INTERNATIONAL CENTRE FOR SETTLEMENT OF INVESTMENT DISPUTES

United Utilities (Tallinn) B.V.

and

Aktsiaselts Tallinna Vesi

Claimants

v.

Republic of Estonia

Respondent

ICSID Case No. ARB/14/24

AWARD

The Tribunal
Mr Stephen L. Drymer, President
Prof. Brigitte Stern, Arbitrator
Sir David A. R. Williams QC, Arbitrator

Secretary of the Tribunal
Mr Paul-Jean Le Cannu

Assistant to the Tribunal
Ms Laurence Ste-Marie

Date of dispatch to the Parties: 21 June 2019

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TABLE OF CONTENTS

I. INTRODUCTION 1

II. PARTIES 1

III. PROCEDURAL HISTORY 1

IV. FACTUAL BACKGROUND 20

A) The Creation of ASTV and its Operation prior to the Privatisation 20

B) The Privatisation of ASTV 22

1) The Privatisation Process Established by the City of Tallinn 22

2) The "Derogation" concerning the Term of ASTV's License, and the 2000 EBRD Loan 26

3) UUTBV's Participation in the Tender Process 26

a) Creation of UUTBV 26

b) Discussions between UUTBV and the City of Tallinn prior to UUTBV's Bid 27

4) Appointment of ASTV as Tallinn's Exclusive Water Supplier and Operator of Sewerage Facility 29

5) UUTBV's Bid 29

a) Share Price 29

b) K-coefficients (Tariffs) 29

C) The Entry of UUTBV into ASTV and the Signature of the Privatisation Agreements 31

1) The Share Sale and Subscription Agreement 31

2) The Services Agreement 31

a) The Body of the Services Agreement 31

b) Schedule E of the Services Agreement 34

3) The Shareholders' Agreement 35

4) The Closing of the Share Sale and Subscription Agreement 36

D) The First Year of Operation after ASTV's Privatisation 36

E) The 2002 Amendment to the Services Agreement 36

F) The 2002 EBRD Loan 38

G) The Entry of the EBRD into UUTBV (and Indirectly ASTV) in 2003 38

H) The ASTV's IPO and the 2005 Amendments to the Services Agreement 38

I) 2005-2008: Reforms Proposals for the Water Tariff Regulation under the 1999 PWSSA 39

1) Reform Proposal of the Ministry of Environment 39

2) Reform Proposal of the State Audit Office 39

3) Reform Proposal of the Chancellor of Justice 40

4) October-November 2007: the Government Cabinet Supports the Ministry of Environment's Reform Proposal 40

5) June 2008: the First Draft Amendment to the 1999 PWSSA by the Ministry of Environment 41

J) The 2007 Amendment to the Services Agreement 42

K) The Ministry of Environment's Draft Amendment to the 1999 PWSSA 43

L) The Statements by the EOKL in 2009 43

M) End of 2008 and 2009: the ECA's Investigation and Analysis of ASTV's Tariff 44

N) The Investigation by the Chancellor of Justice 47

O) The 2009 Amendment to the Services Agreement 49

P) The Anti-Monopoly Bill (AMB) and the ECA Methodology 49

Q) The ECA Methodology 51

1) The Discussion regarding the Methodology 51

2) The Methodology Adopted by the ECA 53

R) ASTV's Tariff Application to the ECA 54

1) ASTV's 2011 Tariff Application 54

2) The ECA's Rejection of the 2011 Tariff Application, and the ECA Prescription 56

S) The Estonian Proceedings 58

T) ASTV's Complaint before the European Commission 62

V. SUMMARY OF THE PARTIES' CLAIMS AND REQUESTS FOR RELIEF 63

A) Claimants' Position 63

1) The Breach of Claimants' Legitimate Expectations Arising Out of the Privatisation 63

2) The Other Alleged FET Breaches, and Unreasonable and Discriminatory Measures 65

3) The Breach of the Umbrella Clause 66

4) The Claimants' Prayer for Relief 66

B) Respondent's Position 67

1) Respondent's Objections to Jurisdiction 67

2) Respondent Denies Having Breached any of its International Obligations 68

a) Claimants cannot Claim any Legitimate Expectations regarding Water Tariffs beyond 2005 68

b) The AMB's Regulatory Reform and the ECA's Measures Do Not Violate FET 69

c) Estonia's Conduct did not Breach its International Obligations in any other Manner 70

VI. JURISDICTION 70

A) The Jurisdiction of the Tribunal over ASTV's Claims 70

1) The Relevant Texts 71

2) The Time when Foreign Control Must Be Established 72

3) UUTBV's Control of ASTV 74

a) The Applicable Legal Standard 74

b) Meaning of Control in International Investment Law 75
c) The Relevant Facts regarding Control over ASTV 77
d) Estonian Law Expert Evidence....83
e) Analysis of the Tribunal: Control of ASTV 85
4) The Relevance of UUTBV's Corporate Structure....87
a) Positions of the Parties, and Relevant International Authorities 87
b) Relevant Facts....89
c) Analysis of the Tribunal: Relevance of the Ultimate Controller of UUTBV 92
B) The *Ratione Voluntatis* Jurisdiction of the Tribunal....93
1) The Breadth and Effect of Art. 26 of the ICSID Convention 93
2) Positions of the Parties on the Application of Art. 26 to the Facts at Hands 95
3) Analysis of the Tribunal: *Ratione Voluntatis* Jurisdiction 96
C) The Alleged incompatibility of the BIT with EU Law 97
1) Respondent's Counter-Memorial and Rejoinder....97
2) Claimants' Reply Memorial.... 100
3) The *Achmea* Judgment 101
4) Respondent's Observations on the *Achmea* Judgment 103
5) Claimants' Observations on the *Achmea* Judgment.... 104
6) The European Commission *Amicus Curiae* Submission.... 104
7) Respondent's Comments on the European Commission *Amicus Curiae*.... 107
8) Claimants' Comments on the European Commission *Amicus Curiae* 107
9) The Declaration of the Majority of EU Member States of 15 January 2019.... 109
10) Respondent's Comments on the EU Majority Declaration 111
11) Claimants Comments' on the EU Majority Declaration.... 112
12) Analysis of the Tribunal: the Tribunal's Jurisdiction and the Irrelevance of the *Achmea* Judgment 113
VII. LIABILITY.... 121
A) Claim of Breach of FET Based on Legitimate Expectations 121
1) A General Approach to FET.... 123
2) The Distinction between Contractual Commitments and Legitimate Expectations 127
3) A Necessary Balance between the Investor's Expectations and the State's Right to Regulate.... 129
4) The Claimants' Legitimate Expectations at the Time of the Privatisation.... 135
a) The Purpose and Objectives of the Privatisation 136
b) The Broader Context of ASTV's Privatisation 140
c) The Nature of the Privatisation Agreements and the Capacity in which the City of Tallinn Intervened in these Acts 143

d) The Terms of the Privatisation Agreements and the Status of the 2001 Business Plan 149

e) Conclusions of the Tribunal on Claimants' Legitimate Expectations at the time of the Privatisation 163

f) The Legality of the Services Agreement and the 2002 and 2007 Amendments... 164

5) The Impact of Post-Privatisation Events on Claimants' Legitimate Expectations........ 165

a) The Payment of Management Fees and Dividends to UUTBV, and the Restructuring of ASTV 165

b) The 2002 Amendment to the Services Agreement 167

c) The Replacement of the 2000 EBRD Loan by the 2002 EBRD Loan 167

d) The Involvement of the EBRD as an Indirect Equity Investor from 2003 to 2010. 169

e) The 2005 IPO........ 169

f) The 2007 Amendment 170

g) The 2009 Amendment and the Foregoing of a 2% K-coefficient 173

h) Conclusion regarding Claimants' Legitimate Expectations Supposedly based on Post-Privatisation Events 174

6) Claim of Breach of the FET Independently of the Existence of Legitimate Expectations 174

a) The Relevance of the Doctrine of Police Powers and of the Good Faith of Respondent 174

b) The Purpose of the AMB and its Adoption 175

c) The Basis of the 2011 Application and Its Rejection 184

d) The Legal Impact of the Entry into Force of the AMB/2010 PWSSA on the Lawfulness and Enforceability of the Tariff part of the Services Agreement 186

e) The Economic Evidence relied on by the Parties 193

B) Claims of Breaches of Due Process, Discrimination and Unreasonable Measures........ 196

1) The Alleged Breaches of Due Process 197

a) Due Process in International Investment Law........ 197

b) The Due Process Breaches pertaining to the Analysis........ 198

c) The Chancellor of Justice's Investigation 205

d) The Due Process Failure in the Development of the Methodology........ 206

e) The Due Process Failure in the Rejection of the 2011 Tariff Application........ 208

2) The Alleged Negative Publicity Campaign against Claimants 208

3) The Alleged Unreasonable and Discriminatory Measures 209

C) Claim of Breach of the Umbrella Clause........ 209

VIII. COSTS........ 210

IX. AWARD........ 213

TABLE OF SELECTED ABBREVIATIONS/DEFINED TERMS

AMB	Anti-Monopoly Bill
APA	Estonian Administrative Procedure Act
Arbitration Rules	ICSID Rules of Procedure for Arbitration Proceedings of 10 April 2006
Art.	Article or Articles
BIT or Netherlands-Estonia BIT or Treaty	Agreement on Encouragement and Reciprocal Protection of Investments between the Kingdom of The Netherlands and the Republic of Estonia which entered into force on 1 September 1993
C-[#]	Claimants' Exhibit
CJEU	Court of Justice of the European Union
Cl. Mem.	Claimants' Memorial on jurisdiction and the merits dated 18 September 2015
Cl. PHB	Claimants' Post Hearing Brief dated 22 February 2017
Cl. Reply	Claimants' Reply on jurisdiction and the merits dated 17 June 2016
CL-[#]	Claimants' Legal Authority
EBRD	European Bank for Reconstruction and Development
ECA	Estonian Competition Authority
EOKL	Estonia Homeowners' Association
EU	European Union
EVEL	Estonian Water Companies Association (Eesti Vee-Ettevõtete Liit)
FET	Fair and Equitable Treatment
Hearing	Hearing on jurisdiction and the merits held 7-11 and 14-15 November 2016
ICSID Convention	Convention on the Settlement of Investment Disputes Between States and Nationals of Other States dated 18 March 1965

ICSID or the Centre	International Centre for Settlement of Investment Disputes
IPO	Initial Public Offering
IRL	Ismaa-Res Publica coalition
IRR	Internal Rate of Return
LOA	Law of Obligations Act
MMU	Mandate Monitoring Unit
NBV	Net Book Value
NEP	Network Extension Programme
R-[#]	Respondent's Exhibit
RAB	Regulatory Asset Base
Resp. C-M	Respondent's Counter-Memorial on jurisdiction and the merits dated 5 February 2016
Resp. PHB	Respondent's Post Hearing Brief dated 22 February 2017
Resp. Rej.	Respondent's Rejoinder on jurisdiction and the merits dated 16 September 2016
RL-[#]	Respondent's Legal Authority
Services Agreement	Services Agreement between Tallinna Linn and AS Tallinna Vesi entered into on 12 January 2001
TFEU	Treaty on the Functioning of the European Union
Tr. Day [#] [Speaker(s)] [page:line]	Transcript of the Hearing
Tribunal	Arbitral tribunal constituted on 19 March 2015
VCLT	Vienna Convention on the Law of Treaties
WACC	Weighted Average Cost of Capital

I. INTRODUCTION

1. This case concerns a dispute submitted to the International Centre for Settlement of Investment Disputes ("ICSID" or the "Centre") on the basis of the *Agreement on Encouragement and Reciprocal Protection of Investments between the Kingdom of The Netherlands and the* ***Republic*** *of Estonia*, which was signed on 27 October 1992 and entered into force on 1 September 1993[1] (the "**BIT**" or "**Netherlands-Estonia BIT**" or the "**Treaty**") and the *Convention on the Settlement of Investment Disputes between States and Nationals of Other States*, which entered into force on 14 October 1966 (the "**ICSID Convention**").

2. The dispute relates to certain steps taken by various organs of Respondent allegedly in breach of the BIT, further to the privatisation of the municipal water and wastewater infrastructure and services in Tallinn, Estonia's capital.

II. PARTIES

3. Claimants are:

United Utilities (Tallinn) B.V. ("**UUTBV**"), a company incorporated under the laws of the Kingdom of The Netherlands, with its registered office at Teleportboulevard 140, 1043 EJ Amsterdam, The Netherlands;[2]

and

Aktsiaselts Tallinna Vesi ("**ASTV**"), a company incorporated under the laws of the Republic of Estonia, with its registered office at Adala 10, Tallinn 10614, Estonia. [3] UUTBV and ASTV are collectively referred to as "**Claimants**."

4. Respondent is the Republic of Estonia ("**Estonia**" or "**Respondent**"; and together with Claimants, the "**Parties**").

5. The Parties' representatives and their addresses are listed above on page (i).

III. PROCEDURAL HISTORY

6. On 15 October 2014, ICSID received a Request for arbitration dated 13 October 2016 from UUTBV and ASTV (the "**Request**" or "**RFA**"), along with Exhibits C-1 to C-46.

7. On 24 October 2014, the Secretary-General of ICSID registered the Request in accordance with Article 36(3) of the ICSID Convention and notified the Parties of the registration. In the Notice of Registration, the Secretary-General invited the Parties to proceed to constitute an arbitral tribunal as soon as possible in accordance with Rule 7(d) of ICSID's Rules of Procedure for the Institution of Conciliation and Arbitration Proceedings.

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[1] **C-1**, BIT.

[2] **C-2**, UUTBV's Articles of Incorporation; RFA, ¶8.

[3] **C-3**, ASTV's Certificate of Incorporation (29 May 1997); RFA, ¶8.

8. The Parties agreed to constitute the Tribunal in accordance with Article 37(2)(a) of the ICSID Convention as follows: the Tribunal would consist of three (3) arbitrators, one (1) to be appointed by each party and the third, presiding arbitrator to be appointed by agreement of the two (2) co-arbitrators.

9. The Tribunal is composed of Mr Stephen L. Drymer, a national of Canada, President, appointed by his co-arbitrators; Sir David A.R. Williams QC, a national of New Zealand, appointed by Claimants; and Professor Brigitte Stern, a national of France, appointed by Respondent.

10. On 19 March 2015, the Secretary-General, in accordance with Rule 6(1) of the ICSID Rules of Procedure for Arbitration Proceedings (the "**Arbitration Rules**"), notified the Parties that all three (3) arbitrators had accepted their appointments and that the Tribunal was therefore deemed to have been constituted on that date. Mr James Claxton, ICSID Legal Counsel, was designated to serve as Secretary of the Tribunal. Further to the departure of Mr James Claxton, Mr Paul-Jean Le Cannu was appointed as Secretary of the Tribunal[4] in April 2015.

11. By letter of 30 March 2015, the Tribunal through its Secretary circulated a draft Procedural Order No. 1 and a draft Agenda for the first session to the Parties for their comments, which the Centre received on 20 April 2015.

12. On 1 May 2015, Respondent filed a Request for bifurcation of the proceeding into separate jurisdiction and merits phases (the "**Request for Bifurcation**") and indicated that it intended to raise at least two (2) objections under ICSID Arbitration Rule 41(1). On the same date, Claimants filed observations, opposing the Request for Bifurcation. The Parties also filed further comments on the draft Procedural Order No. 1 and the timetable. Updated drafts of the agenda and the Procedural Order No. 1 were circulated to the Parties on 3 May 2015.

13. On 5 May 2015, the Tribunal held a first session and a hearing on the Request for Bifurcation at the International Dispute Resolution Centre in London. The Tribunal Secretary circulated the verbatim transcript of the first session to the Parties on 7 May 2015.

14. On 22 May 2015, the Tribunal through its Secretary circulated a revised draft Procedural Order No. 1 for the Parties' comments, in particular of paragraph 20.6.2. Claimants and Respondent submitted their comments on 29 May 2015 and 4 June 2015, respectively. On 5 June 2015, Claimants submitted further comments on paragraph 20.6.2 of draft Procedural Order No. 1 in response to Respondent's letter of 4 June 2015.

15. On 5 June 2015, the Tribunal issued Procedural Order No. 1 ("**PO1**") embodying the agreement of the Parties and the Tribunal's decisions on procedural matters. PO1 records the Parties' confirmation that the Tribunal was properly constituted and that no party has any objection to the appointment of any Member of the Tribunal.[5] The Order also provides, *inter alia*, that the applicable Arbitration Rules are those in effect from 10 April 2006,[6] that the

[4] Parties were advised of same by letter of 30 April 2015.

[5] PO1, ¶2.1.

[6] PO1, ¶1.1.

procedural language is English,[7] that the place of proceeding is Washington, D.C.,[8] and that hearings shall be open to the public. PO1 further provides that the procedural timetable for this arbitration will be determined in a further procedural order once the Tribunal's decision on the Request for Bifurcation has been rendered.[9]

16. By letter of 16 June 2015, the Centre informed the Parties of its intention to publish PO1 on its website by 18 June 2015, pursuant to paragraph 23.1 of PO1, which provides that "[t]he Parties consent to ICSID publication of any Procedural Orders, Decisions and Award issued in the present proceeding, subject to the redaction of confidential information." Both Parties confirmed on 18 June 2015 that they did not wish to propose any redaction to PO1.

17. On 17 June 2015, the Tribunal issued Procedural Order No. 2 ("**PO2**") denying Respondent's Request for Bifurcation and establishing the Timetable for the Arbitration (Annex A), including the date of the hearing on 7-11 and 14-15 November 2016. By letter of the same date, the Centre informed the Parties of its intention to publish PO2 on its website by 19 June 2015, subject to the potential redaction of any confidential information that a Party may propose within that time period. Respondent confirmed on 19 June 2015 that it did not wish to propose any redaction to PO2. Claimants did not submit any comments in response to the Centre's letter of 17 June 2015.

18. On 19 June 2015, the Tribunal through its Secretary issued a revised version of PO1 to include the following individuals in the list of participants in the first session:

   - Mr Kaupo Lepasepp, Mr Simon Gardiner, and Ms Riina Käi, who participated in the first session on behalf of Claimants, as requested by Claimants on 18 June 2015.

   - Ms Kristiina Rebane, who participated on behalf of Respondent.

