GOVERNMENT ATTORNEY'S OFFICE
DIRECTORATE FOR STATE LEGAL SERVICES

SUBDIRECTORATE-GENERAL OF LITIGATION SERVICES

IN THE CASE OF AN ARBITRATION UNDER THE CONVENTION OF 1965 ON THE SETTLEMENT OF INVESTMENT DISPUTES BETWEEN STATES AND NATIONALS OF OTHER STATES (ICSID CONVENTION)

AND

UNDER THE ENERGY CHARTER TREATY
(ICSID ARBITRATION CASE No. ARB/15/42)

BETWEEN:

HYDRO ENERGY 1 S.À.R.L.
HYDROXANA SWEDEN AB

Claimants

and

THE KINGDOM OF SPAIN

Respondent

COUNTER-MEMORIAL ON THE MERITS AND MEMORIAL ON JURISDICTION

ARBITRATORS:

Lord Collins of Mapesbury, LL.D., F.B.A.
Prof. Rolf Knieper
Mr Peter Rees, QC

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is asserted in *Electrabel S.A v. Hungary*, that of "*a non-EU investor and an EU Member State or between an EU investor and a non-EU Member State.*"[12]

82. In this way, the intra-EU investor, with a protection level provided by EU Law, is protected by the judicial system of the EU. The investor from a third party country which is a signatory to the ECT (for example, a Japanese investor) which does not receive through the ECT in the EU Member States the "national" treatment which EU Citizen investors do receive because they are from the EU, may resort to arbitration to defend the rights granted to it by section (1) of Article 10 of the ECT. Any Arbitral Tribunal hearing this latter arbitration may not interfere with the competencies of the CJEU because the EU system does not apply to the investor from a third party country.

(3.3) The purpose of the ECT confirms the interpretation of the Kingdom of Spain

83. Assuming that intra-EU disputes are included within the scope of the protection of the ECT would also mean giving up the objective and purpose of the ECT. To be precise, it would mean assuming that the EU and its Member States promoted, as key players, the creation and conclusion of the ECT to cover an area, that of intra-EU investments, which had been totally covered - and in a far superior manner - for years by EU Law. What's more, it would mean taking competencies away from the CJEU and mistrusting the very protection system given by the EU to its Citizens.

84. The objective of the ECT is to establish "*a legal framework in order to promote long-term cooperation in the energy field, based on complementarities and mutual benefits, in accordance with the objectives and principles of the Charter*"[13]. For its part, the Charter was intended to "promote East-West industrial cooperation through the establishment of legal safeguards in areas such as investment, transit and trade." The ECT "is based on an energy community between the regions of the world that were divided by the iron curtain."[14]

85. In actual fact, the origin of the ECT lies in the wish of the Council of the then EC to speed up the economic recovery of Eastern Europe after the fall of the Berlin Wall through cooperation in the energy sector.[15]

86. Hence, the literal interpretation of Article 26 of the ECT, not only section (1) thereof but also section (6), in accordance with its context and purpose, leads to the fact that there are no grounds for submitting to arbitration disputes between an intra-EU investor and an EU Member State.

(4) The position of the Kingdom of Spain and the European Commission is confirmed by doctrine

[12] *Electrabel S.A v. Hungary*, ICSID No. ARB/07/19, Decision on Jurisdiction, Applicable Law and Liability, 30 November 2012 (original version in English), paragraph 4.158. RL-0002.
[13] Article 1 of the ECT. RL-0006
[14] Preface to the ECT. RL-0006
[15] Ibid.

87. The position expressed by the Respondent is also endorsed by doctrine. In this regard, Bruno Poulain has indicated that:

> *"The [ECT] was initially concluded with the former Soviet republics to improve the safety of the energy supply from Eastern Europe. Bearing in mind the initial raison d'être of this instrument, we cannot do any more than have reservations about its application to purely intra-community situations. Certain elements of its text also seem to endorse the inapplicability of [ECT] Article 26 to intra-Community situations."*[16] *(free translation) (footnote omitted)*

