



School of International Arbitration

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International Arbitration Case Law

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SUEZ, SOCIEDAD GENERAL DE AGUAS DE BARCELONA S.A. AND INTERAGUA SERVICIOS INTEGRALES DEL AGUA S.A

Case Report by Rodolfo Miranda Miranda**
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In a decision rendered on July 30, 2010, under the Bilateral Investment Treaties (BITs) between France and Argentina, and Spain and Argentina, this ICSID award set a standard regarding fair and equitable treatment in investment claims related to public contracts.

Arbitration Panel: Professor Jeswald W. Salacuse (President), Professor Gabriel Kaufmann-Kohler, and Professor Pedro Nikken.

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Digest

1. Introduction

Suez, Sociedad General de Aguas de Barcelona S.A. and InterAgua Servicios Integrales del Agua S.A., a ninety seven-page decision rendered in 2010, is an important award related to the Argentine crisis, and its consequences in government contracts and especially in international investment obligations derived from the BITs entered into by Argentina in the nineties. This award is relevant because it addresses the claims originated within the performance of a water concession agreement, as well as some important issues as expropriation, full protection and security and, finally, fair and equitable treatment (FET).

2. Relevant background and allegations by the Claimants

In the early nineties, Argentina was aware of the necessity of fostering foreign investment and improving public services, among others, water and sanitation. Therefore, it entered into Bilateral Investment Treaties with different countries. In addition, it enacted federal and sub-national laws and regulations fostering private investment in public services. In that context, Argentina entered into two BITs relevant for this case: one with Spain and another one with France, both in 1991.

Four years later, in 1995, after the issuance of national and sub-national laws fostering private investment in water and sanitation, the Province of Santa Fe (hereinafter Province) and Aguas Provinciales de Santa Fe S.A. (hereinafter APSF) signed a Concession Contract (in which, among other provisions, is set the right of the Concessionaire to tariff adjustment¹ and the duty of collaboration between the Parties) for 30 years². The Claimants are stockholders of APSF. Suez, a French company, submitted its claims under the Argentina-France BIT. On the other hand, InterAgua, a Spanish company, submitted its claims under the Argentina-Spain BIT.

After six years of good relations between Province and APSF and good results³, in 2001 came the Argentine crisis. Its economic effects and laws affected the

¹ p. 32

² Before the concession contract, Province itself (by Dirección Provincial de Obras Sanitarias) operated the water services, p. 9-11.

³ p. 12

concession. The Argentinean Government enacted laws forbidding indexation in concession contracts, putting aside the tight relationship between Argentinean Peso and US Dollar, and prohibiting concessionaires from suspending services. Moreover, other economic measures were taken that had a negative impact on the concession and the concessionaire itself.

APSF sought relief from Province by raising tariffs and diminishing APSF's investment obligations; in a nutshell, APSF sought renegotiation to recover the equilibrium after the measures taken by the Government. Province rejected APSF's requests, did not adjust tariffs, and was eager to request exact fulfillment of the investment plan. The Governor expressed his approval to renationalize the water services⁴. APSF tried to terminate the concession and finally, in 2006, Province terminated the Concession Agreement and drew performance bonds delivered by ASPF.

In the meantime, specifically in April 2003, Suez and InterAgua (owners of APSF) submitted a claim against Argentina before ICSID, based on the breach of the Argentina-France and Argentina-Spain BITs, stating namely (a) the lack of cooperation on the part of Province, (b) Province's refusal to increase tariffs and (c) Province's decision to terminate the Concession Agreement and to draw APSF's performance bonds.

According to the Claimants, said facts constituted a breach of both BITs on the part of Argentina, highlighting Argentina's (w) responsibility for direct or indirect expropriation, (x) responsibility for failure to provide protection and security and (y) failure to provide fair and equitable treatment (FET). On the other hand (z), Argentina contested the claims and raised the argument of defense of necessity⁵. Below is a summary of what the Tribunal stated on these issues.

3. *Important procedural issues*

Regarding procedural issues, it is worth mentioning that this case was joined with other cases of water concessions⁶. The award discussed herein is the award of the merits because the Tribunal decided to postpone the award of damages⁷.

⁴ p. 17

⁵ p. 38

⁶ p. 3

⁷ p. 92

The Tribunal declared that it only had jurisdiction to hear the treaty claims, not the contract claims⁸.