19. On 18 September 2015, pursuant to Annex A of Procedural Order No. 2, Claimants electronically filed their Memorial (the "**Memorial**"), along with the following documents:

   - The witness statements of Robert John Gallienne dated September 2015 (unsigned), Ian John Alexander Plenderleith dated September 2015 (unsigned), Jüri Mõis, dated 15 September 2015, Vladimir Panov'i Esimene Tunnistaja Ütlus, dated 11 September 2015 (Estonian language original, together with an English translation);

   - The expert report of Andrew Meaney of Oxera Consulting LLP dated 18 September 2015;[10]

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[7] PO1, ¶11.1.

[8] PO1, ¶10.1.

[9] PO1, ¶14.1.

[10] By email of 23 September 2015, Claimants informed the Centre and the Tribunal that they had identified a minor error in Claimants' expert report and circulated an electronic copy of the corrected expert report, along with a marked-up version showing the corrections made, the following day.

- The index of Claimants' factual exhibits and legal authorities;

- Exhibits C-47 through C-265; and

- Legal authorities CL-1 through CL-17.[11]

20. By email of 9 October 2015, pursuant to paragraphs 10.2 and 20.6 of PO1 and as instructed by the Tribunal, the Centre informed the Parties of the options available to them to hold an open hearing (a livestream to an overflow room or a webcast by internet), and invited them to confirm their preferences as to these options. The Parties were also invited to confirm the hearing venue.

21. By email of 16 October 2015, Claimants confirmed their agreement that the hearing be held at the Hearing Centre of the International Chamber of Commerce (the "ICC") in Paris, and their preference for the hearing to be webcast by internet. By letter of 27 October 2015, Respondent also agreed that the hearing be held at the ICC in Paris. Like Claimants, Respondent further expressed its preference that the hearing be webcast, but proposed that the webcast not be live and be made available on the ICSID website after the hearing, lest witness sequestration be practically impossible to enforce.

22. By letter of 14 December 2015, the Tribunal through its Secretary conveyed the following message to the Parties regarding the webcasting of the hearing:

> The Tribunal notes that the parties are both agreeable to having the hearing held at the ICC Hearing Centre in Paris and webcast. They disagree however as to whether the hearing should be webcast live or once the hearing has been concluded, with the Respondent arguing that 'if the hearing were webcast live, the sequestration of witnesses would be practically impossible to enforce, or if enforced, it would result in the absurd situation that the webcast could be followed by the whole world save the witnesses who have not testified yet.'
>
> The Tribunal does not share the Respondent's reservations as to the proposed live webcast of the hearing. In the Tribunal's view, it is not unusual for a hearing to be webcast live in a case where the applicable procedural rules also require that witnesses be sequestrated. (See recently *Spence International Investments, LLC, Berkowitz et al v. the Republic of Costa Rica* (UNCT/13/2) where a live webcast was deemed to be both desirable to afford 'effective public access to the hearing' and compatible with sequestration.) The Tribunal recalls that it is each party's responsibility to ensure that sequestration is properly complied with.
>
> In view of the foregoing, it is hereby decided that the hearing in this case shall be webcast live from the ICC Hearing Centre in Paris. [Footnote omitted]

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[11] By letter of 7 December 2015, Claimants informed the Centre and the Tribunal that they were producing (i) fuller or corrected versions of certain exhibits and (ii) additional Estonian and Dutch language versions of certain exhibits submitted in English only in September 2015.

23. By letter of 18 December 2015, Counsel for Claimants notified the Centre and the Tribunal that Mr Matthew Weiniger QC was made a partner at Linklaters LLP as of 19 October 2015 and would continue to represent Claimants in these proceedings.

24. On 18 January 2016, Claimants informed the Tribunal that they were producing (i) additional fuller versions of certain exhibits and (ii) additional Estonian and English language versions of certain exhibits where only the English translation or the Estonian original had originally been produced by Claimants. On the same date, the above-described additional documents filed by Claimants on 7 December 2015 and 18 January 2016 were sent to the Tribunal.

25. On 27 January 2016, Estonia filed an Application for an immediate procedural order prohibiting publication of any arbitration materials (the "**Application for an Immediate Procedural Order**" or "**Application**"), along with exhibits R-1 to R-12 and legal authorities RL-1 to RL-3, which the Centre also received in hard copy.[12] Respondent also indicated that it would file a proper request for provisional measures, which it proposed to do by 26 February 2016.

26. By letter of 28 January 2016, the Tribunal informed the Parties of its intention to decide on Respondent's Application for an Immediate Procedural Order on 29 January 2016 and invited Claimants to provide their response by the same date. The Tribunal expressed its understanding and expectation that Claimants would refrain from all further publication or dissemination of materials related to the arbitration until such time as the Tribunal determined the questions raised by Respondent's Application.

27. On 29 January 2016, Claimants submitted their response and proposed to delay the publication of an extract of their Memorial on the condition that the Parties agree on certain terms pending the Tribunal's consideration of Respondent's Application and forthcoming request for provisional measures.

28. After the Tribunal had invited the Parties to communicate directly with each other regarding Claimants' proposal, Respondent informed the Tribunal on 30 January 2016 that the Parties had reached the following agreement, pending the Tribunal's consideration of Respondent's forthcoming request for provisional measures:

> 1. Neither Party shall publish the Memorial, the Counter-Memorial, any witness statement, or any expert report that have been or will be filed in this arbitration, or any summary, excerpt or extract thereof.
>
> 2. Each Party may publish a stock exchange announcement or press release, or make public statements regarding the filing of the Memorial or the Counter-Memorial and the general position that Claimants claim violations of the Treaty and Estonia denies Claimants' claims in full. Such communications shall not discuss the specific content of the Memorial or the Counter-Memorial or the witness statements and expert reports attached thereto, or identify the witnesses and experts. The Parties reserve the right to revisit this agreement with each other and with the Tribunal in the event of material media coverage which goes beyond the fact of the filing of the

[12] See ICSID's letter dated 9 February 2016.

Memorial and Counter-Memorial and that Claimants claim violations of the Treaty and Estonia denies Claimants' claims in full, and which either Party considers it should respond to.

29. On 9 February 2016, Respondent electronically filed its Counter-Memorial dated 5 February 2016, along with the following documents:

- The first witness statements of Mr Indrek Teder (in Estonian and English), Ms Karin Kroon, Mr Ken-Marti Vaher, Mr Märt Ots, and Mr Martin Põder;
- The expert reports of Dr Richard Hern, Mr Hannes Vallikivi, and Mr Märt Rask (in Estonian and English);
- The lists of Respondent's exhibits and legal authorities;
- Exhibits R-13 through R-212; and
- Legal authorities RL-4 through RL-167.

30. By email of 12 February 2016, Respondent submitted the corrected version of its Counter-Memorial, of the report of Dr Richard Hern and of its lists of exhibits and of legal authorities.

31. On 26 February 2016, Respondent filed an Application for Provisional Measures (the "**Application for Provisional Measures**"), along with exhibits R-213 to R-216 and legal authorities RL-168 to RL-175.

32. On 4 March 2016, the Parties exchanged requests for document production ("**Document Requests**") in accordance with paragraph 15 of PO1 (as amended) dated 19 June 2015 and the Timetable at Annex A of PO2.

33. By letter of 16 March 2016 and email of 17 March 2016, the Parties informed the Tribunal of their proposed calendar for the resolution of Estonia's Application for Provisional Measures, which was accepted by the Tribunal on the next day. It provided as follows:

1. Claimants shall file their Response to the Application by 18 March 2016 (the "**Response on PM**");
2. By 22 March 2016, Estonia shall notify Claimants and the Tribunal whether it wishes to file a reply to the Response (the "**Reply on PM**");
3. If Estonia opts to file a Reply, that Reply is to be filed by 1 April 2016, with Claimants' Rejoinder to that Reply, if any, to be filed by 15 April 2016;
4. The Tribunal shall resolve the Application without an oral hearing.

34. On 18 March 2016, Claimants filed their Response on PM to Estonia's Application for Provisional Measures, along with exhibits C-266 through C-269.

35. After advising the Tribunal of its intention of filing a reply on 22 March 2016, Respondent filed its Reply on PM on 1 April 2016, along with exhibits R-218 to R-224 and legal authorities R-177 and R-178.

36. On 1 April 2016, the Parties exchanged responses and/or objections to the other party's Document Requests.

37. On 15 April 2016, the Parties filed their replies to the other Party's objections to their respective Document Requests, accompanied by Redfern Schedules setting out the Parties' positions in respect of the Requests on which rulings are sought.

38. On the same day, Claimants filed a Rejoinder to Estonia's Application for Provisional Measures, together with exhibits C-270 through C-272, and legal authorities CL-26 through CL-27.[13]

39. By letter of 22 April 2016, Claimants filed comments on Respondent's Reply to Claimants' Objections to Respondent's Request for the Production of Documents. Upon the Tribunal's invitation, Respondent filed comments on 28 April 2016 in response to Claimants' letter of 22 April 2016.

40. On 3 May 2016, the Tribunal issued Procedural Order No. 3 ("**PO3**"), which recorded its Decision on the Parties' Requests for Document Production, along with Annex A (Claimants' Document Requests) and Annex B (Respondent's Document Requests). On the same date, the Centre informed the Parties of its intention to publish PO3 on its website by 5 May 2016, subject to the potential redaction of any confidential information that a Party may propose by that date. By letter of 4 May 2016, Respondent proposed that PO3 be published without its Annexes or, alternatively, that specific references to the Parties' submissions, the witness statements and expert reports, and the names of witnesses and experts be redacted from Annexes A and B. By letter of 5 May 2016, Claimants informed the Tribunal that in their view no redactions were necessary and proposed that PO3 be published immediately but that the issue of publication of the Annexes be deferred until the Tribunal's decision on Respondent's objections to publication.

41. By letter of 9 May 2016, the Tribunal through its Secretary informed the Parties that it had asked ICSID to publish PO3 without its Annexes and invited them to submit their comments on the publication of the Annexes once the Tribunal's Decision on Respondent's Application for Provisional Measures had been rendered.

42. On 12 May 2016, the Tribunal issued a Decision on Respondent's Application for Provisional Measures (the "**Decision on Provisional Measures**"). The Tribunal decided as follows:

> (1) Respondent's Application for Provisional Measures is granted in part.
>
> (2) No party is prevented from engaging in general discussion about the case in public, which discussion is not limited to

[13] The Tribunal notes that legal authority CL-27 was in support of Claimants' Reply to Respondent's Objections to Claimants' Requests to Produce Documents dated 15 April 2016.

updates on the status of the case, and may include wider aspects of the case such as a summary of the parties' positions, provided that such public discussion is not used as an instrument to antagonise any party, exacerbate the parties' differences, aggravate the dispute, disrupt the proceedings or unduly pressure any party.

(3) Such public discussion does not include publication of the 'Arbitration Documents,' i.e., the documents filed in this arbitration, such as the parties' written submissions, witness statements, expert reports and documents produced within the framework of document production, or any excerpt or extract thereof.

(4) Any request not granted herein is denied.

43. On the same day, the Centre advised the Parties of its intention to publish the Decision on Provisional Measures on its website by 16 May 2016, subject to the potential redaction of any confidential information that a Party may propose by that date. The Parties were also invited to submit any further comments they may have had on the publication of Annexes A and B to PO3 by 19 May 2016.

44. By letter of 16 May 2016, Claimants informed the Tribunal that in their view no redactions were necessary either to the Decision or to Annexes A and B to PO3. By letter of 19 May 2016, Respondent confirmed its position stated in its letter of 4 May 2016 regarding the publishing of PO3. Claimants commented on Respondent's letter of 19 May 2016 by a letter of 26 May 2016. By email of same day, the Tribunal informed the Parties that it would issue a ruling on the question of the publication of Annexes A and B to PO3 as soon as possible.

45. By letter of 8 June 2016, Claimants requested, with Respondent's consent, a one-week extension until 17 June 2016 to submit their Reply Memorial (the "**Reply**"). Claimants also submitted the Parties' proposed joint amendments to the Procedural Timetable set out in Annex A to PO2. By email of the same date, Respondent confirmed its consent to Claimants' request, which the Tribunal granted also on the same date. A new version of Annex A to PO2 was circulated, reflecting the following agreed amendments:

- Claimants to file their Reply Memorial on 17 June 2016;
- Estonia to file its Rejoinder Memorial on 16 September 2016; and
- Witness notification to take place on 21 September 2016, with the other dates in the timetable remaining unchanged.

46. By letter of 9 June 2016, the Tribunal issued the following ruling on the publication of Annexes A and B to PO3:

> The Tribunal has considered the parties' positions regarding publication of Annexes A and B of Procedural Order No. 3, including their respective proposals regarding redactions. It has considered those positions and proposals in the light of both its recent Decision on Respondent's Application for Provisional Measures ('Decision') and

the parties' consent, as recorded at §23.1 of Procedural Order No. 1 dated 19 June 2015, to ICSID publication of any Procedural Orders, Decisions, and Award issued in this arbitration 'subject to the redaction of confidential information'.

The Tribunal does not consider it appropriate or correct to prohibit publication of Annexes A and B in their entirety. Nor does it consider it appropriate or correct to allow publication of those Annexes in their entirety.

The Tribunal is of the view that the redactions proposed by Respondent go far beyond what is required under the principles set out in the Decision, which are intended to allow for substantive, though not unrestricted, publication of information concerning the arbitration. Moreover, the Tribunal does not consider it reasonable or proportionate to embark upon a redaction-by-redaction process of analysis and determination of each of the innumerable redactions proposed by Respondent. The Tribunal prefers the approach proposed by Claimants, which it considers principled, reasonable, fair and efficient.

Accordingly, as instructed by the Tribunal, ICSID shall shortly publish Annexes A and B with the following information redacted: (i) direct quotations from the parties' submissions, witness statements and expert reports, and exhibits; and (ii) the names of witnesses and experts, as well as third parties other than those which (or who) plainly exercise public functions, such as Estonian Ministries and Ministers, the Estonian Parliament and its members, the Estonian Competition Authority, the State Audit Office, the Legal Chancellor, the City of Tallinn, the European Bank for Reconstruction and Development, and the European Commission.

47. On 17 June 2016, pursuant to the amended Procedural Timetable recorded in Annex A to PO2, Claimants electronically filed their Reply Memorial, along with the following documents:

- The unsigned second witness statement of Robert John Gallienne dated June 2016;
- The second witness statement of Ian John Alexander Plenderleith dated 16 June 2016;
- The first witness statement of Dennis van Rooijen dated 17 June 2016;
- The second expert report of Andrew Meaney dated 17 June 2016;
- The expert opinion of Toomas Pikamäe dated 17 June 2016 (original Estonian version and English translation);
- An index of the factual exhibits to Claimants' Reply Memorial;
- An index of the legal exhibits to Claimants' Reply Memorial;
- Exhibits C-273 through C-411; and

- Legal authorities CL-28 through CL-118.

48. By email of 18 July 2016, the President of the Tribunal wrote to the Parties to propose that Ms Laurence Ste-Marie be engaged as assistant to the Tribunal (the "**Assistant**") and invited the Parties to provide their views on the proposed appointment. Further to the Parties' comments and consent to the appointment of 26 and 28 July and the circulation of draft terms of appointment on 29 July and Claimants' comments thereon of 3 August, the Tribunal circulated the Terms of Appointment for signature by the Parties, Tribunal and Ms Ste-Marie.

49. On 16 September 2016, Respondent filed its Rejoinder Memorial, along with the following documents:

    - The second expert reports of Dr Richard Hern, dated 16 September 2016, Mr Hannes Vallikivi dated 13 September 2016 (in Estonian and English), and Mr Märt Rask dated 15 September 2016 (in Estonian and English);

    - The first witness statement of Mr Falko Sellner dated 16 September 2016;

    - The second witness statements of Mr Ken-Marti Vaher dated 16 September 2016, Mr Märt Ots dated 14 September 2016, and Mr Martin Põder dated 13 September 2016;

    - The lists of Respondent's exhibits and legal authorities;

    - Exhibits R-228 through R-331; and

    - Legal authorities RL-187 through RL-247.[14]

50. By letters of 21 September 2016, each Party notified the Tribunal of the list of fact and expert witnesses that it wished to cross-examine at the hearing.

51. On 29 September 2016, the Tribunal held a pre-hearing telephone conference with the Parties.

52. By letter of 6 October 2016, Claimants filed a request for leave to file nineteen (19) additional exhibits (the "**Proposed Exhibits**") to the documents accompanying their Reply Memorial dated 17 June 2016 (the "**First Request**").

53. Upon the Tribunal's invitation, Respondent filed on 10 October 2016 observations on the First Request, asking the Tribunal that it be rejected.

54. By letter of 14 October 2016, Claimants filed comments on Respondent's observations on the First Request.

55. By email of 21 October 2016, Claimants submitted a further request for leave to file one additional exhibit (the "**Second Request**").

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[14] By email of 21 September 2016, Respondent submitted a corrected version of its Rejoinder Memorial dated 16 September 2016, along with a redline comparing the version of 16 September to the corrected version of 21 September, and a corrected list of legal authorities.

56. By letter of the same day, Respondent wrote to the Tribunal regarding the examination of three (3) of its witnesses. Respondent indicated that Mr Sellner could only testify by video conference on 10 November, that Mr Ots had reconsidered his decision to testify in English, and Mr Teder would not be able to attend the hearing due to a medical condition. The Tribunal invited Claimants' comments by email of the same day.

57. By letter of 23 October 2016, the Tribunal granted Claimants' First Request and asked the Parties "to discuss and, it is to be hoped, agree on 'reasonable and practical measures' intended to allow Estonia to 'address Claimants' arguments based on the Proposed Exhibits,' […] and to revert to the Tribunal in this regard by no later than Wednesday, 26 October 2016." The Tribunal also invited Respondent to submit its comments on the Second Request.

58. By letter of 24 October 2016, Claimants submitted their comments on the examination of Messrs Sellner, Ots, and Teder. Although Claimants had no substantive comment on the position regarding Messrs. Ots and Sellner, they requested that the Tribunal take into account the lack of opportunity to cross-examine Mr Teder in deciding the weight to be afforded to his evidence. They also reserved the right to address the reliability of his witness statement in their later submissions.

59. By email of 24 October 2016, the Parties requested a one-day extension until 25 October 2016 to submit the (i) Chronology, (ii) Dramatis Personae, (iii) List of Issues, and (iv) Skeleton Arguments, which they were to submit pursuant to Annex A of PO2. By email of 25 October 2016, the Tribunal granted the Parties an extension until 25 October 2016 to file their Skeleton Arguments and until 6:00 pm GMT on 27 October 2016 to file the other documents. On 25 October 2016, the Parties submitted their Skeleton Arguments.