88. Moreover, as aptly stated by Professor Jan Kleinheisterkamp:

> *"Why should investors from certain member states enjoy a greater degree of protection than that afforded by the European Treaties? Why should arbitral tribunals, in a purely intra-EU context, not be bound to the same restrictions on judicial review as courts of the Union and the member states? Moreover, in the light of the fact that the European Treaties have put into place the well-tested procedural mechanisms that ensure that the EU laws, establishing supra-national standards of protection of investments within the internal market, are they applied and interpreted autonomously, untainted by national parochial conceptions, and uniformly? And going beyond the substantive standards of protection: why should European investors in the Internal Market be allowed to crosscut the existing supranational judicial system of the CJEU by using an alternative system of international arbitration?*
>
> *[…]In summary, there seem to be good reasons for the Commission to push for ensuring that EU law is the only regime governing investment flows within the European market and that the CJEU is the only ultimate instance for interpreting and applying these rules. And, indeed, it does not seem too far-fetched to expect the CJEU to follow the Commission on this point.[…]*
>
> *Given the Commission's strong determination to eliminate the parallelism of standards and recourses for investments inside the Internal Market, it can be expected that also the intra-EU dimension of the ECT will be eventually targeted by the Commission and may disappear if member states cooperate or are forced to cooperate by the CJEU."*[17] *(footnotes omitted)*

89. This author adds that:

> *"The essence of this conflict is, indeed, about whether tribunals can be allowed to review, on the basis of the latter, the legality of government measures that are, at least in theory, fully under the CJEU's control of the European market rules and*

[16] *Développements récents du droit communautaire des investissements internationaux*, Bruno Poulain, Revue Générale de Droit International Public, C XIII/2009, 4; page 881. The omitted footnote says: *"Our opinion is based on Article 25 of the [ECT], which proposes a disconnection clause to the benefit of the parties of a regional economic integration organisation and in Article 16, which appears to link material right and the controversy solution mechanism."* (free translation). RL-0060.

[17] *Investment protection and EU Law: the intra- and extra- EU dimension of the Energy Charter Treaty*, Jan Kleinheisterkamp, Journal of International Economic Act 15 (1), Oxford University Press, 2012, pages 101, 103 and 108. RL-0064.

fundamental rights, and the above sketched 'policy space' they reserve to the Union and the Member States."[18] *(footnotes omitted)*

90. In actual fact, as is stated by Professor Jan Kleinheisterkamp, the problem raised is not a problem of the selection and application of the "most favourable regulation". The issue is that between EU Member States and their Citizens, EU Law puts aside the application of any other regulation by virtue of the principle of supremacy.

91. It is thus a question of determining whether in the light of EU Law, it is valid to apply within the European Union in conflicts between an EU investor and an EU State the provisions of an International Treaty or whether, by contrast, in these intra-EU relations solely EU Law applies. Assuming that it is not disputed that EU Directives on Renewable Energies are the framework for Spanish legislation which the Claimants supposedly believed when making its investment, the issue must be settled in the light of the interpretation of Community Law and with regard to these matters Spain cannot submit its decision to forums other than the EU judicial system by dint of Article 344 of the TFEU.

92. As has been stated above, any dispute settlement system introduced by a Treaty affecting the fundaments of the EU is incompatible with the EU Law. Article 26(6) of the ECT requires the settlement of those issues under litigation in accordance with *"this Treaty [the ECT] and applicable rules and principles of international law"*. The rules and principles of the EU are rules and principles of International Law and must be applied with the same hierarchy as the ECT itself. Accepting arbitration to settle litigation which affects the freedom of establishment and the free circulation of capital of a Community investor in EU territory in the context of Renewable Energies is contrary to EU Law and incompatible with the actual content of Article 26(6) ECT.

93. For the sake of transparency and good faith, this Objection cannot be concluded without mentioning the impact on the result of this arbitration that may have the existence of a procedure before the European Commission as regards the evaluation of the measures supporting Renewable Energies and cogeneration in Spain (procedure SA.40348 2014/N).

94. This case must be understood in the light of the Order of 22 October 2014 of the Court of Justice of the European Union laid down regarding preliminary ruling C-275/13, (ELCOGAS case) referring to Spain, paragraph 33, which concludes as follows:

"Article 107 of the TFEU, section 1, must be interpreted in the sense that the amounts attributed to a private electricity producing company which are financed by all the electricity end users established in national territory and which are distributed to Electric Sector companies by a public organisation in accordance

[18] Ibid.

with predetermined legal criteria, constitute a State intervention or by means of State funds."[19]

95. Said legal classification made by the CJEU implies that the Member States are required to bear in mind the Guidelines on State aid for environmental protection and energy 2014-2020, approved by means of a Communication from the European Commission 2014/C 200/01 as well as those revoked and approved by the latter by means of a Communication from the European Commission 2008/C 82/01.

