisbon on 17 December 2004. This Treaty aimed to establish a legal framework promoting long-term cooperation in the field of energy for the countries' mutual benefit.

From the start we must make it clear that the issue at hand with Bulgaria is fully covered by the scope of this Treaty. This can be clearly appreciated when we look at the definitions therein under article 1. It defines economic activity in the energy sector as (with some exceptions also set out by the text): "an economic activity concerning the exploration, extraction, refining, production, storage, land transport, transmission, distribution, trade, marketing, or sale of Energy Materials and Products". The definition of 'investment' is very broad, and includes "every kind of asset, owned or controlled directly or indirectly by an Investor" (tangible and intangible goods, property rights and shares, credits, intellectual property, returns and any rights conferred by law or contract or by virtue of any contracts or licenses granted by Public Authorities). The investor, with regard to another Contracting Party, is a natural person who has the nationality of that State and resides there permanently according to the applicable national law, or to legal persons constituted in accordance with the applicable legislation in the country. With regard to a third State, an investor is the natural or legal person who complies, mutatis mutandis, with the aforementioned conditions for investors from signatory states to the Treaty.

The conventional text, which regulates a variety of issues (international markets, sovereignty over energy resources, environmental issues, taxation, privileged state entities, etc.) pays special attention to the promotion and protection of investments and to the resolution of disputes, focusing on the difference between an investor and a Contracting Party. At the outset we must point out the relationships and potential differences between the Treaty and other International Agreements are solved using a 'most favorable' principle. I.e. the Agreement applied will be the one that is most favorable to the investor or investment (article 16).

Part III of the Treaty (articles 10-17) regulates the promotion and protection of investments. Fair and equal treatment of the investments made by investors from other Contracting Parties is guaranteed, and cannot be less favorable that the treatment prescribed by International Law, including obligations derived from the treaties. Also, it literally states that "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" (article 10.1 in fine).

The definition of "treatment" is set out in article 10.3, and means treatment "accorded by

Contracting Parties which is no less favorable than that which it accords to its own Investors or to Investors of any other Contracting Party or any third state, whichever is the most favorable".

Regarding investments in its territory, each State will endeavor to restrict the exceptions to the treatment set out in article 10.3 to a minimum, and to gradually ease restrictions on investors from other Contracting Parties.

The States will give investments made by investors from other Contracting Parties, as well related activities (management, maintenance, use, enjoyment etc…) treatment which is no less favorable than that given to the investments of their own investors or investors from another Contracting Party or third State, with the most favorable treatment available being the one that must be applied (article 10.7).

Logically, the conventional text pays special attention to the system for expropriation (article 13). Investments shall not be subject to nationalization, expropriation or measures with equivalent effect unless the decision is motivated by the public interest, is not discriminatory, is done under due process of law, and prompt and effective compensation is paid. Also, the text states that expropriation includes those cases where a Contracting Party expropriates the assets of a company based in its territory in which investors from another member state have invested, including when this has been set up via participation in their share capital. In all cases, the affected investor will have the right, in accordance with the host country's legislation, for a court or other competent and independent authority to review its case, the value of its investment and the payment of the compensation.

In the present case, the behavior of the Bulgarian authorities could be considered an indirect expropriation or a measure with equivalent effect, since it involves actions that will depreciate or reduce the core value of the investment. We must remember that their decision has a large economic impact and interferes with the legitimate expectation of the investors, since it infringes their rights granted to them by previous authorizations.

The amount of compensation that the person subject to an expropriation should receive is equal to the fair market value of the investment immediately before the announcement of the measure or the intent to carry out the measure that affects the value of the investment. The value should be expressed in a freely convertible currency chosen by the investor and include fixed interest in accordance with market rates.

In this regard we must point out that the Treaty also expressly guarantees the freedom to transfer payments related to the investment across borders, including: the initial capital, additional capital, returns, payments under a contract, including loans, unspent income, proceeds from the whole or partial sale of the

investment, payments arising out of the settlement of a dispute, and the compensation for expropriations and responsibility for losses. The transfers are to be made without delay and in a freely convertible currency (article 14).
In the same way we must remember that that conventional text recognizes the right to subrogation when a Contracting Party or its designated agency makes a payment under an indemnity or guarantee given in respect of an investment of an investor in the territory of another Contracting Party (article 15).

Part V of the Treaty deals with the settlement of disputes. Article 27 regulates differences between Contracting Parties as to the interpretation or application of the Treaty itself, establishing mechanisms similar to those in Bilateral Agreements on Reciprocal Promotion and Protection of Investments. But this is a specific problem that does not concern us now.

What we are interested in right now is the Treaty's regulation of the settlement of disputes between an investor and a Contracting Party which is set out in article 26. This article establishes that if a dispute arises it must first, if possible, be settled amicably. If a solution is not found within a period of three months from the date on which either party to the dispute requested amicable settlement, then the investor may choose to submit it for resolution in one of three ways, a) before the courts or administrative tribunals of the Contracting Party that is party to the dispute; b) in accordance with any previously agreed dispute settlement procedure; c) in arbitration proceedings. Here it is important that Bulgaria is one of the countries included in Annex ID of the Treaty, and therefore does not permit an investor to submit the same dispute to arbitration if it has previously applied to the ordinary courts or used a previously agreed dispute settlement procedure.

When the investor chooses arbitration, it must send its consent in writing for the dispute to be submitted to: a) The International Centre for Settlement of Investment Disputes (ICSID) opened for signature at Washington, 18 March 1965, or as necessary its Additional Facility Rules; b) a sole arbitrator or ad hoc arbitration tribunal established under the UCITRAL Arbitration Rules; or c) an arbitral proceeding under the Arbitration Institute of the Stockholm Chamber of Commerce. The arbitral Tribunal will make its decision considering the Energy Charter Treaty and the applicable rules of International Law.

The arbitral awards made, which may include awards of interest, shall be final and binding on the parties. If a State and a sub-national government or authority are concerned, the award shall provide that the Contracting Party may pay monetary damages in lieu of any other remedy granted. The Contracting Parties shall carry out any such away without delay and shall make provision for the effective enforcement of such awards in its territory. Here we must remember that article 26.5.b)

indicates that at the request of any party to the dispute the arbitration will be held in a state that is a party to the New York Convention of 10 June 1958 on the recognition and execution of foreign arbitral awards.

The latest news we have indicates that political negotiations have started at the highest levels to try to unblock the problems caused by Bulgaria's decision to halt the construction of the South Stream pipeline. But if this possible solution does not come to fruition the investors harmed by the decision have, thanks to the Energy Charter Treaty, access to numerous mechanisms to protect their rights, including in particular the possibility of various forms of investment arbitration.

PARA MÁS INFORMACIÓN

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