60. By letter of 25 October 2016, further to the Parties' exchanges regarding the examination of Messrs Sellner, Ots, and Teder, the Tribunal asked the Parties to submit an updated hearing schedule. On 28 October 2016, Respondent submitted a medical certificate attesting to Mr Teder's health condition.

61. By letter of 26 October 2016, Respondent confirmed that it did not object to Claimants' Second Request of 21 October 2016 on the condition that the additional document introduced into the record be treated confidentially and that appropriate measures be put into place for that purpose at the hearing.

62. On 27 October 2016, the Parties submitted their agreed Chronology and Dramatis Personae, and their respective Lists of Issues.

63. Further to the Parties' request conveyed by Respondent in the above-referred letter of 26 October, the Tribunal granted the Parties until 28 October 2016 to pursue an agreement on the "reasonable and practical measures" intended to allow Respondent to address Claimants' arguments based on the Proposed Exhibits. The Tribunal also acknowledged Estonia's consent to the filing of the document referred to in Claimants' request of 21 October 2016. As regards Estonia's concern to ensure that the document to which it refers is not improperly disclosed to the public *via* the planned web broadcast of the hearing, Tribunal informed the Parties that it had liaised with the Secretariat in that respect and that they had identified a means of ensuring that any off-the-record discussions or other necessarily confidential

information was not inadvertently webcast. It asked the Parties to notify it immediately of any further or specific protocol required as well as to raise the issue with the other Party directly.

64. By letter of 28 October 2016, Claimants asked the Tribunal to make an order that the Parties' experts be permitted to make a presentation of up to twenty (20) minutes at the start of their examination, including using PowerPoint presentations. Claimants also requested that the Tribunal make an order that the "reasonable and practical measures" referred to by the Tribunal take the form of Claimants' proposal, namely that they provide Respondent with "a list of topics/issues by reference to which Claimants currently expect to rely on the Additional Exhibits," rather than "a list of references to the specific propositions allegedly supported by specific parts of the [Additional Exhibits]" [alterations from the original] as proposed by Respondent, whom the Tribunal invited to respond to Claimants' requests by 31 October.

65. By separate letter of the same date, Claimants advised the Tribunal that it intended to examine during direct examination their witness, Mr Dennis van Rooijen, on matters that had arisen after his witness statement was signed.

66. By letter of 31 October 2016, Respondent indicated that it preferred not to have experts' presentations at the hearing, and requested that the Tribunal order Claimants to provide "a list of references to the specific propositions allegedly supported by specific parts of the Additional Exhibits […], with the understanding that the propositions and references to the relevant parts of the Additional Exhibits should be as precise as if Claimants had cited and/or quoted the Additional Exhibits in their Reply Memorial."

67. By letter of 1 November 2016, the Tribunal informed the Parties that they were free to choose to have their experts make presentations by way of direct examination, including with demonstrative visual aids if desired, of no longer than twenty (20) minutes, with the time so used to be counted against the Party in question. As to the Additional Exhibits, the Tribunal further informed the Parties of its decision that Claimants' proposal, *i.e.* the production of a list of topics/issues by reference to which Claimants expect to rely on the Additional Exhibits, was the more reasonable and practical in the circumstances.

68. On 2 November 2016, further to the Tribunal's request of 25 October, the Parties submitted an amended draft hearing schedule.

69. On 3 November 2016, Claimants submitted a list of topics/issues to which Claimants' Additional Exhibits relate.

70. On 6 November 2016, the Parties exchanged by email the demonstratives which they intended to use in their opening submissions at the hearing.

71. A hearing on jurisdiction and the merits was held at the ICC in Paris, on 7-11 and 14-15 November 2016 (the "**Hearing**"). The following persons were present at the Hearing:[15]

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[15] The final list of representatives and individuals who participated in the hearing was sent to the Parties by ICSID on 23 November 2016.

Tribunal:

Mr Stephen L. Drymer	President
Professor Brigitte Stern	Arbitrator
Sir David A. R. Williams QC	Arbitrator

ICSID Secretariat:

Mr Paul Jean Le Cannu	Secretary of the Tribunal

Assistant to the Tribunal:
Ms Laurence Ste-Marie

For Claimants:

Mr Matthew Weiniger QC	Linklaters LLP
Mr Iain Maxwell	Herbert Smith Freehills LLP
Ms Louise Barber	Herbert Smith Freehills LLP
Mr Maximilian Szymanski	Herbert Smith Freehills LLP
Ms Elizabeth Reeves	Herbert Smith Freehills LLP
Ms Joanna Barry	Herbert Smith Freehills LLP
Mr Kaupo Lepasepp	Sorainen
Ms Piibe Lehtsaar	Sorainen
Mr Simon Gardiner	Aktsiaselts Tallinna Vesi / United Utilities (Tallinn) B.V. / United Utilities Group PLC
Mr Karl Brookes	Aktsiaselts Tallinna Vesi / United Utilities (Tallinn) B.V. / United Utilities Water PLC
Ms Riina Käi	Aktsiaselts Tallinna Vesi

For Respondent:

Mr Rostislav Pekař	Squire Patton Boggs
Mr Luka S. Misetic	Squire Patton Boggs
Dr Eveli Lume	Squire Patton Boggs
Ms Ariane Sproedt	Squire Patton Boggs
Mr Matej Pustay	Squire Patton Boggs
Mr Anton Sigal	Primus
Mr Chirag Mody	Primus
Ms Kristiina Rebane	Ministry of Justice of the Republic of Estonia

Court Reporter:
Ms Claire Hill

Interpreters:
MsTiiu Soomer
Ms Karin Kreedo-Massa

72. During the hearing, the following persons were examined:

On behalf of Claimants:
Witnesses:

Mr Robert Gallienne	National Joint Utilities Group
Mr Jüri Mõis	JMB Investeeringute OÜ
Mr Vladimir Panov	Former Deputy Mayor of Tallinn
Mr Ian Plenderleith	Dee Valley Water Group

Mr Dennis van Rooijen	Orangefield Group
Mr Lars Van Marrelo (attending with Mr Dennis van Rooijen)	
Experts:	
Mr Andrew Meaney	Oxera
Mr Takuma Habu (attending with Mr Meany)	Oxera
Ms Sahar Shamsi (attending with Mr Meany)	Oxera
Mr Toomas Pikamäe	Eversheds Ots &Co

On behalf of Respondent:

Witnesses:	
Mr Märt Ots	Competition Authority, Republic of Estonia
Mr Martin Põder	World Bank
Mr Ken-Marti Vaher	Parliament, Republic of Estonia
Ms Karin Kroon	Ministry of Environment, Republic of Estonia
Mr Falko Sellner	Advisory business (by video from Pristina, Kosovo)
Experts:	
Mr Hannes Vallikivi	Law firm Derling
Mr Märt Rask	Law firm Rask
Dr Richard Hern	Nera Consulting
Ms Clara Segurola (attending with Dr Hern)	Nera Consulting
Ms Zuzana Janeckova (attending with Dr Hern)	Nera Consulting

73. On 10 November 2016, the Centre received an email from Mr Helis Evart of Glimstedt, who indicated that he represented the Estonian Competition Authority (the "**ECA**"), asking for permission to record the hearing from the live webcast. On 11 November 2016, this email was forwarded to the Parties and the Tribunal. Counsel for Respondent informed the Tribunal that it would liaise with Glimstedt as requested by the Tribunal.

74. On the last day of the hearing, 15 November 2016, the Parties informed the Tribunal of their agreement to file one (1) round of post-hearing briefs on 31 January 2017, with a possibility to seek permission to apply for a rebuttal on new points. There being no agreement between the Parties as to the number of pages, the issue was left to be decided by the Tribunal. The Tribunal also asked the Parties to state their views on the fate of the webcast, as to which they disagreed, with Claimants arguing that the video recording of the hearing should remain on the ICSID website and Respondent contending that the video recording may be used by the Parties as they see fit, including for publication on their own website, but opposing publication on the ICSID website.

75. On 22 December 2016, the Centre advised the Parties that the audio recording of the hearing had been uploaded to BOX. Pursuant to paragraph 21.4 of PO1, the Parties were invited to inform the Tribunal of any agreed corrections to the hearing transcripts by 5 January 2017, which was later postponed to 13 January 2017 at the request of the Parties.

76. On 23 December 2016, having considered the Parties' views on the fate of the webcast and the length of post-hearing briefs, the Tribunal informed the Parties of its decisions (i) not to

overrule Respondent's objection to posting the recording on the ICSID website, especially where transparency can be achieved by publication on ASTV's website, and (ii) to limit the length of post-hearing briefs to a hundred (100) pages. The Tribunal further advised the Parties that it had not ruled out the possibility of asking the Parties to address certain specific issues in their post-hearing briefs, it being understood that the Parties could if necessary apply for an extension of the filing deadline to address these issues.

77. On 13 January 2017, Claimants submitted the Parties' agreed corrections to the hearing transcript, which Ms Claire Hill, the court reporter, incorporated in a revised version of the transcript. The revised hearing transcript was circulated to the Parties on 27 February 2017.

78. By letter of 24 January 2017, the Tribunal through its Secretary circulated its list of topics and questions for the Parties to address in their post-hearing briefs. The Tribunal also invited the Parties to confer with each other with a view, if necessary, to proposing an appropriate extension of the deadline for the filing of the Parties' post-hearing briefs.

79. On 27 January 2017, Claimants informed the Tribunal on behalf of the Parties that on 26 January 2017, the Tallinn Circuit Court issued a decision in the Estonian proceedings, which the Parties wished to put on record and comment on in their post-hearing briefs. In addition, in order to allow the Parties to respond to the Tribunal's questions and to address the new decision of the Tallinn Circuit Court, the Parties proposed, by agreement, that the deadline for the exchange of post-hearing briefs be extended to 22 February 2017, and the page limit for those post hearing briefs be increased to one hundred twenty-five (125) pages.

80. On the same date, the Tribunal informed the Parties that it accepted their proposals.

81. By emails of 22 February 2017, the Parties simultaneously filed their post-hearing briefs, with Claimants also filing an updated estimate of damages from Mr Meaney of Oxera, dated 21 February 2017, a copy of exhibit C-432, and Claimants' index of legal exhibits to their post-hearing brief. On 1 March 2017, Claimants commented on a calculation error which they saw in Respondent's post-hearing brief.

82. The Parties filed their submissions on costs on 12 May 2017 and their reply submissions on same on 26 May 2017.

83. On 20 December 2017, Claimants provided to the Tribunal an update on the status of the Estonian proceedings between ASTV and the ECA by submitting a copy of the Estonian Supreme Court decision issued on 12 December 2017 (the "**Supreme Court Decision**"), an English translation of this decision as well as submissions on the impact of the decision on the current arbitration.

84. On 22 December 2017, the Tribunal invited Respondent to comment on the Estonian Supreme Court Decision by 5 January 2018. That same day, Respondent requested an extension until

12 January 2018 to file its remarks as well as leave to file its own translation of the decision, both of which were granted by the Tribunal.[16]

85. Respondent filed its remarks and its own translation of the Supreme Court Decision on 12 January 2018. On 19 January 2018, Claimants asked to file a reply, and did so on 26 January 2018 after obtaining the Tribunal's authorisation. With permission of the Tribunal, on 9 February 2018 Respondent filed a rejoinder. On 13 February 2018, Claimants expressed certain disagreements with Estonia's submissions but refrained from seeking another opportunity to comment on the Supreme Court Decision.

86. On 13 March 2018, Respondent sought leave to file (i) a copy of the judgment rendered by the Grand Chamber of the Court of Justice of the European Union (the "**CJEU**") in Case C-284/16 (*Slovak Republic v Achmea BV*; the "***Achmea* Judgment**" and the "***Achmea* Case**")[17] that addresses the compatibility of investor-state arbitration clauses in intra-EU bilateral investment treaties, and (ii) observations on the *Achmea* Judgment. Claimants consented to Respondent's requests, provided that they would also have an opportunity to comment, and the Tribunal consequently invited the Parties to file simultaneous ten-page submissions on 26 March 2018.

87. On 25 March 2018, Claimants sought leave of the Tribunal to submit a document request to Respondent, consisting of the written observations that Estonia had filed in the *Achmea* Case. Further to the Tribunal's invitation, Respondent provided its comment on this request on 27 March 2018. The next day, the Tribunal informed the Parties of its rejection of Claimants' request. As directed by the Tribunal, the Parties filed their respective submission on the *Achmea* Judgment on 29 March 2018, together with legal authorities CL-123 through CL-133 and legal authorities RL-250 through RL-261, respectively.

88. On 22 August 2018, the European Commission filed an Application for Leave to Intervene as a Non-Disputing Party, along with annexes 1 and 2 (the "**European Commission's Application**").

89. On 24 August 2018, the Tribunal invited the Parties to comment on the European Commission's Application of 22 August 2018 by 31 August 2018.

90. On 31 August 2018, as per the Tribunal's instructions, the Parties filed their respective comments on the European Commission's Application.

91. On 2 October 2018, the Tribunal issued its Decision on the Application for Leave to Intervene as a Non-Disputing Party Submitted by the European Commission. The Tribunal decided as follows:

> (1) The Commission's Application is granted in part;

[16] Art. 16.3 of PO1 provides that no party shall be permitted to file an additional document after the filing of its respective written submission, save in exceptional circumstances, and that, where a party seek leave to file such document, it must not annex such document to its request.

[17] **RL-251**, CJEU, Case C-284/16, *Slovak Republic v. Achmea B.V.* [2018] ECLI:EU:C:2018:158 [*Achmea* Judgment].

> (2) The Commission is granted leave to participate in the present arbitration as a non-disputing party to the extent and in the manner set out below;
>
> (3) The Commission is invited to submit a single, written amicus curiae submission of not more than 15 pages on the legal question specified at para. 12 of its Application, by no later than 10 days from the date of dispatch of the present Decision to the Commission*;*
>
> (4) The parties (Claimants on the one hand, Respondent on the other) may each file comments of not more than 15 pages to the Commission's submission, should they wish to do so, within 14 days of the date of transmission to them of the Commission's submission;
>
> (5) The Commission's request for access to the documents filed in the case is rejected;
>
> (6) The Commission's request for attend any further hearing in the case is rejected, as no such hearing is either scheduled or foreseen.

92. By letter of the same date, the Centre informed the Parties of its intention to publish the Decision on its website by 4 October 2018, subject to the potential redaction of any confidential information that a Party may propose by that date. No comments were received from the Parties.

93. On 18 October 2018, the European Commission filed an *Amicus Curiae*, along with annexes EC 1 through EC 20 (the "**Amicus Brief**").

94. On 19 October 2018, Respondent wrote to the Tribunal requesting that the award in the case of *UP and C.D Holding Internationale v. Hungary* (ICSID Case No. ARB/13/35) rendered on 9 October 2018, referred to in the European Commission's Amicus Brief, be produced by the Commission. On 22 October 2018, Respondent withdrew its request.

95. On 1 November 2018, Claimants filed their Comments on the European Commission's Amicus Brief, along with legal authorities CL-134 through CL-140. On the same date, Respondent submitted its comments on the European Commission's Amicus Brief, together with legal authorities RL-262 through RL-275.

96. On 21 November 2018, Respondent sought leave to file a copy of the German Federal Court of Justice's decision in the *Achmea* Case following the judgement of the CJEU in this case and, on 23 November 2018, the Tribunal invited the Claimants to provide their comments on same. After Claimants did on 27 November 2018, the Tribunal dismissed the Respondent's request on 14 December 2018.

97. By letter of 21 December 2018, Claimants requested that the Tribunal issue "its decision in this arbitration without delay, with its reason to follow thereafter when the Award is issued."

98. On 24 December 2018, Respondent submitted preliminary comments on Claimants' request of 21 December 2018 and requested an extension until 4 January 2019 to comment on the request, which was granted by the Tribunal on 2 January 2019.

99. On 4 January 2019, Respondent filed its supplemented response to Claimants' request of 21 December 2019.

100. By email of 8 January 2019, Claimants requested the opportunity to provide a brief reply to Respondent's letter of 4 January 2019. That same day, the Tribunal granted Claimants' request and, on 11 January 2019, Claimants submitted said reply.

101. By email of 14 January 2019, Respondent requested leave to comment on Claimants' reply of 11 January 2019. On 15 January 2019, the Tribunal granted Respondent's request and invited Respondent to file a brief comment solely on the issue whether Claimants may request that the Tribunal "issue its decision in this arbitration without further delay, with its reasons to follow in its Award" by 18 January 2019.

102. By letter of 17 January 2019, Respondent (i) informed the Tribunal that "the Representatives of the Governments of Estonia and the Netherlands [had] signed a declaration of the majority of the Member States of the European Union dated 15 January 2019 […] on the legal consequences of the judgement of the Court of Justice of the European Union […] in the proceedings Slovak Republic v. Achmea BV […] and on investment protection in the European Union [(the "**EU Majority Declaration**")]"; and (ii) sought leave to file a copy of the Declaration along with an explanation of its importance and implications for this arbitration.

103. By letter of 18 January 2019, Respondent filed its comments on Claimants' request of 11 January 2019 regarding the issuance of the Award.

104. By letter of 29 January 2019, the Tribunal through its Secretary informed the Parties that it rejected Claimants' request of 21 December 2018, "noting Respondent's 18 January 2019 statement that the Estonian Competition Authority (ECA) is prepared to extend the time limit for ASTV to file its submissions in the regulatory proceedings in question so as to allow the Tribunal to issue its final award."

105. By letter of the same date, Respondent informed the Tribunal as follows:

> Estonia is no longer in a position to guarantee that an extension is granted if ASTV re-applies for one. Thus, Estonia withdr[ew] the penultimate paragraph of its letter of 18 January 2019 to the Tribunal and respectfully request[ed] that the Tribunal reject Claimants' application on the other grounds explained in Estonia's communications of 24 December 2018, 4 January 2019 and 18 January 2019.

106. Estonia further explained in its letter that it was planning and that it planned to inform the Tribunal of the ECA's decision on that day.