96. The existence of this procedure is particularly relevant in the light of the decision of the Commission of 26 May 2014, ordering Romania to suspend payment of an award handed down in an ICSID arbitration, *Micula v. Romania*. The Commission adopted a first decision, in accordance with Council Regulation (EC) No. 659/1999, which allows the Commission to suspend the payment of any aid which it considers illegal. Subsequently, through a decision on 30 March 2015 the Commission decided that "*the payment of compensation by Romania to two Swedish investors by dint of the revoked aid regime breaches the EU State Aid rules*" and that "*by paying the compensation granted to the Claimants, Romania is actually granting an advantage equivalent to the revoked aid regime*". The Commission thus concluded that said compensation is equivalent to State Aid incompatible with EU Law and must be returned by the beneficiary companies.[20]

97. We also must mention final Decision C(2016) 7827 of 28 November 2016 by the European Commission, issued on the SA.40171 (2015/NN)–Czech Republic aid case file in regards to the "Promotion of electricity production from renewable energy sources". The European Commission's interpretation in that Decision on the application of the ECT to intra-EU conflicts is particularly relevant.

"(147) In case of the Energy Charter Treaty, it is also clear from the wording, the objective and the context of the treaty that it does not apply in an intra-EU situation in any event. In general, when negotiating – as in the case of the Energy Charter Treaty – multilateral agreements as a "block", the Union and its Member States only intend to create international obligations vis-à-vis third countries, but not inter se. That has been particularly clear in case of the Energy Charter Treaty, which had been initiated by the Union in order to promote investment flows from the then European Communities to the East, and energy flows in the opposite direction, as part of the external action of the European Communities. It is also borne out by the wording of Articles 1(3) and 1(10) of the Energy Charter Treaty, which defines the area of a regional economic integration organisation as the area of that organisation. The lack of competence of Member States to conclude inter se investment agreements and the multiple violations of Union law set out above in

[19] Order of the Court of Justice of the European Union laid down regarding the preliminary ruling C-275/13, ELCOGAS, on 22 October 2014. (English version). R-0033.
[20] Decision (EU) 2015/1470 by the Commission on 30 March 2015 pertaining to State aid SA.38517 (2014/C) (ex 2014/NN) carried out by Romania, Arbitration Award Micula/Romania on 11 December 2013. R-0002.

recitals (143) to (145) also constitute relevant context for the interpretation of the Energy Charter Treaty in harmony with Union law, so as to avoid treaty conflict.
(148) For those reasons, the ten investors cannot rely on the Energy Charter Treaty or the German-Czech BIT.
(149) In any event, there is also on substance no violation of the fair and equitable treatment provisions. First, as explained above, the Czech Republic has not violated the principles of legitimate expectation and equal treatment, neither under its domestic law nor under Union law. As both under the Energy Charter Treaty and the German-Czech BIT Union law is part of the applicable law, the principle of legitimate expectation under the fair and equitable treatment provision has to be interpreted in line with the content of that principle under Union law. Second, in case of the Energy Charter Treaty, it has been expressly recognized by Arbitral Tribunals that the provisions of the Energy Charter Treaty have to be interpreted in line with Union law, and that in case of conflict, Union law prevails. It is settled case-law that a measure that does not violate domestic provisions on legitimate expectation generally does not violate the fair and equitable treatment provision.
(150) Finally, the Commission recalls that any compensation which the Arbitral Tribunals were to grant would constitute in and of itself State aid. However, the Arbitral Tribunals are not competent to authorise the granting of State aid. That is an exclusive competence of the Commission. If they were to award compensation, they would violate Article 108(3) TFEU, and any such award would not be enforceable, as that provision is part of the public order"[21] *(Emphasis added).*

(5) Conclusion

98. In view of the above, it is considered that the Arbitral Tribunal, with all due respect, lacks jurisdiction to hear the present intra-EU dispute brought by investors from Luxembourg and France against the Kingdom of Spain. Luxembourg, Sweden and Spain were all EU member States when the ECT went into effect. Hence, the Claimants fail to comply with the requirement foreseen in Article 26(1) of the ECT which states that in order to be able to resort to arbitration the dispute must be between a Contracting Party and an investor of a different Contracting Party.