4. Analysis

4.1. Responsibility for direct or indirect expropriation

The Claimants said that BITs protect investors, granting them the right to receive compensation in the event of direct and indirect expropriation. Direct expropriation occurs when states take property directly from investors, while indirect expropriation occurs when *“host states invoke their legislative and regulatory powers to enact measures that reduce the benefits investors derive from their investments but without changing or cancelling investor’s legal title to their assets or diminishing their control over them”*⁹.

In this respect, the Claimants said that, as shareholders of ASPF, they had an indirect interest in the Concession and this constitutes an investment. They claimed that Province’s failure (for which Argentina had to answer internationally because States are to answer for the acts or omissions of their sub-national entities) to adjust tariffs and to cooperate, and, finally, its decision to finally terminate the Concession Agreements deprived the Claimants’ investments.

The Tribunal said that, the negative impact of the actions by Province notwithstanding, the Claimants maintained control of their investment and were not excluded from its management. Also, the Tribunal added that the Claimants always maintained the property and control of APSE, and that the measures enacted by the government diminishing investment value did not constitute expropriation¹⁰.

On the other hand, the Tribunal declared that Province’s failure to adjust tariffs did not constitute a substantial deprivation of the investment¹¹.

⁸ p. 19

⁹ p. 40

¹⁰ p. 43

¹¹ p. 47

Regarding the unfair termination claimed as expropriation, the Tribunal held that the Claimants did not have any rights over the physical water assets. Nevertheless, there are some cases where tribunals have held that contract termination is deemed as expropriation¹². In this case, Province was part of the contract and terminated it according to its own terms (though that same fact can constitute a breach of an international treaty)¹³.

Regarding the national measures taken to face the crisis in Argentina, the Tribunal considered that general measures do not constitute expropriation when they are accepted as “*within the police power of States*”¹⁴.

Therefore, the Tribunal declared that said measures did not constitute expropriation against the Claimants’ investments.

4.2. Responsibility for failure to provide protection and security

The Claimants argued that the obligation to provide full protection referred to physical and legal protection. Argentina rejected this argument and claimed that the obligation of providing full protection referred to protecting the investment in a physical manner¹⁵.

Even though the Tribunal recognized that other tribunals have provided broader protection (not only physical)¹⁶ in this regard, it was utterly convinced of the traditional concept of full protection: the duty of a State to protect investments against physical threats. This was not the case because at no time were APSF or its owners victims of physical attacks.

Regarding the interrelation between full protection and security and FET, the Tribunal held that the latter includes the former, so a violation of the duty of protection is a violation of FET, but not vice versa. Thus, “*stability of the business environment and legal security are more characteristic of the standard of fair and*

¹² p. 49

¹³ p. 51

¹⁴ p. 45

¹⁵ p. 55

¹⁶ p. 57

*equitable treatment, while the full protection and security standard primarily seeks to protect investment from physical harm.”*¹⁷

As a result, the Tribunal considered that Argentina had not violated its obligation of protecting and giving security to investments.

4.3. Failure to provide fair and equitable treatment

The first issue addressed by the Tribunal was the level of protection of FET, because the Argentina- France BIT referred to “*the principles of international law.*” Then Argentina argued that FET is limited “*to the international minimum standard, and that such limitation is also implicit in the Argentina-Spain BIT*”¹⁸.

However, the Tribunal rejected this argument because the reference is to principles of international law, not to the “*minimum standard under customary international law*”. Thus, according to the ordinary meaning interpretation stated in Article 31(1) of the Vienna Convention, FET is not limited to the international minimum standard; rather, it is to be interpreted using all relevant sources of international law¹⁹.

Argentina contended that it had breached the FET obligation because the country was undergoing a crisis and it was the duty of the State to adopt measures to face it. It also claimed that the concession had stopped being profitable for the Claimants even before the crisis²⁰.

Regarding the concept of FET, the Tribunal said that “*arbitral tribunals have increasingly taken into account the legitimate expectations that a host country has created in the investor and the extent to which conduct by the host government subsequent to the investment has frustrated those expectations.*”²¹

¹⁷ p. 59

¹⁸ p. 63

¹⁹ p. 64

²⁰ P. 69 -70

²¹ p. 74. In supporting its definition, Tribunal cited *Saluka* and *Bayindir vs. Pakistan*.

Regarding expectations, the Tribunal considered that Argentine laws, treaties and Province's legal framework for the concession created legitimate expectations in the Claimants²².