107. By letter of 30 January 2019, the Tribunal (i) asked Claimants to file by 1 February 2019 any observations that they wished to make with regard to the Respondent's request to file the EU Majority Declaration; and (ii) invited both Parties

> to inform the Tribunal whether, if the Tribunal were minded to allow the Declaration to be admitted in the record (after receiving the Claimants' observations), they would agree to dispense with the submission of

> observations on the Declaration itself, taking into consideration that the document is both clear and speaks for itself, and that the question of the legal consequences of the Achmea Judgement and its impact on this arbitration and final award have been, as noted by the Respondent, "extensively argued in [the parties'] prior submissions."

108. By letter of the same date, Claimants informed the Tribunal that they did not wish to pursue their request of 21 December 2018 at that time. Claimants, however, reserved the right "to revive their Request in future."

109. By letter of 31 January 2019, Claimants agreed to Respondent filing a copy of the EU Majority Declaration and to dispense with the submission of observations on the EU Majority Declaration provided that Estonia also agreed to this proposal.

110. By letter of the same date, Claimants informed the Tribunal that the ECA "ha[d] granted ASTV's extension request, thereby extend[ing] the deadline for ASTV to respond in the ongoing regulatory proceedings with the ECA to 1 April 2019."

111. By letter of 31 January 2019, the Tribunal, through its Secretary, confirmed receipt of Claimants' letter of 30 January 2019 and noted that Claimants did not at that stage pursue their request of 21 December 2018.

112. By letter of 1 February 2019, Respondent maintained its 17 January 2019 request that "the Parties be permitted to submit short comments on the EU Majority Declaration and its significance for the Tribunal's decision on Estonia's intra-EU objection."

113. On 2 February 2019, the Tribunal granted Respondent's request of 17 January 2019 and invited the Parties to submit their observations on the Declaration by 8 February 2019.

114. On 8 February 2019, Respondent filed a copy of the EU Majority Declaration (RL-276), along with its comments thereon. That same day, Claimants submitted their comments on the EU Majority Declaration, together with exhibits C-433 through C-435.

115. On 11 February 2019, Claimants filed their observations on Respondent's comments of 8 February 2019, stating that "Estonia used the opportunity of its comment to also make submissions on matters going beyond the Majority Declaration." Claimants further indicated that it did not seek leave to file the authorities referred to in its letter or to comment on them unless the Tribunal so desired.

116. By email of 15 February 2019, the Tribunal through its Secretary informed the Parties that it had taken note of the points made and the matters referred to in Claimants' letter of 11 February 2019.

117. By letter of 4 March 2019, Claimants requested that the Tribunal provide an update as to whether it expected to render its award by the end of March 2019.

118. By letter of 15 March 2019, the Tribunal through its Secretary informed the Parties that it would render its award by 3 May 2019.

119. By letter of 30 April 2019, the Tribunal, through its Secretary, further informed the Parties that due to unexpected scheduling conflicts among Tribunal members, the Tribunal's award could not be fully finalized and circulated to the parties until June. By letter of 30 May 2019, the Parties were advised that the Award would be rendered by Friday 21 June 2019.

120. By letter of 8 May 2019, Respondent sought leave to file a copy of Opinion No. 1/17 of the CJEU, along with an explanation of its importance for this arbitration and its implications for the Tribunal's decision in this matter. By letter of 10 May 2019, Claimants submitted comments on the Respondent's request and asked the Tribunal to reject it.

121. By letter of 15 May 2019, the Tribunal, through its Secretary, informed the Parties of its decision to reject the request, there being no compelling reason to enter into the record what Respondent referred to as "further" reasoning and comments of the CJEU on matters that have already been extensively briefed by the parties.

122. The proceeding was closed on 20 June 2019.

IV. FACTUAL BACKGROUND

A) THE CREATION OF ASTV AND ITS OPERATION PRIOR TO THE PRIVATISATION

123. Tallinn Waterworks and Sewerage Management, the predecessor of ASTV, was formed in 1967 in the Estonian Soviet Socialist Republic. Further to the collapse of the Soviet Union, the management of local water supply and sewerage was assigned by the Estonian Government (the "**Central Government**") to various municipalities.[18] Tallinn Waterworks and Sewerage Management was transferred to the City of Tallinn in 1992 and was reorganised as the Tallinn Waterworks and Sewerage Municipal Enterprise.

124. In 1994, the Tallinn Waterworks and Sewerage Municipal Enterprise entered into a twinning agreement with the Helsinki Water and Sewage Works for the improvement of the quality of its services. This project was financed by a loan of the European Bank for Reconstruction and Development (the "**EBRD**") of 44.44 million Deutsche Marks (the "**1994 EBRD Loan**").[19] The Estonian State intervened in this loan agreement as a guarantor of the Tallinn Waterworks and Sewerage Municipal Enterprise (the "**State Guarantee**").

125. In 1997, ASTV was incorporated as a public limited company entirely owned by the City of Tallinn and all assets, contractual rights and obligations of the Tallinn Waterworks and Sewerage Management were transferred to ASTV.[20]

126. ASTV (and its predecessor) and the EBRD communicated several times during the period 1995-1998 regarding the level of water tariffs, the possibility of waiving certain financial covenants of the 1994 EBRD Loan as well as ASTV's financing plan and investment

[18] **RL-30**, Estonian Local Government Organisation Act (2 June 1992), s. 6(1).

[19] **C-6**, 1994 Loan Agreement between the EBRD and Tallinn Waterworks and Sewerage Municipal Enterprise (27 May 1994).

[20] **C-3**, ASTV's Certificate of Incorporation (29 May 1997); **C-10**, ASTV Information Memorandum (3 July 2000).

programme.[21] In September 1998, the EBRD communicated to the Ministry of Finance of Estonia its Semi-Annual Monitoring Report of ASTV, including financial statements and financial projections, and brought to the attention of the Ministry certain breaches and other financial issues.[22] In October 1998, the EBRD also copied the Ministry of Finance on its correspondence with ASTV regarding the latter's investment plan.[23]

127. The 1994 EBRD Loan contained a covenant that the water tariffs from 1 March 1995 would be maintained by ASTV at levels at least equal (in real terms) to 1.3 times those applicable on 1 March 1994. As later became clear in the Information Memorandum associated with ASTV's privatisation, ASTV appears to have been in breach of the covenant since 1998, which was the last time during the pre-privatisation period that it increased its tariffs.[24]

128. In February 1999, the Estonia Parliament enacted the Public Water Supply and Sewerage Act, which entered into force on 22 March 1999 (the "**1999 PWSSA**"). The 1999 PWSSA set out a national legislative framework regulating the public water supply and sewerage.[25]

129. Pursuant to the 1999 PWSSA, so-called "water undertakings" were to be appointed by decision of local government councils. The supervision of water tariffs remained at the municipal level. In this latter respect, s. 14(3) of the 1999 PWSSA laid out the following criteria for the determination of water tariffs:

> (3) The price of the service specified in subsection 1 of this section shall be established such that the water undertaking can:
>
> 1) cover production costs;
>
> 2) comply with quality and safety requirements;
>
> 3) comply with environmental protection requirements;
>
> 4) operate with justified profitability.

130. On 26 July 1999, the City of Tallinn adopted a decision to *decrease* ASTV's water tariffs as of 1 October 1999.[26] Various exchanges ensued between the EBRD, the City of Tallinn and the

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[21] **C-273**, Letter from the EBRD to Mr Enno Pere (5 October 1995); **C-274**, Letter from the EBRD to Mr Enno Pere (21 October 1996); **C-275**, Letter from the EBRD to the Minister of Finance of Estonia (23 October 1996).

[22] **C-277**, Fax from Paul Covenden, EBRD, to the Minister of Finance of Estonia – Attachment: Monitoring Report for Tallinn Water (24 September 1998).

[23] **C-278**, Letter from EBRD to Urmo Raiend (26 October 1998).

[24] **C-6**, 1994 Loan Agreement between the EBRD and Tallinn Waterworks and Sewerage Municipal Enterprise (27 May 1994), s. 4.05b); **C-10**, ASTV Information Memorandum (3 July 2000), p 195.

[25] **C-40**, 1999 PWSSA (10 February 1999).

[26] It was reported in newspapers, see **C-52**, Baltic Times article, "Kallas demands the recovering of the water tariff" (31 August 1999), p 1367.

Ministry of Finance, and the matter was discussed by the Government of Estonia on 31 August 1999.[27] On 24 November 1999, the City of Tallinn revoked its decision.[28]

131. On 22 December 1999, the Tallinn City Council adopted Resolution No. 47, regulating water supply and sewerage services. The regulation reiterated the pricing provisions of s. 14(3) of the 1999 PWSSA and delegated to the City government the authority to establish the procedure for determining water tariffs.[29]

B) THE PRIVATISATION OF ASTV

1) The Privatisation Process Established by the City of Tallinn

132. On 6 July 1999, the Tallinn City Council adopted a decision to sell 18 million shares of ASTV to private investors.[30] The EBRD demonstrated an interest in this privatisation and offered its collaboration, expertise and support.[31]

133. The City of Tallinn established a committee to manage the privatisation process (the "**Privatisation Committee**") and retained various industry, legal and financial advisors to assist, including SevernTrent Water International ("**SevernTrent**"), the law firm Allen & Overy, and Suprema Securities AS ("**Suprema**").

134. On 20 April 2000, the Privatisation Committee approved an explanatory memorandum that had been prepared by Suprema, setting out the objectives and general parameters of ASTV's privatisation (the "**Explanatory Memorandum**").[32]

135. The objectives of the privatisation were stated as follows:

> • To increase the quality of water and sewerage services and increase the availability of the service, incl. to cover the whole City with the public sewerage system, and to secure the quality of drinking water complying with the requirements of the European Union by the end of 2011 at the latest.
>
> • To finance large investments by raising private capital,

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[27] **C-282**, Letter from EBRD to Mr Edgar Savisaar (24 August 1999); **C-283**, Letter from Siim Kallas and Aare Järvan to Mayor Peeter Lepp (30 August 1999); **C-284**, Minutes of meeting of Government of Estonia (31 August 1999).

[28] **RL-223**, Regulation No. 100 of the City of Tallinn (24 November 1999).

[29] **RL-67**, Regulation of the Tallinn City Council No. 47 "Procedure for regulating the price of the water supply and sewerage service of Tallinn public waterworks and sewerage" (22 December 1999).

[30] **C-9**, Minutes of the meeting of the City of Tallinn committee for preparing and implementing the tender (20 April 2000).

[31] **C-281**, Letter from the EBRD to Deputy Mayor Eve Fink (11 August 1999).

[32] **C-401**, Suprema material for the Privatization Committee (14 April 2000); **C-9**, Minutes City of Tallinn committee for preparing and implementing the tender (20 April 2000) and Explanatory Memorandum (5 March 2000). The Information Memorandum refers to the Transaction Committee but reference will later to be made to the Privatization Committee.

• To use the know-how and management experience of the private sector to increase the efficiency of Tallinna Vesi,

• To develop a stable and transparent tariff regulation,

• To regulate water management instead of company management.[33]

136. In aid of these objectives, the Explanatory Memorandum provided that, under the terms of the privatisation, the chosen investor would acquire 50.4% of ASTV's common shareholding, comprised of 28 million existing shares and by subscribing to 30 million newly created shares.

137. The Explanatory Memorandum envisaged an investment horizon of at least 15-20 years and underscored that investors could expect certainty with respect to the control of management, the ability to make decisions according to parameters previously agreed on, the ability to decide the tariff distribution, as well as clear and stable tariff regulation.[34]

138. Regarding the determination of water tariffs, Suprema noted that (i) water tariffs are directly related to both the level of services and the needed investment, and (ii) tariffs must allow the investor to achieve justified profitability. It advised adopting a formula based on a price index and pre-established coefficients designed to reflect the operating expenses and investment needs of ASTV.[35]

139. With respect to ASTV's corporate structure, the Explanatory Memorandum indicated that ASTV's Supervisory Council, the organ ultimately responsible for ASTV's management, would be constituted by a majority of the investor's representatives and that the investor would determine the composition of ASTV's Management Board, the body entrusted with the daily management of ASTV (and whose activities are supervised by the Supervisory Council). The City of Tallinn was to be issued a preferred share, the B-share or so-called "***golden share***," which entailed veto rights on certain important decisions by the Supervisory Council and the General Meeting of ASTV's shareholders, the highest governing body of ASTV. The City of Tallinn would also retain the right to revoke ASTV's license.[36]

140. On 26 June 2000, the City of Tallinn issued a notice for sale of a 50.4% stake in ASTV (the "**Tender Notice**")[37] and, on 3 July 2000, the City of Tallinn circulated an information

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[33] **C-9**, Minutes of the meeting of the City of Tallinn committee for preparing and implementing the tender (20 April 2000) and Explanatory Memorandum (5 March 2000), p 135.

[34] **C-9**, Minutes of the meeting of the City of Tallinn committee for preparing and implementing the tender (20 April 2000) and Explanatory Memorandum (5 March 2000), pp 146-148.

[35] **C-9**, Minutes of the meeting of the City of Tallinn committee for preparing and implementing the tender (20 April 2000) and Explanatory Memorandum (5 March 2000), pp 141 and 143.

[36] **C-9**, Minutes of the meeting of the City of Tallinn committee for preparing and implementing the tender (20 April 2000) and Explanatory Memorandum (5 March 2000), pp 149-150.

[37] **C-12**, Notice of Tender (26 June 2000).

memorandum (the "**Information Memorandum**"),[38] which was based on the Explanatory Memorandum.

141. The Information Memorandum provided background information on the prevailing regulatory framework, including the criteria for setting water tariffs under the 1999 PWSSA, but contained a waiver of liability in that respect and encouraged bidders to conduct their own legal due diligence.[39]

142. The City of Tallinn set out a two-stage selection process. Prospective investors had first to meet pre-qualification criteria, including international experience in the management of water and wastewater systems, to be considered as qualified bidders (the "**Qualified Bidders**").[40] Draft transaction documents and other relevant documents would be made available to the Qualified Bidders which would be invited to conduct their due diligence and to comment on the draft transaction documents.[41]

143. The Information Memorandum explained that, as a result of the transaction, the investor would hold 50.4% of ASTV's ordinary shares (A-shares). The investor would gain management control over ASTV *via* majority shareholding in the Supervisory Council and the right to appoint the members of ASTV's Management Board. The City of Tallinn would hold the balance of ASTV's A-shares, in addition to the B-share. The investor and the City would be required to enter into a shareholders' agreement.[42]

144. The Information Memorandum also detailed the level of services that ASTV would be required to achieve over the first five (5) years of operation after the privatisation (*i.e.* from 2000 to 2005) and laid out tentative levels of services for the 2006-2010 period.[43]

145. Regarding the determination of water tariffs, the Information Memorandum indicated that the regulatory framework remained to be defined and that the proposals being discussed assumed that the Tallinn City Government would act as the regulator for the years 2001-2005. It also explained that tariffs would have to comply with the 1999 PWSSA.[44] The Information Memorandum stated that water tariffs would be determined on a yearly basis according to the following formula:

$\Delta T = CPI + K$

Where

- ΔT = annual change in tariff;

[38] **C-10**, ASTV Information Memorandum (3 July 2000).

[39] **C-10**, ASTV Information Memorandum (3 July 2000), p 221.

[40] **C-10**, ASTV Information Memorandum (3 July 2000), pp 224-227.

[41] **C-10**, ASTV Information Memorandum (3 July 2000), p 224.

[42] **C-10**, ASTV Information Memorandum (3 July 2000), p 223.

[43] **C-10**, ASTV Information Memorandum (3 July 2000), pp 231 and ff.

[44] **C-10**, ASTV Information Memorandum (3 July 2000), p 240.

- CPI = change in Consumer Price Index (the CPI being published in the monthly bulletin of Estonian Statistics six months before the new tariff increases are to be applied); and

- K = a coefficient to reflect potential productivity and efficiency gains and an increase in tariffs to finance the provision of the agreed level of service to customers.

146. The tariff determination method set out in the Information Memorandum distinguished between tariffs for the first five (5) years (2001-2005) and those for the years 2006 to 2015, inclusively.

147. Concerning the years 2001 to 2005, the tariffs were to be determined as a result of the bid process. The Information Memorandum specified that the bid was to contain a business plan sufficiently detailed "to enable the tariffs to be determined in respect of the investment required and the levels of service to be achieved."[45]

148. Concerning the 2006 to 2015 period, a price review was to take place in the fifth year of operation (2005) to determine the value of the K-coefficients for the subsequent five (5) years. ASTV would be required to submit a business plan for that period "to enable the Regulator to fulfil his duties."[46] "Regulator" was defined as an entity related to the City of Tallinn.[47]

149. The Information Memorandum stated that the bids would be evaluated according to two (2) criteria: (i) the price of the A-shares to be sold and issued to the investor, and (ii) the K-coefficients of the yearly changes in the price of water and wastewater for the first five (5) year period (*i.e.* from 2001 to 2005). The first factor was attributed a 40% weight and the second one, a 60% weight. The bidders were not required to bid on the K-coefficients for the years after 2005.

150. The bidders were further required to include in their bid: 1) "a detailed business plan of [ASTV], including investment schedule and sources of financing necessary to meet the levels of service" and 2) a "description of sources of financing of the purchase and subscription price."[48]

151. The Information Memorandum disclosed that the 1994 EBRD Loan to ASTV was backed by the State Guarantee and that this loan would be refinanced upon privatisation and the State Guarantee terminated.[49]

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[45] **C-10**, ASTV Information Memorandum (3 July 2000), p 214.

[46] **C-10**, ASTV Information Memorandum (3 July 2000), p 241.

[47] "Tallinn City Price and Competition Board, or any other regulatory body established within the City of Tallinn to regulate the water industry Operators," **C-10**, ASTV Information Memorandum (3 July 2000), p 161.

[48] **C-10**, ASTV Information Memorandum (3 July 2000), p 228.

[49] **C-10**, ASTV Information Memorandum (3 July 2000), p 219.