B. Lack of jurisdiction of the Arbitral Tribunal to hear an alleged breach by the Kingdom of Spain of obligations derived from section (1) of Article 10 of the ECT through the adoption of taxation measures by Act 15/2012: absence of consent from the Kingdom of Spain to submit this matter to arbitration given that, pursuant to Article 21 of the ECT, section (1) of Article 10 of the ECT does not generate obligations regarding taxation measures of the Contracting Parties

(1) Introduction

99. Without prejudice to the Jurisdictional Objection described above, the Arbitral Tribunal, with all due respect, lacks jurisdiction to hear the dispute on the alleged breach by the Kingdom of Spain of obligations derived from section (1) of Article 10

[21] Final Commission Decision C(2016) 7827, of 28 November 2016, regarding case number SA.40171 in the State Aid Register (2015/NN)– Czech Republic. RL-0003

Union and ensuring that the consumer of electricity does not have to bear excessive costs in the different activities.

955. The outcome of the reform has been that some activities and their facilities have seen their remuneration revised upwards while others have seen it revised downwards. This is with the aim of respecting the basic principles of recovering the investment, maintaining operation and obtaining a reasonable rate of return.

956. This regime has respected the legal principles, developed and validated by case-law and known to each and every one of the diligent operators.

957. The new rules are characterised by their exhaustiveness as they involve a detailed examination of the costs of around 2,000 standard facilities, by the publicity of the procedures that led to the setting of the standard facilities and the parameters, and by the thoroughness involved in setting them.

958. Ultimately, this regulatory framework not only provides a global response to protecting and encouraging investments in Spain, but the Kingdom of Spain also maintains its commitment to continue subsidising the facilities.

959. In this sense, it is worth highlighting that the following costs estimate is included in the Economic Report of Order IET/1045/2014[601]:

TECHNOLOGY	Estimation of premiums received 1998-2013 (millions of €)	Estimation of outstanding premiums as of 2014 to the end of the entire lifespan (millions of €)	Estimation of the total premiums received throughout the entire lifespan (millions of €)
COGENERATION	12,917	19,504	32,421
PHOTOVOLTAIC	14,617	64,234	78,851
THERMOSOLAR	2,640	32,464	35,104
HYDROELECTRIC	4,263	1,250	5,513
WIND POWER	15,400	20,500	35,900
BIOMASS AND BIOGAS	2,003	6,685	8,688
WASTE TREATMENT	2,626	4,220	6,846
INCINERATION OF WASTE AND BLACK LIQUORS	1,827	1,708	3,535
TOTAL RENEWABLES, COGENERATION AND WASTE	56,294	150,565	206,859

(2.10) Existence of a European Commission State aid procedure in relation to Order IET/1045/2014 and the rules that this replaces.

960. As it has already been stated, the remuneration policy in favour of renewable energy sources in the European Union is subject to directives approved by the European Commission.

961. Until recently, there were different interpretations of the status of state aid of the amounts received by producers through the bills paid by consumers. These interpretative doubts have been clarified by the Order of 22 October 2014 of the

[601] Administrative record on draft Order IET/1045/2014; Regulatory Impact Analysis Memorial, page 100. R-0051. (Procedure, document 15.03).

Court of Justice of the European Union laid down regarding preliminary ruling C-275/13, (ELCOGAS case) referring to Spain, par. 33, which concludes as follows[602]:

" Article 107.1 TFEU must be interpreted as meaning that the sums awarded to a private electricity producer that are financed by all the end users of electricity within the national territory and distributed among the companies in the electricity sector by a public organisation according to predetermined legal criteria constitute aid granted by the State or through State resources ".

962. As a consequence of this resolution, Spain informed the European Commission of the support measures for renewable energy and cogeneration adopted through Ministerial Order IET/1045/2014. To this effect, the Commission has opened proceeding SA.40348 2014/N.

963. Article 4.3 of the Treaty on the European Union (TEU) establishes the obligations assumed by the State under the principle of loyal cooperation. In this way, according to the second and third paragraphs of this provision:

"The Member States shall take any appropriate measure, general or particular, to ensure fulfilment of the obligations arising out of the Treaties or resulting from the acts of the institutions of the Union.
The Member States shall facilitate the achievement of the Union's tasks and refrain from any measure which could jeopardise the attainment of the Union's objectives".

964. This provision does not establish a mere principle of limitation, but rather imposes binding obligations on States, whose breach can lead to, by application of Articles 258 and 260 of the Treaty on the Functioning of the European Union (TFEU), to a Ruling of the Court of Justice of the European Union to impose an economic penalty and/or a coercive fine on the State.

965. Among the obligations that the TFEU imposes on Member States, is the prohibition on granting state aid, except in the cases permitted by Treaties. In accordance with Article 107.1 of the TFEU, *"Save as otherwise provided in the Treaties, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market".*

966. Following the definition that the Elcogas Court Order provided on the concept of State Aid, the Respondent was obliged, under the provisions of Articles 107 and 108 TFEU, to notify the European Commission of the existence of support measures for renewable energy and cogeneration in Spain, relating to the arbitration proceedings that this Tribunal is considering.