Even though the Tribunal rejected the aforementioned claims, it granted this claim, declaring that Province's acts and omissions in prejudice of APSF did constitute a breach of fair and equitable treatment (FET) on the part of Argentina against the Claimants.

Thus, the Tribunal considered that Province performed the following wrongful actions²³:

- Not cooperating with APSF to solve problems together.
- Not raising the tariffs as it was obliged to by the Concession Contract.
- Even worse, it raised tariffs in 129% in favor of the electricity company (operated by the State), but not in favor of the water services (operated by APSF)
- Severely limited renegotiation against APSF.
- Insisting on requesting APSF to fulfill its investment plan, despite its lack of resources.
- Preventing APSF from collecting infrastructure charges from new customers (as it was established in the Concession Contract), but not providing funds (cross subsidies) to finance service expansion.
- Terminating the Concession Contract, collecting performance bonds and not paying APSF's unamortized investments.

Those actions "*frustrated the legitimate expectations of the Claimants*" and, hence, constitute a breach of FET²⁴.

4.4. **Argentina's argument of defense of necessity**

Argentina referred to article 25 of the International Law Commission Articles of Responsibility by which States can invoke necessity as an exception to fulfill their international obligations if **(i)** the measure was the only way to safeguard an essential interest, **(ii)** does not seriously impair an essential interest of other

²² p. 76

²³ p. 78-83

²⁴ p. 84

States, **(iii)** the international obligation does not exclude the possibility of invoking necessity and **(iv)** the State has not contributed to the situation of necessity²⁵.

Regarding **(i)**, the Tribunal stated that Argentina did not meet this condition because Province had other “*more flexible means*”²⁶ for the continuation of the water services.

Regarding **(ii)**, the Tribunal stated that Argentina met this condition because the interests of the Spanish and French investors affected could not be considered as essential for France and Spain.

Regarding **(iii)**, the Tribunal stated that Argentina met this condition because neither BIT referred to necessity, and, therefore, they did not exclude the possibility of its application by the State.

Regarding **(iv)**, the Tribunal said that Argentina did not meet this condition. According to the Tribunal, though there was an international crisis, Argentina’s last governments did not handle the economy well (deficient fiscal policy, excessive spending, among others); hence, Argentina had contributed to its own state of necessity²⁷.

For the reasons stated above, the Tribunal rejected the argument of defense of necessity set forth by Argentina.

5. Decision

- Argentina did not expropriate the Claimants’ investments.
- Argentina did not breach the full protection and security duty.
- Argentina failed to provide the Claimants with fair and equitable treatment (FET).
- Argentina’s defense of necessity was not valid.
- Deference of the decision of damages (bifurcation).

²⁵ p. 85

²⁶ p. 89

²⁷ p. 90

6. *Pedro Nikken's separate opinion*

Pedro Nikken concurs with the decision, except with the arguments whereby the Tribunal considered that Argentina breached FET. He disagrees when it comes to considering “legitimate expectations” in defining FET because the reference to legitimate expectations goes beyond the FET regulations in international investment treaties.

Regarding the reference to “principles of international law” in the FET clause of the Argentina-France BIT, Nikken considers that is a “*clear reference to the minimum standard, the only standard on “treatment of aliens”*”, which is the only standard that existed at the time the BIT was signed²⁸.

To Nikken, FET obliges a State to act in due diligence by “*canons of good governance*”; FET does not include any stability commitment²⁹. Nikken considers that paragraph 307 of *Saluka* gives a good concept of FET.

To determine if FET was complied with or not by the State, Nikken says that it should be determined if “*measures taken by Argentina were such that any reasonably good government of a well-organized modern State could have adopted them if it had to deal with a crisis of the proportions faced by Argentina, or whether, on the contrary, and to what extent, they were unreasonable, disproportionate, discriminatory, or in any way arbitrary.*”³⁰

Argentina –Nikken affirms– acted as any country would act to face crisis, so its measures (i.e. freezing tariffs) did not violate FET.

Nonetheless, freezing tariffs should be exceptional and temporal, “*for the period strictly necessary to address the emergency*”³¹. Argentina, however, failed to increase tariffs after the crisis had ended, and failed to provide solutions to restore the economic balance of the concession. This conduct constitutes a breach of FET, and that is why finally Nikken concurs with his colleagues in saying that Argentina breached FET against the Claimants.

²⁸ Paragraphs 8 and 16.

²⁹ Paragraph 30.

³⁰ Paragraph 37.

³¹ Paragraph 43.