2) The "Derogation" concerning the Term of ASTV's License, and the 2000 EBRD Loan

152. On 5 May 2000, prior to the issuance of the Tender Notice and of the Information Memorandum, the City of Tallinn had applied to the Ministry of Finance for a "derogation" to the applicable regulation setting the maximum term of licenses to operate water undertakings. Whereas the applicable regulation provided for a recommended term of five (5) years, the City of Tallinn requested to be allowed to establish a twenty-year term for ASTV's license.[50]

153. On 20 June 2000, after having sought and obtained advice from the ECA,[51] the Ministry of Finance recommended to the City of Tallinn to apply for a right to grant a license for fifteen (15) years.[52] On 1 August 2000, the Prime Minister and other members of the Estonian Government signed an order allowing the City of Tallinn to grant a fifteen-year license to ASTV.[53]

154. On 31 October 2000, in preparation for ASTV's privatisation, ASTV and the EBRD agreed on a credit facility of EUR 22.5 million (the "**2000 EBRD Loan**")[54], structured as follows: EUR 15.5 million were to replace the 1994 EBRD Loan and EUR 7 million were to replace an existing syndicate loan from various banks. The State Guarantee was to be released upon the drawing of the 2000 EBRD Loan. This loan was never drawn and was replaced by another financing facility in 2002.[55]

3) UUTBV's Participation in the Tender Process

a) Creation of UUTBV

155. UUTBV was created on 11 July 2000 for the purpose of bidding on ASTV's privatisation. UUTBV was at the time a 50%-50% joint venture between United Utilities International Limited ("**United Utilities**") and International Water (Holdings) BV ("**International Water**"), which itself was a joint venture between Bechtel and Edison.[56]

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[50] **C-13**, Request for sole license period extension from the City of Tallinn to the Ministry of Finance (20 years) (5 May 2000).

[51] **C-289**, Letter from Peeter Tammistu to Aare Järvan (29 May 2000); **C-288**, Letter from Aare Järvan to the ECA (24 May 2000); see also **C-290**, Draft Order and associated documents submitted by Siim Kallas to the Government House, p 4298.

[52] **C-14**, Response from the Ministry of Finance (20 June 2000).

[53] **C-15**, Order granting exception to license period (1 August 2000); **C-290**, Draft Order and associated documents submitted by Siim Kallas to the Government House (12 July 2000) and **C-406**, Minutes of meeting of the Government of Estonia (1 August 2000).

[54] **C-17**, 2000 Loan Agreement between ASTV and the EBRD (31 October 2000).

[55] See below at paragraphs 203-206.

[56] **C-252**, Structure charts showing changes in shareholding of UUTBV over time.

b) Discussions between UUTBV and the City of Tallinn prior to UUTBV's Bid

156. After having pre-qualified as a Qualified Bidder,[57] UUTBV sought clarifications and exchanged with the City of Tallinn and its advisors on several issues, three (3) of which have particular bearing on the current dispute: the definition of "*justified profitability*," the status of the *business plan* to be enclosed with the bids, and the matter of *control* over ASTV.

(i) Pre-Bid Discussion regarding Justified Profitability

157. On 16 October 2000, UUTBV put to Suprema that the reference to "justified profitability*"* in the 1999 PWSSA "*needs to be clearly defined.*"[58] Approximately one (1) month later, UUTBV stressed that the tariff mechanism ought to be predictable so as to ensure a level of certainty of the investor's revenues. UUTBV further suggested that the privatisation agreements define the method for determining water tariffs beyond 2005.[59]

158. In a meeting on 17 November 2000 (the "**November 2000 Meeting**"), UUTBV and the City of Tallinn's advisers discussed the issue of justified profitability. The City's advisors expressed their unwillingness to "consider any definition of 'Justified Profitability' that specified a number (or range of numbers) or made explicit reference to the Investor's Business Plan," stressing that they did not want to create a "fixed income instrument."[60] It was agreed that UUTBV would propose a method for determining justified profitability,[61] which UUTBV did on 18 November 2000:

> We propose that the following principles should be used as the basis for the establishment of "Justified Profitability" when tariff levels are determined.
>
> • Target Rate of Return will be set by an independent financial advisor, to be selected by agreement by the Parties.
>
> • He or she will select a number (5) of market comparables (which may include the short listed bidders) to be used in setting the appropriate target rate of return / justifiable profit.
>
> • He or she will take into consideration the Business Plan of the Bidder submitted at the time of the bid, and will take into account the difference

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[57] Two (2) other entities would have been pre-qualified by the City of Tallinn, Vivendi/RWE Ruhrwasser and Lyonnaise des Eaux/Northumbrian Water, Cl. Mem., ¶75.

[58] **C-67**, Letter from UUTBV to Suprema (16 October 2000) [emphasis added], UUTBV included this concern in a section entitled "There is an unacceptable level of regulatory uncertainty at present." See also **C-68**, Letter from UUTBV to Suprema (18 October 2000), p 1427.

[59] **C-77**, Letter from UUTBV to Suprema (13 November 2000), p 1452.

[60] **C-79**, Notes of Meeting between UUTBV, Suprema, Luiga & Mugu, Allen & Overy and SevernTrent (17 November 2000), pp 1459 and 1460.

[61] **C-79**, Notes of Meeting between UUTBV, Suprema, Luiga & Mugu, Allen & Overy and SevernTrent (17 November 2000), p 1460.

> in risk profiles between resident countries (based on country FX credit ratings).[62]

159. On 23 November 2000, the Privatisation Committee resolved to include the following methodology in the privatisation contracts to better define "justified profitability":

> As of the fifth year, the tariff coefficients are determined for an advance period of five years by way of negotiations between the city and the company on the basis of the company's tender. The tender also includes the investor's understanding of JP [justified profitability]. If the city considers the offered JP [justified profitability] to be unjustified and the parties fail to reach a consensus, the size of JP [justified profitability] shall be determined by an independent international expert who shall analyse JPs [justified profitability] of five comparable companies and shall additionally take into account:
>
> - the generally accepted business practices of water companies
> - the economic situation of Estonia and Tallinn
> - the vision presented in the business plan[.][63]

(ii) The Pre-Bid Discussion regarding the Status of the Business Plan

160. At the November 2000 Meeting, UUTBV and the City of Tallinn advisors also addressed the status of the business plan to be included in the bid. Whereas the City of Tallinn's advisors were divided on this issue, UUTBV informed them that the approval of the business plan before the closing of the transaction was "essential."[64]

161. A few days after, on 21 November 2000, Suprema transmitted to UUTBV a memorandum summarising the changes to be incorporated into the privatisation agreements. In response to UUTBV's request to obtain approval of the business plan prior closing, the memorandum stated, under the heading "Action taken":

> Shareholders undertake to carry out the business plan as attached to the SHA [the Shareholders' Agreement], provided it does not violate other Clauses in the SHA [the Shareholders' Agreement] and the AoA [Articles of Association].[65]

162. On 23 November 2000, the Privatisation Committee resolved to not consider the business plans to be submitted with the bids in the evaluation of the tenders. The Committee also

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[62] **C-80**, Letter from UUTBV to Suprema (18 November 2000), pp 1461-1462.

[63] **C-16**, Tallinn City Council Committee on Privatisation of ASTV Meeting Minutes (23 November 2000).

[64] **C-79**, Notes of Meeting between UUTBV, Suprema, Luiga & Mugu, Allen & Overy and SevernTrent (17 November 2000), p 1457.

[65] **C-81**, Email from Priit Koit to Tim Lowe (21 November 2000), Attachment: "Memorandum for International Water / United Utilities regarding incorporation of changes to the Transaction Documents and the Service Agreement" (20 November 2000).

resolved that such business plans would only become binding on the Parties upon approval by ASTV's Supervisory Committee.[66]

(iii) The Pre-Bid Discussion regarding control over ASTV

163. Throughout its exchanges with the advisors of the City of Tallinn, UUTBV raised concerns regarding control of the privatised ASTV. These issues were addressed in various amendments to the draft privatisation agreements, with the exception of UUTBV's request to modify the veto rights of the City of Tallinn.[67]

4) Appointment of ASTV as Tallinn's Exclusive Water Supplier and Operator of Sewerage Facility

164. On 23 November 2000, the Council of the City of Tallinn adopted Decree No. 396 appointing ASTV as the exclusive water supplier and operator of sewerage activity in the main public water supply and sewerage activity area of Tallinn for a period of fifteen (15) years.[68]

5) UUTBV's Bid

165. On 1 December 2000, UUTBV submitted a bid to the City of Tallinn. Only one (1) other Qualified Bidder, Compagnie Locale d'Investissement et de Gestion 4 S.A. ("**CLIG 4**"), submitted a bid.[69]

a) Share Price

166. UUTBV bid for the purchase of 30 million new shares to be issued by ASTV for a price of 687,000,000 Kroons (equivalent to approximately EUR 44 million) and the purchase of 28 million shares from the City of Tallinn for a price of 641,200,000 Kroons (equivalent to approximately EUR 41 million). As a result, UUTBV offered to invest a sum of 1,328,200,000 Kroons (EUR 84,871,908).[70]

b) K-coefficients (Tariffs)

167. UUTBV's bid provided for the following K-coefficients for the years 2001-2005:

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[66] **C-16**, Tallinn City Council Committee on Privatisation of ASTV Meeting Minutes (23 November 2000), p 283.

[67] **C-66**, Letter from UUTBV to Suprema (9 October 2000); C-71, Email from Tim Lowe to David Kerr and others (24 October 2000); **C-80**, Letter from UUTBV to Suprema (18 November 2000).

[68] **C-21**, City of Tallinn's Council Decree No. 396 (30 November 2000).

[69] **C-48**, Resolution of the City of Tallinn regarding the Issue and Sale of Shares of ASTV (21 December 2000).

[70] **C-48**, Resolution of the City of Tallinn regarding the Issue and Sale of Shares of ASTV (21 December 2000).

2001	2002	2003	2004	2005
0%	0%	0%	15%	15%

168. As required by the Information Memorandum, UUTBV included a business plan for ASTV covering the period 2001-2005 (the "**2001 Business Plan**"), which was also intended to be used as a basis for the drafting of future ASTV's business plans:

> This Business Plan covers in detail the period 2001-2005 inclusive, and provides the commercial, financial, operational and technical basis upon which the period from 2006 onwards will be defined. This Business Plan will therefore be used as the basis for the drafting of future Company Business Plans.[71]

169. The 2001 Business Plan included financial projections for the entire term of ASTV's license (the "**Financial Model**"), comprised of a "cash flow statement" laying out the projected distributions to ASTV's shareholders over the fifteen-year period.[72]

170. The 2001 Business Plan also set out a methodology for the determination of water tariffs for the years after 2005, including how the City of Tallinn or other "Regulator" would assess justifiable profitability. According to the 2001 Business Plan, justifiable profitability would be determined by reference to five (5) international proxy companies.[73]

171. On 5 December 2000, the City of Tallinn Privatisation Committee adopted a resolution declaring UUTBV's bid to be "the best offer."[74]

172. The 2001 Business Plan gave rise to various exchanges between Suprema and UUTBV over the following weeks.[75] After UUTBV had provided the requested particulars, the Tallinn City Government passed a resolution on 21 December 2000 that also declared UUTBV's bid to be the best submitted. The resolution specified that, should UUTBV fail to execute a purchase and sale contract within one (1) month, the second best bidder would acquire a right to conclude such a contract under the "terms and conditions listed in point 2 above." These terms and conditions consisted of the purchase price and K-coefficients included in UUTBV's bid.[76]

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[71] **C-20**, Shareholders' Agreement (12 January 2001), s. 1.1 of the Business Plan, p 383.

[72] **C-20**, Shareholders' Agreement (12 January 2001), pp 454-458.

[73] **C-20**, Shareholders' Agreement (12 January 2001), pp 464-466. The 2001 Business Plan refers to the "Regulator/City/MMU," the MMU being the Mandatory Mandate Unit (see below at paragraph 180).

[74] **C-85**, Minutes of Meeting of the Privatisation Committee (5 December 2000), ss. 3 and 4.

[75] **C-87**, Letter from Pritt Koit to Tim Lowe (12 December 2000); **C-89**, Letter from Tim Lowe to Pritt Koit (18 December 2000).

[76] **C-48**, Resolution of the City of Tallinn regarding the Issue and Sale of Shares of ASTV (21 December 2000).

C) THE ENTRY OF UUTBV INTO ASTV AND THE SIGNATURE OF THE PRIVATISATION AGREEMENTS

173. Between 12 and 22 January 2001, the following agreements were entered into:

- The Share Sale and Subscription Agreement;
- The Services Agreement;
- The Shareholders' Agreement.

1) The Share Sale and Subscription Agreement

174. On 12 January 2001, the City of Tallinn, UUTBV and ASTV entered into a Share Sale and Subscription Agreement (the "**Share Sale and Subscription Agreement**").[77]

175. UUTBV subscribed to 30 million newly issued ordinary shares in ASTV (for a price of about EUR 44 million) and purchased from the City of Tallinn 28 million ordinary shares (for a price of about EUR 41 million).[78] As a result, UUTBV acquired of 50.4% of ASTV's ordinary shareholding. The City of Tallinn owned from thereon the balance of the ordinary shareholding, as well as the B-share.

2) The Services Agreement

176. On the same date, ASTV and the City of Tallinn executed the Services Agreement setting out the terms according to which ASTV was to supply water and sewerage services to the region of Tallinn (the "**Services Agreement**").[79]

a) The Body of the Services Agreement

177. The Services Agreement defined ASTV's mandate as the:

> […] exclusive rights and obligations acquired and assumed by the Company under this Agreement and under the Resolution of Tallinn City Council Number 396 dated 30 November, 2000 including, without limitation, the obligation of the Company to perform the Services and the right to charge the Tariffs pursuant to the Statutory Requirements and this Agreement and the appointment of the Company as the provider of the Services pursuant to the PWSSA […].[80]

178. The Services Agreement further stipulated that the Mandate Period was to start from the fulfilment of certain conditions precedent to the transaction and to expire fifteen (15) years

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[77] **C-49,** Closing Memorandum of the Share Sale and Subscription Agreement for the 58,000,000 Shares of ASTV as of 12 January 2001 between Tallinna Linn, ASTV and UUTBV (24 January 2001) ["**Closing Memorandum**"].

[78] **C-19**, Share Sale and Subscription Agreement (12 January 2001), Clauses 4 and 5.

[79] **C-22**, Services Agreement (including schedules) (12 January 2001).

[80] **C-22**, Services Agreement (including schedules) (12 January 2001), Clause 1, s.v. "Mandate."

after the adoption of Resolution No. 396 granting ASTV's license, or at the termination of the agreement.[81]

179. The Services Agreement detailed the levels of services ("**Service Levels**") as well as the capital investment requirements ("**Investment Requirements**") to be fulfilled by ASTV. These capital investments included works for the extension of Tallinn's water infrastructure network.

180. The Services Agreement defined the Regulator as "the independent water utilities regulator appointed pursuant to the regulatory framework referred to in Clause 5(3),"[82] which provision concerned the setting up of the Mandate Monitoring Unit (the "**MMU**"). The MMU was to be created shortly after the privatisation to monitor ASTV's compliance with the Service Levels and to assume an advisory role in the determination of the tariffs.[83] The City undertook that the City of Tallinn, the Regulator or an "*other person responsible for setting the Rates*" would determine the water tariffs in accordance with Clause 7 of the agreement with the support of MMU.[84]

181. Clause 7(1)(a) provided that water tariffs were to be determined in accordance with the provisions of the agreement and "Statutory Requirements," which were defined as including changes in the applicable law. Further, tariffs ought to reflect the stated Tariff Criteria (Part I of Schedule E, discussed below) as well as the K-coefficient and a price index:

> The Rates of Tariffs shall be determined in accordance with the Tariff Criteria and to the extent consistent with the Tariff Criteria shall reflect:
>
> (i) the K coefficient as provided in paragraph (c); and
>
> (ii) any changes in the Retail Prices Index referred to in Clause 12(3) as provided in the Tariff Criteria.[85]

182. As did the Information Memorandum, the Services Agreement distinguished between the first five (5) years of the fifteen-year license period (*i.e.* 2001-2005), referred to as the first five (5) "Operating Years" or the "Initial Period," and the subsequent ten (10) years (*i.e.* 2006-2015). The K-coefficients for the years 2001-2005 were those included in UUTBV's bid, as provided in Part II of Schedule E to the Services Agreement. The K-coefficients for the subsequent years were to be determined according to the process set out in Part I of Schedule E, in accordance with the following criteria at Clauses 7(4) and 8:

[81] **C-22**, Services Agreement (including schedules) (12 January 2001), Clause 1, s.v. "Mandate Period."

[82] **C-22**, Services Agreement (including schedules) (12 January 2001), Clause 1.

[83] **C-22**, Services Agreement (including schedules) (12 January 2001), Clause 5(3).

[84] **C-22**, Services Agreement (including schedules) (12 January 2001), Clause 7(4)(a).

[85] **C-22**, Services Agreement (including schedules) (12 January 2001), Clause 7(4)(b).

(4) (a) The City undertakes that:

(i) the City, the Regulator or other person responsible for setting the Rates of the Tariffs in accordance with the Statutory Requirements (the 'Tariff Authority'); and

(ii) the Mandate Monitoring Unit in making recommendations in relation to the Rates of the Tariffs,

shall determine or recommend (as applicable) the Rates of Tariffs in accordance with the provisions of this Clause 7.

(b) The Rates of Tariffs shall be determined in accordance with the Tariff Criteria and to the extent consistent with the Tariff Criteria shall reflect:

(i) the K coefficient as provided in paragraph (c); and

(ii) any changes in the Retail Prices Index referred to in Clause 12(3) as provided in the Tariff Criteria.

It is acknowledged that operation of the Tariff Criteria may result in it not being possible to increase the Rates to reflect fully increases which would otherwise be required pursuant to Clause 16 (Variations) or Clause 17 (Changes in Law). In this event the Company shall not under this Agreement, to the extent that the Rates have not been increased, be obliged to carry out the Capital Works or make the changes to the Services as required by the operation of Clauses 16 and 17, and shall not be required to comply with the additional requirements comprised in the Change of Law, and to such extent any failure to comply with such obligations shall be deemed to be due to a Force Majeure Event. This relief of liability shall not affect the operation of the Statutory Requirements but the City shall take all action within its powers to procure that the Company is relieved of its liability under the Statutory Requirements in the same manner as it is relieved of liability under this Agreement.

(c) (i) In respect of the period during the First Operating Year from 1st April 2020[] to 31st December, 2001 and the four Operating Years commencing 1st January, 2002, 1st January, 2003, 1st January, 2004 and 1st January, 2005, the City shall, undertake in determining the Rates of Tariffs in accordance with the Tariff Criteria, to use the K coefficient for the relevant Operating Year as set out in Schedule E Part II.

(ii)The K coefficient for the Operating Periods following the Initial Period shall be determined in accordance with the criteria set out in Clauses 7(4)(a) and (b) and the provisions of Clause 8.[86]

[86] **C-22**, Services Agreement (including schedules) (12 January 2001), Clause 7(4)(a), (b) and (c).