967. Notification of the aid allows the State not only to comply with the obligations derived from the Treaties but also to ask the Commission to declare their

[602] Order of the Court of Justice of the European Union laid down regarding the preliminary Judgement C-275/13, ELCOGAS, on 22 October 2014. R-0033.

compatibility based on the Guidelines for state aid for environmental protection and energy 2014-2020. The declaration of compatibility through a Commission Decision is the only legal channel for the aid in question not to be recovered, in accordance with what is laid down in Articles 107.3.c) and 108 TFEU.

968. In accordance with Article 108 TFEU, the Commission has the exclusive power to declare the compatibility of an aid with the European Union Law, the only body that is competent to review the legality of this decision being the Court of Justice of the European Union, according to a well-established case-law.

969. Both the exclusive competence of the Commission to declare the compatibility of the aid, and that of the Court of Justice of the European Union to review the legality of the declaration, are mandatory regulations that do not permit any possible derogation and form part of the public policy of the European Union.

970. Consequently, and for reasons of transparency and good faith in the development of the arbitration proceedings, the Kingdom of Spain informs the Arbitral Tribunal of the existence of said proceedings.

971. Said communication is particularly relevant in the light of the decision of the Commission of 26 May 2014[603], ordering Romania to suspend payment of an award handed down in an ICSID arbitration, *Micula v. Romania*.

972. Subsequently, through a decision on 30 March 2015[604], the Commission decided that "the payment of compensation by Romania to two Swedish investors by dint of the revoked aid regime breaches the EU State Aid rules" and that "by paying the compensation granted to the Claimants, Romania is actually granting an advantage equivalent to the revoked aid regime". The Commission has, therefore, concluded that said compensation is equivalent to incompatible State Aid and must be returned by the beneficiary companies.

973. Finally, as has already been mentioned in Section III.B.1 of this Memorial, special emphasis should be given to Final European Commission Decision C(2016) 7827, of 28 November 2016, regarding state aid case number SA.40171 (2015/NN)– Czech Republic, on the "*Promotion of electricity production from renewable energy sources*", the contents of which have already been analysed.

K. The Measures in dispute have been acknowledged as necessary Macroeconomic control measures as well as stabilising the economy and reasonable measures.

974. The Claimant questions the rationality and proportionality of the measures from a regulatory viewpoint, based on the subjective opinion of its experts. However, this opinion contrasts with the opinions of various institutions and agents that have assessed the new regulatory framework.

[603] Document by the Commission C (2014) 6848 final of 1 October 2014, ordering Romania to suspend payment of an award handed down in an ICSID arbitration, Micula v. Romania. R-0180.
[604] European Commission decision of 30 March 2015 declaring the compensation recognised in arbitral award *Micula v. Romania* to be State aid incompatible with the TFEU (Press Communication of the Commission, English version). R-0002.

V. PETITUM AND RESERVATION OF RIGHTS

1351. In light of the arguments expressed herein, the Kingdom of Spain respectfully requests the Arbitral Tribunal to:

a) To declare its lack of jurisdiction over the claims of the Claimants or, if applicable, the inadmissibility of said claims.

b) Secondarily, should the Arbitral Tribunal decide that it has jurisdiction to hear this dispute, dismiss all of the Claimant's claims regarding the merits, as the Kingdom of Spain has in no way breached the ECT, pursuant to that expressed in section III herein, with regard to the merits of the matter;

c) Secondarily, to dismiss all the Claimant's claims for damages as the Claimant has no right to compensation, in accordance with section V herein; and

d) Order the Claimant to pay all costs and expenses derived from this arbitration, including ICSID administrative expenses, arbitrators' fees and the fees of the legal representatives of the Kingdom of Spain, their experts and advisors, as well as any other cost or expense that has been incurred, all of this including a reasonable rate of interest from the date on which these costs are incurred until the date of their actual payment.

1352. The Kingdom of Spain reserves the right to supplement, modify or complement these allegations and present any and all additional arguments that may be necessary in accordance with the ICSID Convention, the ICSID rules of arbitration, procedural orders and the directives of the Arbitral Tribunal in order to respond to all allegations made by the Claimant in regards to this matter.

Madrid, 24 February 2017

Respectfully submitted,

Diego Santacruz Descartin

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