183. Clause 8 provided for a project review to be conducted at each five-year block of the license period, each being defined as an "**Operating Period**." Concerning the second and third Operating Periods (*i.e.* after the first five (5) year of the license period), the MMU was to review ASTV's performance for the current Operating Period and the programme for the next one:

> Within six months prior to the end of each period of five Operating Years the first such period being the Initial Period (each an 'Operating Period'), the City and the Company or, following the establishment of the Mandate Monitoring Unit, the Mandate Monitoring Unit shall review the performance of the Company during the current Operating Period and the programme for the next Operating Period (the 'Project Review') in accordance with the procedure set out in Clause 9 (Review Procedure). The Project Review shall cover the following matters: […]
>
> (b) in relation to the period of the next Operating Period (being the period of the next five Operating Years):
>
> > (i) measures to be taken to comply with the Requirements applicable to the period;
> >
> > (ii) the matters listed in paragraphs (a)(iii), (iv), (v) and (vi); and
> >
> > (iii) the K-coefficient.

b) Schedule E of the Services Agreement

184. Schedule E of the Services Agreement provided for a process for determining the Rate of Tariff, for both the Initial Period and the two (2) subsequent Operating Periods.

185. Part I of Schedule E of the Services Agreement, entitled "Rate of Tariff Criteria," laid out the procedure for determining the tariffs for the two (2) last Operating Periods (*i.e.*, 2006-2010 and 2011-2015) by first providing that tariff shall be set in accordance with the 1999 PWSSA and the following formula:

> $T1 = T0 * (1+ \Delta THI + K)$
>
> Where
>
> T1 – Rate of Tariff for the next period
>
> T0 – Rate of Tariff for the current period
>
> Δ THI – Change in CPI (per cent)
>
> K-coefficient, reflecting additional change in the Rate of Tariff (per cent)

> The accounting period for the change shall be 12 months to the end of a quarter, which ends less than 6 months prior to the fixing of the new Rate of Tariff by the City.[87]

186. Second, the Parties were to negotiate and agree on the applicable K-coefficients, which were to reflect "the change in necessary expenses to be made by the Company to achieve the set Service Levels, and justified profitability, but […] not include the changes in costs that are included in the change of CPI."[88] The Services Agreement provided that K-coefficients were to be presented for five (5) years in advance and that ASTV had to submit a proposal in that respect, including "a detailed business plan for the period to be regulated."[89]

187. Schedule E also particularised the "criteria of justified profitability" by stating that it would be determined by reference to five (5) suitable market comparable and by taking into account the following:

> (i) generally accepted commercial principles for water and wastewater utilities
>
> (ii) the specific economic situation in Tallinn and Estonia and
>
> (iii) the Business Plan.[90]

3) The Shareholders' Agreement

188. Also on 12 January 2001, UUTBV, the City of the Tallinn and ASTV executed a shareholders' agreement (the "**Shareholders' Agreement**").[91]

189. The 2001 Business Plan, as submitted by UUTBV in its bid, was appended to the Shareholders' Agreement and, at s. 5.5.8, the Parties undertook to "make reasonable efforts to ensure the fulfilment of the Business Plan."[92]

190. The Shareholders' Agreement also provided that UUTBV would appoint four (4) of the seven (7) members of the Supervisory Council,[93] and it was agreed that the votes of UUTBV's appointees would be sufficient for the election and/or removal of all the members of the Management Board.[94]

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[87] **C-22**, Services Agreement (including schedules) (12 January 2001), p 616.

[88] **C-22**, Services Agreement (including schedules) (12 January 2001), p 616.

[89] **C-22**, Services Agreement (including schedules) (12 January 2001), p 617.

[90] **C-22**, Services Agreement (including schedules) (12 January 2001), p 618.

[91] **C-20**, Shareholders' Agreement (12 January 2001).

[92] **C-20**, Shareholders' Agreement (12 January 2001), p 368.

[93] **C-20**, Shareholders' Agreement (12 January 2001), ss. 3.1.1 and 3.1.2(b).

[94] **C-20**, Shareholders' Agreement (12 January 2001), s. 3.1.12.

4) The Closing of the Share Sale and Subscription Agreement

191. On 22 January 2001, International Water issued a performance guarantee in favour of the City of Tallinn for the fulfilment of UUTBV's obligations under the Share Sale and Subscription Agreement.[95]

192. All conditions precedent having been met, the transaction contemplated by the Share Sale and Subscription Agreement was closed on 24 January 2001 and a closing memorandum was executed by the City of Tallinn, ASTV and UUTBV (the "**Closing Memorandum**"). The Closing Memorandum recorded the payment of the share price by UUTBV and the signature of the Subscription Agreement. It also recorded the execution of the Letter of Understanding, which set out UUTBV and the City of Tallinn's common understanding of the status and interpretation of the 2001 Business Plan.

D) THE FIRST YEAR OF OPERATION AFTER ASTV'S PRIVATISATION

193. On 29 March 2001, as contemplated in the 2001 Business Plan, UUTBV and ASTV concluded a technical services agreement for the provision by UUTBV of certain management services to ASTV in return for a management fee (the "**Technical Services Agreement**").[96]

194. Later in 2001, it was resolved at ASTV's General Meeting to pay out dividends in the total amount of EUR 11.6 million from (i) ASTV's annual profits of EUR 1.5 million and (ii) ASTV's investment reserve.[97] UUTBV received an amount of EUR 5.9 million in such dividends.

195. Further to a proposal by UUTBV, it was also resolved at an extraordinary General Meeting of ASTV to reduce the share capital of ASTV by 80%, from EUR 71.3 million to EUR 12.8 million.[98] As a result, UUTBV received EUR 30.6 million. Such restructuring had also been envisioned in the 2001 Business Plan, although at a later stage of the first five (5) years of the privatisation.[99]

E) THE 2002 AMENDMENT TO THE SERVICES AGREEMENT

196. In April 2002, the City of Tallinn informed ASTV that it wished to enter into negotiations with respect to a number of issues, the most notable being the determination of tariffs. The City of Tallinn expressed concerns regarding the increase of tariffs planned for 2005 to 2010 in the light of the rising cost of living in Estonia and the negative impact that an increase could have on ASTV's business and customers.[100]

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[95] **C-92**, Performance Guarantee provided by United Utilities International Limited (22 January 2001).

[96] **C-113**, Prospectus for ASTV 2005 IPO (2005), p 1885; **C-49**, Closing Memorandum.

[97] **C-90**, ASTV Annual Report 2000, pp 10 and 32.

[98] **C-295**, Minutes of ASTV EGM (1 November 2001).

[99] **C-20**, Shareholders' Agreement (12 January 2001), pp 452-453.

[100] **C-98**, Letter from City of Tallinn to ASTV and letter from ASTV to City of Tallinn of same date (10 April 2002).

197. The negotiations spanned the following six (6) months. The issues identified by the City of Tallinn were discussed for the first time on 23 April 2002 at ASTV's Supervisory Council. In its reply of 25 April 2010,[101] ASTV put to the City of Tallinn that a review of levels of tariffs would require as a corollary a review of the investments program, and of the Service Levels, and that it would be necessary to ensure the respect of the financial conditions on which the original investment was made.[102]

198. On 30 September 2002, the City of Tallinn, ASTV and UUTBV concluded an amendment to the Services Agreement (the "**2002 Amendment**").[103]

199. Schedule I: Part V of the 2002 Amendment revised the K-coefficients for the 2003-2005 years, as determined through the bidding process, and introduced K-coefficients for the years 2006-2010:[104]

Year	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**
Original K Coefficient (%)	0	+15	+15	-	-	-	-	-
Amended K Coefficient (%)	-3.8	+10	+10	+6.5	+6.5	+6.5	+2	+2

200. Pursuant to the new Financial Model attached to the 2002 Amendment, the tariffs for the period beyond 2010 (2011-2015) were assumed to be only based on the CPI as the K-coefficients were set to zero (0).[105]

201. The 2002 Amendment also laid out the functions and responsibilities to be assumed by the MMU at its Schedule I, Part III, as foreshadowed in the Services Agreement.[106]

202. Finally, the 2002 Amendment addressed the reimbursement of costs incurred for the expansion for ASTV's network.[107]

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[101] **C-100**, Letter from ASTV to City of Tallinn (25 April 2002).

[102] **C-100**, Letter from ASTV to City of Tallinn (25 April 2002), p 1580 and, at p 1582, ASTV stated that "we will be creative and co-operative in our joint endeavours to find a solution to your proposals, but these must respect the financial conditions upon which the original investment of 85 million euro was based."

[103] **C-30**, Agreement on Amending the Project Agreements (30 September 2002) [the "**2002 Amendment**"].

[104] **C-30**, 2002 Amendment, Schedule I.

[105] **C-30**, 2002 Amendment, p 776.

[106] **C-22**, Services Agreement (including schedules) (12 January 2001), Clause 5(3)(a) and Schedule H.

[107] **C-30**, 2002 Amendment Agreement, Schedule I: Part V.

F) THE 2002 EBRD LOAN

203. The 2000 EBRD Loan, which had been executed for purposes of the privatisation, as mentioned above at paragraph 154, was never drawn. Rather, ASTV entered into a new loan agreement of EUR 80 million with the EBRD (the "**2002 EBRD Loan**"),[108] which replaced the 2000 EBRD Loan.

204. The purpose of the 2002 EBRD Loan was to finance the water supply and sewerage network extension programme (referred by the stakeholders as the Network Extension Programme or the "**NEP**") and other investments required under the Services Agreement, to refinance the 1994 EBRD Loan, to finance the costs of the 2000 EBRD Loan as well as to restructure ASTV's balance sheet through share capital reduction.

205. Two (2) securities were granted in favour of the EBRD. First, UUTBV pledged its shares in ASTV to the EBRD.[109] Second, UUTBV, its shareholders, ASTV and the EBRD entered into a Share Retention and Subordination Agreement pursuant to which ASTV pledged all of its material assets, present and future.[110]

206. The 2002 EBRD Loan resulted in the release of the State Guarantee.[111]

G) THE ENTRY OF THE EBRD INTO UUTBV (AND INDIRECTLY ASTV) IN 2003

207. In 2003, United Utilities and the EBRD each purchased 50% of International Water's stake in UUTBV.[112] After the transaction, United Utilities held a 75% shareholding, and the EBRD a 25% shareholding, in UUTBV.[113]

208. The EBRD exited its investment on 29 October 2010.[114]

H) THE ASTV'S IPO AND THE 2005 AMENDMENTS TO THE SERVICES AGREEMENT

209. In 2005, ASTV was the subject of an initial public offering ("**IPO**"). UUTBV and the City of Tallinn jointly sold 30% of ASTV's shareholding on the Tallinn Stock Exchange, and ASTV became a publicly traded company. As a result of the IPO, UUTBV held 35.3% of ASTV's ordinary shareholding and the City of Tallinn 34.7%.[115]

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[108] **C-23**, 2002 Loan Agreement between ASTV and EBRD (8 November 2002).

[109] **C-24**, Share Pledge Agreement 2002 (8 November 2002).

[110] **C-25**, Share Retention and Subordination Agreement (8 November 2002).

[111] **C-27**, Letter from the EBRD (11 January 2012).

[112] The ECA approved the transaction on 5 December 2003, **R-183**, Merger Clearance of the ECA (5 December 2003).

[113] **C-251**, Snapshot of ASTV website showing financial reports (2015).

[114] Cl. Reply, ¶525; **C-252**, Structure charts showing changes in shareholding of UUTBV over time.

[115] **C-29**, Agreement on Amending the Project Agreements (10 March 2005), Clause 3.2.

210. Two (2) amendments to the Services Agreement were executed by ASTV, the City of Tallinn and UUTBV in connection with the IPO. The first concerned certain changes in the structure of ASTV (the "**First 2005 Amendment**"),[116] whereby the signatories recorded among other things their intention to maintain the *status quo* as to the balance of rights between the City of Tallinn and UUTBV and the maintenance of UUTBV's full operational control of ASTV. The second concerned a review of the Network Extension Programme (the "**Second 2005 Amendment**"), which would have become necessary due to the insufficiency of the City of Tallinn's financing.[117]

I) 2005-2008: Reforms Proposals for the Water Tariff Regulation under the 1999 PWSSA

211. In 2005, various Estonian authorities began discussing reforms to the water tariff regulatory framework. Three (3) reform proposals have been referred to in the course of these proceedings:

- The reform proposal of the Ministry of Environment;
- The reform proposal of the State Audit Office;
- The reform proposal of the Chancellor of Justice, Mr Allar Jõks.

1) Reform Proposal of the Ministry of Environment

212. In 2006, the Ministry of Environment became concerned that the tariffs charged by various water undertakings in Estonia did not cover all of the relevant costs. More specifically, there was a concern that many localities had failed to implement appropriate tariffs and that the water undertakings were not abiding by the tariff increases forecasted in applications for European Union aid. The Ministry of Environment concluded that these failures had a negative impact on the country's infrastructure and that it was necessary to transfer the authority over water pricing to an independent State agency. The Ministry of Environment proposed an amendment to the 1999 PWSSA accordingly.[118]

2) Reform Proposal of the State Audit Office

213. In 2005, the State Audit Office, an independent government agency responsible for financial supervision and auditing of the Estonian public sector, commenced an audit of the wastewater development projects supported by the European Union. For the purposes of this investigation, the State Audit Office commissioned an expert assessment of three (3) EU-funded projects, which was completed in 2006.[119] In its report published in 2007, the State Audit Office concluded that the level of water tariffs failed to cover all costs and did not ensure sustainable

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[116] **C-29**, Agreement on Amending the Project Agreements (10 March 2005).

[117] **C-31**, Agreement on Amending the Services Agreement (14 March 2005).

[118] Kroon 1st WS, ¶¶6-13; **R-140**, Extract from the Ministry of Environment's work plan (2007).

[119] **R-143**, Expert Appraisal, Audacon Eesti OÜ (2006).

management. Amongst other, it recommended that authority over water tariffs, water supply and sewerage service be transferred to an entity forming part of the Ministry of Environment.[120]

214. Following its investigation, the State of Audit Office recommended to the Minister of Environment to initiate the process for amending the 1999 PWSSA in order to transfer the authority for setting water tariffs, which it had already undertaken.[121]

3) Reform Proposal of the Chancellor of Justice

215. Concurrently with the foregoing initiatives, Mr Allar Jõks, the Chancellor of Justice, an independent official mandated to review the conformity of Estonian legislation with the national constitution,[122] expressed criticism regarding the water tariffs system in 2005 and 2006.

216. The Chancellor's concerns were directed at what he considered to be an abuse of dominance by the water utility companies.[123] In 2007, the Chancellor of Justice suggested the establishment of an independent body to supervise the determination of water tariffs.[124]

4) October-November 2007: the Government Cabinet Supports the Ministry of Environment's Reform Proposal

217. On 4 October 2007, the Ministry of Environment submitted a memorandum and draft decision to the cabinet of the Central Government concerning the financing of water infrastructure projects funded by the European Union. Among the Ministry's recommendations was a proposal to amend the legislative framework so as to transfer authority for the determination of water prices from local, city and rural governments to a competent existing national authority.[125]

218. On 9 October 2007, the Ministry of Environment convened municipal representatives, including from the City of Tallinn, to a public information session on its ongoing work concerning the funding of water infrastructure projects. Proposed amendments to the 1999 PWSSA were then introduced.[126]

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[120] **R-142**, Development of wastewater treatment in rural areas supported by Cohesion Fund projects, Audit Report, State Audit Office (24 May 2007), p 2 and ss. 3.1 and 3.2; **R-186**, State Audit Office, Overview of the use and preservation of the State's assets in 2006 (2007), ¶¶216-226.

[121] Kroon 1st WS, ¶¶18 and 19.

[122] **RL-90**, Chancellor of Justice Act (12 May 2010, version in force on 10 March 2009).

[123] **R-106**, Chancellor of Justice, Overview of the Activities of the Chancellor of Justice in 2004, Yearbook 2005 (1 September 2005) pp 40-43; **R-107**, Chancellor of Justice, Overview of the Activities of the Chancellor of Justice in 2005, Yearbook 2006 (1 September 2006), p 209.

[124] **R-109**, Article by the Chancellor of Justice, "The Chancellor of Justice: verification of justification of the prices for water services and transport of waste requires state supervision" (8 November 2007).

[125] **R-146**, Memorandum for the Cabinet Meeting (4 October 2007).

[126] **R-150**, List of local municipalities who were invited to the information day, p 2; **R-149**, Letter of the Ministry of Environment to local municipalities (28 September 2007); Kroon 1st WS, ¶25.

219. On 22 November 2007, the cabinet of the Central Government approved the Ministry of Environment's proposal to amend the legislative framework applying to the water and sewerage services.[127]

5) June 2008: the First Draft Amendment to the 1999 PWSSA by the Ministry of Environment

220. The Ministry of Environment finalised its draft amendments to the 1999 PWSSA in June 2008.[128] The amendments provided that:

- Only the governments of the local municipality would have authority to determine the water tariffs (as opposed to both municipal governments and local councils under the 1999 PWSSA). The local councils would however retain the power to set out the procedure for determining water tariffs;[129] and

- Two (2) State agencies at the national level would be entrusted with the control of the level of the water tariffs: the ECA and the Environmental Inspectorate.[130] Where tariffs would be found to be non-compliant, these authorities would be authorised to issue binding orders to increase or lower tariffs in order to bring them to an appropriate level. Should a local municipality fail to abide by such order within six (6) months, the ECA could directly enforce it:

> If the price of the service specified in subsection (1) of this section is not fair and does not correspond to the expenses of the water undertaking specified in subsection (3) of this section, the Competition Authority and the Environmental Inspectorate shall have the right to issue a precept to the local government for the establishment of a new service price.
>
> […] If the local government has not established a price complying with requirements within 6 months after receiving a precept specified in subsection (3^2), the Competition Authority shall have the right to establish with an order a new service price complying with subsection 14 (3), which shall be made public at least ninety days before the price is applied, publishing a notice concerning the change of the price in at least one local or county newspaper twice with an interval of two weeks.[131]

[127] **R-148**, Minutes of the Cabinet Meeting (22 November 2007), p 3.

[128] **RL-91**, Draft Act Amending the Public Water Supply and Sewerage Act (2008) ["**Draft Act Amending the PWSSA**"].

[129] **RL-91**, Draft Act Amending the PWSSA, s. 12.

[130] **RL-91**, Draft Act Amending the PWSSA, s. 15.

[131] **RL-91**, Draft Act Amending the PWSSA, s. 13.

J) THE 2007 AMENDMENT TO THE SERVICES AGREEMENT

221. On 30 November 2007, the City of Tallinn, UUTBV, and ASTV concluded a fourth amendment to the Services Agreement (the "**2007 Amendment**").[132] A 2007-2020 business plan was appended.[133]

222. By way of this new amendment, the mandate period of ASTV was extended until 30 November 2020 (even though ASTV's current license expired in 2015).[134] It was also agreed to re-profile the K-coefficients negotiated in the 2002 Amendment as follows:

Year	2008	2009	2010	2011	2012	2013	2014
2002 Amendment K factor (%)	6.5	2	2	-	-	-	-
2007 Amendment K factor (%)	6.5	2	2	0	0	0	0

	2015	2016	2017	2018	2019	2020
2002 Amendment K factor (%)	-	-	-	-	-	-
2007 Amendment K factor (%)	0	0	0	0	0	0

223. As discussed below, this agreement on tariffs would remain unchanged, save for the 2010 K-coefficient, which in October 2009 ASTV agreed to set to zero (0).[135]

224. Finally, the 2007 Amendment reviewed the compensation scheme regarding the costs of the Network Expansion Programme but did not alter the schedule for the delivery of the works to be completed.[136]

[132] **C-32**, Agreement on Amending the Project Agreements (30 November 2007) [the "**2007 Amendment**"].

[133] **C-125**, ASTV Business Plan 2007 (30 November 2007).

[134] **C-32**, 2007 Amendment, Clause 2.1.1.

[135] **C-153**, Letter from ASTV to City of Tallinn (28 September 2009).

[136] **C-32**, 2007 Amendment, Clauses 3 and 4.

K) THE MINISTRY OF ENVIRONMENT'S DRAFT AMENDMENT TO THE 1999 PWSSA

225. On 12 January 2009, the Minister of Environment presented its proposed amendment to the Environment Committee of the Estonian Parliament and further held presentations in that respect with other Estonian officials and authorities, including the ECA.[137] Two (2) days later, the draft amendment was presented to the Ministry of Economic Affairs and Communications, which at the time had jurisdiction over the ECA.[138]

226. On 20 October 2009, the most recent version of the Ministry of Environment's draft amendment to the 1999 PWSSA was made publicly available on the website of the Central Government. A copy of the draft amendment was also communicated to various stakeholders, including the Estonia Homeowners' Association (the "**EOKL**"),[139] a not-for-profit organisation that receives funding from the Ministry of Economic Affairs and Communications and that advocates for Estonian landowners.

227. In contrast to the first draft amendment prepared by the Ministry of Environment, this amendment assigned the regulatory authority over water tariffs in large city areas to the ECA.[140]

L) THE STATEMENTS BY THE EOKL IN 2009

228. Throughout 2009,[141] the EOKL issued various public statements concerning the level of Estonian water tariffs. In a January 2009 press release, EOKL called for a reduction of ASTV's

[137] **R-152**, Session Minutes of the Environmental Committee of the Estonian Parliament (12 January 2009); **R-153**, Letter of the Ministry of Environment to the Ministry of Economic Affairs and Communications and the ECA (14 January 2009).

[138] **R-153**, Letter of the Ministry of Environment to the Ministry of Economic Affairs and Communications and the ECA (14 January 2009).

[139] Kroon 1st WS, ¶31; **RL-89**, Ministry of Environment's Draft Act Amending the PWSSA (2009), p 1.

[140] **RL-89**, Ministry of Environment's Draft Act Amending the PWSSA (2009), Clause 25: "The local government shall verify the compliance of the application to set prices with the legislation of the local government and with this Act, the public water supply and sewerage development plan and if the licensed territory of the water undertaking is situated in a waste water collection area with pollution load below 2,000 population equivalent then the unified methodology to calculate prices for water services. The approval process of the application to set prices depends on the water undertaking's licensed territory. If the licensed territory of a water undertaking is situated in a waste water collection area with pollution load of 2,000 population equivalent or more, the water undertaking shall submit the application to set prices, approved by the local government, in turn to the Competition Authority for approval before setting the prices for water services."

[141] It is to be noted that the EOKL had already issued a press release concerning ASTV's water tariff on 1 August 2008, **R-238**, Article by the EOKL "The mechanism of price increase in the City of Tallinn is inappropriate" published on Estonian Homeowners' Association website (1 August 2008).

tariffs.[142] Other public statements by the EOKL regarding ASTV's tariffs followed over the year of 2009.[143]

229. At the time, two (2) members of the EOKL's management board, Mr Ken-Marti Vaher and Mr Urmas Reinsalu, were members of the Estonian Parliament affiliated with the Ismaa-Res Publica coalition (the "**IRL**"), the party then in control of Parliament.[144]

M) END OF 2008 AND 2009: THE ECA'S INVESTIGATION AND ANALYSIS OF ASTV'S TARIFF

230. On 5 December 2008, the ECA issued a decree launching an investigation of the water and sewerage service market.[145]

231. For the purposes of its investigation, the ECA sought information from fifty (50) municipalities, including the City of Tallinn[146] which provided the requested information on 12 January 2009.[147]

232. In the context of its investigation, in February 2009, the ECA also requested detailed information from water utility companies, including ASTV, regarding their profits and accounting practices.[148]

233. Representatives of the ECA and of ASTV met on 3 March 2009.[149] On 25 March 2009, ASTV complied with ECA's request, noting at the same time that the information it provided was

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[142] The EOKL issued two (2) other press releases in January 2009 regarding water tariff policy.

[143] **R-120**, Article by the EOKL, "Homeowners Association's roundtable for water price regulation: the transfer of monopolies under the control of the Competition Authority" (26 January 2009); **C-143**, MTÜ Eesti Omanike Keskliit press release, "330 million profit from 400 [thousand] people" (23 January 2009); **C-144**, Various press articles (30 January 2009 to 23 November 2010), where the EOKL criticised ASTV's increased profits; **C-150**, Press article, "Reinsalu: Tallinna Vesi must be bridled fast" (27 April 2009), where Mr Reinsalu criticised ASTV's tariffs increase and payment of dividend; **C-145**, Press article, "Owners' Union is planning to take the dispute over water tariff to the court," where the EOKL disclosed that it will likely bring civil proceedings against ASTV and seek ECA's intervention, p 2617; **R-129**, Letter of the EOKL to the Harju County Governor (21 May 2009), where the EOKL requested that the Chancellor of Justice assess the legality of ASTV's tariffs; **C-154**, Blog post by Ken-Marti Vaher, "Responses to Anti-Monopoly Bill" (8 October 2009); **C-152**, Press article, "Homeowners Association: Tallinna Vesi should reduce its tariffs by at least 20%" (28 September 2009); **C-155**, Press article, "State is willing to take monopolies in hand" (13 October 2009).

[144] **C-36**, EOKL Commercial registry extract (2 December 2009). It is noted that Mr Vaher only became a member to the EOKL's management board in April 2009, Vaher 2nd WS, ¶7.

[145] **R-159**, ECA's Order No. 1.1-2/08-0001-061 (5 December 2008); **RL-27**, Estonian Competition Act of 2002, s. 55(2).

[146] **R-160**, Letter from the ECA to local municipalities (17 December 2008); **C-37**, ECA Information Request (12 February 2009).

[147] **R-162**, Letter from the City of Tallinn to ECA (16 January 2009).

[148] **C-37**, ECA Information Request (12 February 2009); **R-161**, Letter of the ECA to AS Tartu Veevärk (12 February 2009); **R-228**, Letter from the ECA to Esmar Ehitus OÜ (12 February 2009).

[149] Plenderleith, 1st WS, ¶57.

confidential and commercially sensitive "inside information" within the meaning of the Securities Market Act.[150]

234. On 3 April 2009, Mr Juhan Parts, the Minister for Economic Affairs and Communications, publicly criticised ASTV's level of profit and stated that the City of Tallinn had not been in a position to resist the increase of water tariffs owing to the terms of the Services Agreement. The Minister further announced that the tariff setting process was changing, referring to the Ministry of Environment's works on amending the 1999 PWSSA. On the same day, Mr Ots, director of the ECA, was reported to have stated that legislation supersedes contract but acknowledged that the ECA could only intervene in cases of "extremely high profitability."[151]

235. Representatives of ASTV and the ECA met during the fall 2009, in particular on 3 November 2009.[152]

236. On 30 November 2009, the ECA issued a report entitled "Analysis and Opinion on AS Tallinna Vesi' Price Formation" (the "**Analysis**") by which the ECA primarily attempted to determine "what would the prices applied by ASTV be in a situation, if the prices were controlled by an independent regulator following the recognised price regulations principles."[153] The ECA Analysis was said to be based on publicly available information.[154] The ECA nonetheless specified that the main conclusion of its preliminary analysis, which took into consideration non-public information, did not differ from the Analysis.[155]

237. The ECA Analysis assessed ASTV's price structure, as well as the notion of "justified profitability." For this purpose, the ECA relied on the return on invested assets methodology, which the ECA elected to base on the net book value (the "**NBV**") of ASTV's assets.[156] The ECA posited that ASTV's *allowed rate of return* ought to correspond to its weighted average cost of capital (the "**WACC**"), which it calculated to be 8.31%. The ECA compared this figure with ASTV's *actual rate of return* on invested assets, which it calculated to be of 16.9% for 2007 and 18.1% 2008. The ECA inferred from the difference between these "allowed" and "actual" rates that the City of Tallinn had failed to fulfil its responsibility as the regulator of water tariffs in Tallinn.[157]

238. The ECA further expressed concerns as to whether the water tariffs applied by ASTV were cost-based and compliant with the relevant law and regulations. It noted that ASTV had failed

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[150] **C-148**, Letter from ASTV to the ECA (25 March 2009).

[151] **C-149**, Press article, "The State bridles Tallinna Vesi's tariff policy" (3 April 2009).

[152] Ots 1st WS, ¶49; Plenderleith 2nd WS, ¶13.

[153] **C-38**, ECA's Analysis of Tariffs (30 November 2009), p 904 [the "**ECA Analysis**"].

[154] **C-38**, ECA Analysis, p 876.

[155] **C-38**, ECA Analysis, p 876.

[156] **C-38**, ECA Analysis, pp 901-903; see Ots 1st WS, ¶¶39-41.

[157] **C-38**, ECA Analysis, p 901: "From the data presented in Table 8 it concludes that the return on invested assets of ASTV in 2008 (18.1%) is considerably higher (18.1/8.31=2.18 times higher) than the company's weighted average capital cost that is taken as the basis in the formation of justified profitability, because WACC = 8.31%."

to provide the ECA with its calculations for water and wastewater services by price components and that it had not found any evidence that the City of Tallinn had conducted any detailed review of ASTV's costs.[158]

239. The ECA Analysis did not address either the terms of the Services Agreement, or, more generally, ASTV's privatisation and UUTBV's investment. Rather, the ECA took the position that its method of assessment of justifiable profitability was wholly incompatible with the Services Agreement.[159]

240. In transmitting its Analysis to ASTV, on 30 November 2009, the ECA recommended that ASTV look to the Tallinn City Government "in order to bring the price of water supply and sewerage services into compliance with the law."[160] The ECA informed ASTV that it intended to publish the Analysis and issue a press release no later than 10:00 the following morning.[161] It also invited ASTV to communicate its comments by 1 February 2010.

241. On 1 December 2009, Mr Ots, the ECA director, was reported to have stated that based on the ECA Analysis, water tariffs in Tallinn could be decreased by 25%, and that he had publicly recommended that ASTV submit a new tariff application to the City of Tallinn.[162]

242. Further to the communication of the ECA Analysis, representatives of ASTV met with the ECA, including on 4 January 2010.[163] ASTV explained its disagreement with the ECA's methodology for determining "justified profitability," which according to ASTV, failed to consider the appropriate period, failed to take into account the privatisation value of the company, and improperly disregarded the tariff-setting process adopted by the City of Tallinn.

243. On 1 February 2010, ASTV communicated to the ECA its position in writing regarding the ECA Analysis. ASTV refused to submit a new tariff application to the City of Tallinn to reduce its tariff on the ground that it would be in breach of both applicable legislation and the Services Agreement. ASTV further submitted to the ECA that the 1999 PWSSA neither defines "justified profitability" nor establishes any methodology for determining justified profitability.

244. Regarding the economic analysis performed by the ECA, ASTV submitted that it disregarded appropriate international standards in three (3) respects:

- The length of the regulatory period: the ECA would have wrongly based its analysis on data for only a two-year period, whereas data for a 3-5 year period would have been required;

[158] **C-38**, ECA Analysis, pp 881 and 882.

[159] **C-38**, ECA Analysis, p 903.

[160] **C-157**, Letter from Märt Ots to Ian Plenderleith (30 November 2009), p 2682.

[161] **C-157**, Letter from Märt Ots to Ian Plenderleith (30 November 2009), p 2682.

[162] **C-158**, Äripäev press article (2 December 2009).

[163] Plenderleith 1st WS, ¶¶65-77.

- The use of real or nominal returns: the ECA used nominal returns, without next taking into consideration the inflation rate in Estonia during the relevant period;

- The regulatory asset value: the ECA wrongly referred to ASTV's historic NBV without making any allowance for the capital invested on privatisation.[164]

245. ASTV closed its remarks by bringing to the ECA's attention that Estonia is signatory to several international treaties, including one (1) with UK, and that an "unbalanced approach to price regulation" could lead to a breach of Estonia's international obligations.

N) THE INVESTIGATION BY THE CHANCELLOR OF JUSTICE

246. In July 2009, concurrently with the ECA's investigation, Mr Indrek Teder, the then-Chancellor of Justice, launched an investigation on the legality of ASTV's tariffs under the 1999 PWSSA and the provisions of the Competition Act on abuse of dominant position.[165] Mr Teder seized himself of the matter after the Harju County Governor received an application from the EOKL to that effect.[166]

247. On 28 August 2009, Mr Teder sent a request for information to the City of Tallinn.[167] In its reply dated 23 October 2009,[168] the City of Tallinn explained that ASTV's water tariffs had been established in the Services Agreement and reported that, in a decision dated 17 September 2009,[169] ASTV's privatisation was deemed "non-satisfactory and detrimental to the interest of the City of Tallinn and its citizens."[170]

248. On 1 December 2009, the ECA transmitted the ECA Analysis to Mr Teder and invited him to issue an opinion on same.[171] Mr Teder next made a request for information to the ECA,[172] with which the ECA complied on 23 February 2010.[173] The ECA notably explained that the determination of tariffs by way of agreement, such as the Services Agreement, could not

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[164] **C-165**, Letter from ASTV to the ECA (1 February 2010).

[165] **R-131**, Letter of the Chancellor of Justice to the EOKL and the Harju County Governor (July 2009).

[166] The EOKL had initially applied to the Governor of the Harju County, **R-129**, Letter of the EOKL to the Harju County Governor (21 May 2009); **R-130**, Letter of the Harju County Governor to the Chancellor of Justice (17 June 2009).

[167] **C-151**, Letter from Chancellor of Justice to Edgar Savisaar, Mayor of Tallinn (28 August 2009).

[168] **R-132**, Letter of the City of Tallinn to the Chancellor of Justice (23 October 2009).

[169] **R-194**, Decision of the Tallinn City Council (17 September 2009). The City of Tallinn thereby states that it had been deprived from making management decision in some respects, criticizes the payment of dividend and reducing ASTV's capital share in 2002, and also states that the justified profitability rate agreed on was more than twice the profitability usually applicable to natural monopolies.

[170] **R-194**, Decision of the Tallinn City Council (17 September 2009), ¶1.

[171] **R-133**, Letter of the ECA to the Chancellor of Justice (1 December 2009).

[172] **R-134**, Letter of the Chancellor of Justice to the ECA (27 January 2010).

[173] **R-135**, Letter of the ECA to the Chancellor of Justice (23 February 2010).

satisfy the requirement of "justified profitability" of the undertaking prescribed by s. 14(3) of the 1999 PWSSA.

249. On 15 March 2010, after learning of the exchanges between the Chancellor of Justice and the ECA, ASTV transmitted additional comments to the Chancellor.[174]

250. On 23 March 2010, the Chancellor of Justice issued a recommendation to the City of Tallinn enjoining it to bring ASTV's tariffs into compliance with the applicable law.[175] The Chancellor of Justice stated that s. 14 PWSSA, and more specifically the phrases "cost-oriented" and "justified profitability," ought to be construed and applied according to general principles of competition law.[176] He acknowledged that in respect of the water industry, this would require modelling a competitive market. He concluded that, for the regulation adopted by a local government to be compliant with the law, the local government ought to define the phrases "cost-based" and "justified profitability" in a manner that lead to fair price by reference to prices in a real competitive market situation.[177] Relying on the ECA Analysis, he stated that the application by the City of Tallinn of the phrases "cost-based" and "justified profitability" breached the law and he requested that City Regulation No. 75 dated 30 September 2009 regarding water tariffs be modified accordingly.

251. The City of Tallinn refused to amend ASTV's water tariffs, claiming that the Chancellor of Justice had exceeded his jurisdiction. Most notably, the City asserted that Regulation No. 75 was an administrative act (as opposed to a legislative act of general application), the legality of which is not subject to review by the Chancellor of Justice.[178]

252. The Chancellor of Justice applied to the Supreme Court of Estonia for an order enforcing his recommendation. On 22 November 2010, the Court dismissed the application, holding that Regulation No. 75 was an administrative act over which the Chancellor had no authority.[179] In a press release regarding its decision, the Supreme Court noted, however, that such administrative act may be challenged before the Administrative Court.[180] The Chancellor of Justice closed his investigation but invited consumers to commence legal proceedings against ASTV. The EOKL began assembling potential claims in that respect.[181]

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[174] **C-167**, Letter from ASTV to Chancellor of Justice (15 March 2010).

[175] **C-168**, Proposal No. 8 from Chancellor of Justice (23 March 2010).

[176] **C-168**, Proposal No. 8 from Chancellor of Justice (23 March 2010), ¶¶13 and 14.

[177] **C-168**, Proposal No. 8 from Chancellor of Justice (23 March 2010), ¶18.

[178] **R-136**, Letter of the City of Tallinn to the Chancellor of Justice (14 April 2010).

[179] **C-192**, Decision of Estonian Supreme Court in case No. 3-4-1-6-10, "Petition of the Chancellor of Justice to declare invalid § 1 of regulation No. 75 of the Tallinn City Government" (22 November 2010).

[180] **R-329**, Press Release of the Estonian Supreme Court, "Supreme Court: The water prices in the City of Tallinn could have been challenged in the administrative court" (22 November 2010).

[181] Teder 1st WS, ¶19; **C-144**, Various press articles (30 January 2009 to 23 November 2010), p 2616; **C-193**, BNS article, "Teder: water tariff in Tallinn requires a court opinion" (22 November 2010).

O) THE 2009 AMENDMENT TO THE SERVICES AGREEMENT

253. In September 2009, the City of Tallinn, ASTV and UUTBV entered into a final amendment to the Services Agreement (the "**2009 Amendment**").[182] The Parties agreed to extend the duration of the Network Extension Programme to 31 March 2012 and to modify the payments to be made by the City of Tallinn in this respect.

P) THE ANTI-MONOPOLY BILL (AMB) AND THE ECA METHODOLOGY

254. In parallel with the ECA's Investigation,[183] Mr Reinsalu and Mr Vaher, both members of the IRL and EOKL,[184] drafted a proposed Anti-Monopoly Bill (the "**AMB**"). The AMB addressed issues pertaining to the heating and water tariffs from a consumer's perspective and sought, amongst other, to amend the 1999 PWSSA.[185]

255. In June 2009, Mr Vaher and Mr Reinsalu discussed ASTV's tariffs with the ECA. Mr Ots informed them that ASTV's actual profitability was 19.6%, whereas its justified profitability was 7-8%.[186]

256. On 8 October 2009, Mr Vaher presented the AMB to the Estonian Union of Cooperative Housing Association in the course of its annual forum.[187]

257. The AMB was introduced in the Estonia Parliament on 15 October 2009, shortly before the release of the ECA Analysis. The explanatory letter appended to the AMB (the "**AMB Letter**") stated that the objective of the AMB was to enhance consumers protection with regards to water and heating tariffs:

> The objective of this law is to amend the District Heating Act, Public Water Supply and Sewerage Act, Competition Act and Penal Code in such a manner as to ensure a higher protection of consumers in their relations with companies providing universal services and in a dominant position and in the price formation of their services.
>
> This will be achieved through:
>
> 1) Fixed justified rates of return,
>
> 2) Undertaking's obligation to initiate lowering prices if the input prices or other production costs change,

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[182] **C-33**, Agreement on Amending the Project Agreements (16 September 2009).

[183] See above at paragraphs 230-245 and ff.

[184] See above at paragraph 229.

[185] **C-39**, Explanatory Letter to the Draft AMB (15 October 2009) ["**AMB Letter**"].

[186] Vaher 1st WS, ¶36; Ots 1st WS, ¶66; this information was included in the letter introducing the bill to the Estonian Parliament on October 15, 2009, **C-39**, AMB Letter.

[187] **C-154,** Blog post by Ken-Marti Vaher, "Responses to Anti-Monopoly Bill" (8 October 2009).

3) The right of establishing temporary prices by the Competition Authority,

4) Full control of the Competition Authority over the heat producers,

5) Control of the Competition Authority over 52 larger water undertakings,

6) Stricter punishment for a significant violation of the requirements.[188]

258. The AMB Letter explicitly referred to ASTV – the only undertaking referred to by name in the Letter – as an example of how the 1999 PWSSA had failed to properly protect consumers:

> Poor protection of consumers' rights and not following the competition law has in more conspicuous cases led to a situation in which for example the productivity of the assets invested of the leading water undertaking of Tallinn is 19.6%. Taking as the basis the general European practice regarding the justified rate of profit of the water undertaking (7-8%), if the draft bill applies the price of water for the end consumer of Tallinna Vesi alone should reduce by ca 24% next year.
>
> Prices of these services influence significantly also consumer prices. Based on the earlier statistics of the Ministry of Finance, a reduction in the prices of Tallinna Vesi by ca 24% alone would bring about an estimated reduction in CPI by ca 0.2%.[189]

259. The most salient amendments put forward by the AMB were the following:

- The ECA, in lieu of municipalities, was to supervise the setting of tariffs of water undertakings servicing more than 2,000 people, which included ASTV. As a result, the concerned undertakings could only charge tariffs previously approved by the ECA;[190]
- The ECA would have jurisdiction to establish recommended principles for the calculation of water tariffs (the "**ECA Methodology**" or the "**Methodology**");[191]
- The water utilities company had to apply for new tariffs in cases of change of circumstances (including regarding costs and expenses).[192]

260. Under the AMB, water utilities companies were to apply the tariffs in force as at 31 October 2010 until the adoption of the ECA Methodology, and agreements entered into before 1

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[188] **C-39**, AMB Letter, p 908.

[189] **C-39**, AMB Letter, p 908. The figures referred to would have been provided by the ECA, Vaher 1st WS, ¶36.

[190] **RL-87**, Anti-Monopoly Bill (amending s. 142(1) of PWSSA) (3 August 2010), s. 2(9), amending s. 14^2 (1) of the 1999 PWSSA [AMB]; Vaher 1st WS, ¶30.

[191] **RL-87**, AMB, s. 2(9), amending s. 14^2 (9) of the 1999 PWSSA; Vaher 1st WS, ¶32.

[192] **RL-87**, AMB, s. 2(9), amending s. 14^2 (6) of the 1999 PWSSA.

November 2010 would remain in force if not contrary to the PWSSA.[193] The ECA would be allowed to order water utilities companies to bring their tariffs in compliance with the law before 1 November 2010 and would have the right to set temporary tariffs should the concerned water utility undertaking fail to make the necessary adjustments.[194]

261. The AMB was modified in two (2) significant respects prior to its adoption. First, the AMB initially set a maximum limit to "justified profitability," and this limit was removed.[195] Second, the phrase "justified profitability" was qualified by the addition of the words "*of the capital invested by the water undertaking.*"[196] This modification was proposed by the ECA for the purpose of clarifying that non-refundable aid would not be included in the assets base for calculating justified profitability.[197]

262. On 5 March 2010, a second version of the AMB Letter (the "**Second AMB Letter**") was submitted for the first parliamentary reading of the AMB. At the plenary session of Parliament, the draft AMB was merged with the draft amendment prepared by the Ministry of Environment.[198]

263. The AMB was enacted by the Estonian Parliament on 3 August 2010 and entered into force on 1 November 2010.[199]

Q) THE ECA METHODOLOGY

1) The Discussion regarding the Methodology

264. In May or June 2010, the ECA started developing the Methodology envisioned by the AMB.[200] On 7 September 2010, the ECA circulated a draft Methodology to various stakeholders, including ASTV and the City of Tallinn, and invited them to comment.[201]

265. ASTV and the City of Tallinn provided the ECA with their comments on 27 September 2010.[202] ASTV stressed the importance of considering the privatisation process of 2001 and recommended using the approach adopted by Ofwat, the English and Welsh regulator of water

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[193] **RL-87**, AMB, s. 2(15), amending s. 16 (6) of the 1999 PWSSA.

[194] **RL-87**, AMB, s. 2(14), amending s. 15^5 (1) and (2) of the 1999 PWSSA.

[195] Vaher 1st WS, ¶35.

[196] **RL-87**, AMB, s. 2(8), amending s. 14 (2)5) of the 1999 PWSSA.

[197] **R-124**, Amendment proposals to the AMB by the ECA (22 March 2010).

[198] Kroon 1st WS, ¶33; Vaher 1st WS, ¶41.

[199] **C-43**, PWSSA 2010, Amended 3 August 2010, p 1.

[200] Ots 1st WS, ¶73.

[201] **R-169**, Letter from the ECA to ASTV and the City of Tallinn (7 September 2010); **C-162**, ECA, "Recommended principles for calculating the price for water service" (2010).

[202] **C-178**, Letter from Ian Plenderleith to Märt Ots (27 September 2010).

sector. The City of Tallinn, for its part, referred the ECA to the terms of the Services Agreement and announced that it had commissioned an analysis by Oxera, an English consultancy firm.[203]

266. Representatives of the ECA and ASTV met in October 2010. Their disagreement concerning the relevance of the terms of the Services Agreement was evident.[204]

267. ASTV also provided to the ECA an accounting analysis of the ECA Methodology by PricewaterhouseCoopers (the "**PWC Report**"). PWC noted, *inter alia*, that the Methodology did not consider income tax, that the ECA used a nominal WACC and that the Methodology was based on the NBV of assets.[205]

268. The Estonian Water Companies Association (*Eesti Vee-Ettevõtete Liit*, "**EVEL**") submitted two (2) reports to the ECA, prepared by the accounting consultancy KPMG that raised similar concerns.[206]

269. On 25 October 2010, the ECA circulated a second draft of the Methodology.[207] In its comments on this new draft, the EVEL stated that the changes were only cosmetic.[208]

270. On 9 November 2010, the ECA adopted the Methodology further to the entry into force of the AMB on 1 November 2010. The Methodology was published on the ECA's website on 12 November 2010.[209]

271. On 15 November 2010, ASTV filed a complaint before the Chancellor of Justice for various breaches of due process by the ECA in its consultation regarding the Methodology.[210] On 12 April 2011, the Chancellor issued a recommendation to the ECA in which he concluded that the ECA had failed to properly explain the respective role of the participants in the consultation process.[211]

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[203] **C-179**, Letter from the City of Tallinn to the ECA (27 September 2010).

[204] Ots 1st WS, ¶77; Plenderleith 1st WS, ¶71.

[205] Plenderleith 1st WS, ¶¶101-106; **C-181**, PricewaterhouseCoopers Report on the ECA Proposed Methodology (22 October 2010).

[206] **C-177**, Letter from KPMG Baltic SIA to Estonian Water Works Association (24 September 2010); **C-182**, KPMG Baltic SIA report on the ECA's Proposed Methodology (26 October 2010).

[207] Ots 1st WS, ¶78.

[208] **C-183**, Letter from EVEL to Märt Ots (26 October 2010).

[209] **C-188**, ECA's Methodology (12 November 2010).

[210] **C-189**, Letter from ASTV to Chancellor of Justice (15 November 2010).

[211] **C-215**, Letter from Chancellor of Justice to ASTV (11 April 2011); **R-171**, Chancellor of Justice, "Recommendation to respect Lawfulness and Good Administration Practices" (12 April 2011).

272. On 8 December 2010, the ECA responded to the comments and opinions received regarding the Methodology.[212] It stated that water undertakings were required by law to justify the investments to be taken into consideration in the determination of tariffs and that guidelines shall not discriminate the water undertakings based on either their ownership or size.

273. On 10 December 2010, ASTV submitted a complaint against Estonia to the European Commission alleging that Estonia was violating the freedom of establishment and the freedom of capital guaranteed by the Treaty on the Functioning of the European Union ("**TFEU**") through the enactment of the AMB.[213]

2) The Methodology Adopted by the ECA

274. The ECA Methodology relies on two (2) principal notions: the value of the undertaking's *regulatory asset base* (the "**RAB**"), which is to be compared to a benchmark of justified profitability;[214] and the *nominal WACC*, which is used to define justified profitability.[215]

275. The Methodology defined the RAB as "the capital invested into the undertaking by the undertaker"[216] and provided that it was to be determined according to the formula below:

RAB = RABr + WC,

Where

RAB – regulated asset base;

RAB r – residual book value of RAB in the end of a regulation period;

WC – working capital.[217]

276. The Methodology specified that physical assets were to be assessed according to their NBV,[218] and that the working capital of a water utility company should be set at 5% of the value of the regulated assets.[219]

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[212] **R-32**, Explanations by the ECA to water undertakings regarding the "Recommended Principles of Water Service Price Calculation"; **C-164**, ASTV Quarterly Updates: Q2 2010, Q3 2010, Q4 2010, Q1 2011, Q2 2011, Q3 2011, Q4 2011, Q2 2012, Q3 2012, Q4 2012, Q3 2013 (2010-2013), p 2278.

[213] **C-196**, Complaint submitted by ASTV to the European Commission (10 December 2010).

[214] Ots 1st WS, ¶¶81-93.

[215] Ots 1st WS, ¶93.

[216] **C-188**, ECA's Methodology (12 November 2010), Clause 5.4.2.

[217] **C-188**, ECA's Methodology (12 November 2010), Clause 5.8.

[218] **C-188**, ECA's Methodology (12 November 2010), Clause 5.4.1.

[219] Ots 1st WS, ¶92; **C-188**, ECA's Methodology (12 November 2010), Clause 5.9.

R) ASTV'S TARIFF APPLICATION TO THE ECA

1) ASTV's 2011 Tariff Application

277. On 9 November 2010, the same day that the ECA adopted its Methodology, ASTV filed a tariff application with the ECA (the "**2011 Tariff Application**") by which ASTV sought approval of the tariffs for the years of 2011 to 2015, inclusively.[220]

278. In order to provide comfort as to ASTV's level of profitability, ASTV enclosed a report by Oxera on the estimated allowed revenues of ASTV.

279. The Oxera report adopted a "building block approach" aimed at capturing the main aspects of the methodology applied by Ofwat. The report only considered ASTV's revenues of 2010 and 2011 and assumed that the regulator would have considered ASTV's operating expenses appropriate. Oxera concluded that, since the privatisation, ASTV had under-recovered, based on a high level comparison of ASTV's regulatory capital value, set at the price paid by UUTBV at privatisation, and ASTV's so-called vanilla WACC, which accounts for the pre-tax cost of debt and post-tax cost of equity.[221] More specifically, Oxera assessed ASTV's allowed revenues for 2010-2011 to EEK 764 million. Oxera acknowledged that the NBV method could also be used to assess allowed revenues but stated that this method does not align with the Ofwat principles:

> For 2010-11, the allowed revenues are estimated to be EEK 764m. This result is highly sensitive to a number of assumptions described in section 3, and in particular the opening RCV [Regulatory Capital Value]. As described in the earlier sections, the opening RCV relies on the assumption that the replacement cost of ASTV's assets was greater than the value inferred from the price paid at the time of privatisation. An alternative could be to use the net book value of assets at the time of privatisation, but this would be out of line with the real Financial Capital Maintenance approach adopted by Ofwat.[222]

280. On 17 November 2010, the ECA informed ASTV that the 2011 Tariff Application suffered from deficiencies that prevented it being considered.[223] The ECA notably stated that it was not open to ASTV to apply for a tariff increase for the period of 2011 to 2015 and that the 2011 Tariff Application did not allow for a proper assessment of ASTV's costs.[224] The ECA closed by enjoining ASTV to cure the listed deficiencies by 13 December 2010, to use the ECA's questionnaire developed for the purposes of tariffs application and to provide the financial data for the previous three (3) financial years so as to allow for the assessment of the justifiability of the costs and revenues to be included in the tariff submitted for approval.[225]

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[220] **C-187**, Letter from ASTV to the ECA, enclosure: 2011 Tariff Application (9 November 2010).

[221] **R-172**, Oxera Consulting Ltd, "Estimating allowed revenues for ASTV" (3 November 2010).

[222] **R-172**, Oxera Consulting Ltd, "Estimating allowed revenues for ASTV" (3 November 2010), p 9.

[223] **C-190**, Letter from the ECA to ASTV (17 November 2010).

[224] **C-190**, Letter from the ECA to ASTV (17 November 2010), pp 3198 and 3199, 3200 and 3201.

[225] **C-190**, Letter from the ECA to ASTV (17 November 2010), pp 3201-3202.

281. Representatives of ECA and ASTV met the following day. It appears that Mr Ots informed ASTV that pursuant to the applicable law, a tariff application could not cover a five-year period and that, although the fulfilling of ECA's questionnaire was mandatory, the ECA Methodology was merely a recommendation.[226]

282. ASTV and the ECA continued to exchange correspondence over the following six (6) months.[227]

283. On 2 December 2010, ASTV resubmitted a further tariff application.[228] ASTV stated that the 2010 PWSSA did not prevent establishing tariffs over several years, namely for the 2011-2015 period.[229] ASTV also acknowledged not having followed the ECA Methodology but stated that its application and the information provided to ECA were sufficiently detailed for the ECA to discharge its supervisory role.[230]

284. On 15 January 2011, after additional exchanges, the ECA agreed to initiate a formal review of ASTV's application.[231]

285. On 28 February 2011, the ECA informed ASTV of its intention to reject its tariff application and offered ASTV the opportunity to respond by 15 March 2011. The ECA also notified ASTV that it had initiated an investigation into ASTV's existing tariffs.[232]

286. The ECA stated that ASTV's tariffs may only be assessed by reference to the PWSSA, and not the agreements between the company and the City of Tallinn.[233] The ECA excluded the possibility that tariffs might be set for the period 2011 to 2015 because it would not be possible

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[226] Plenderleith 1st WS, ¶112; **C-191**, Minutes of Meeting between ASTV and the ECA (18 November 2010). Mr Plenderleith also testifies that Estonia took the same position before the European Commission. During this meeting, Mr Ots agreed to explore the establishment of a multi-year tariff application, see **C-191**, Minutes of Meeting between ASTV and the ECA (18 November 2010), pp 320 and 3205.

[227] **C-195**, Letter from ASTV to the ECA (2 December 2010); **C-197**, Letter from the ECA to ASTV (13 December 2010); **C-199**, Letter from ASTV to the ECA (23 December 2010); **C-200**, Letter from ASTV to ECA (28 December 2010); **C-205**, Minutes of meeting between the ECA and ASTV (3 January 2011); **C 206**, Letter from ASTV to the ECA (11 January 2011); **C-207**, Letter from ASTV to the ECA (14 January 2011); **C-208**, Letter from the ECA to ASTV (9 February 2011); **C-209**, Letter from the ECA to ASTV (28 February 2011); **C-201**, ASTV Annual Report 2010; **C-211**, Letter from the ECA to ASTV (2 March 2011); **C-212**, Letter from the ECA to ASTV (1 April 2011); **C-214**, Letter from ASTV to the ECA (5 April 2011).

[228] **C-195**, Letter from ASTV to the ECA (2 December 2010).

[229] **C-195**, Letter from ASTV to the ECA (2 December 2010), p 3224, referring to s. 14 of the PWSSA.

[230] **C-195**, Letter from ASTV to the ECA (2 December 2010), p 3229: "Although our tariff application does not follow the recommended methodology and application forms published on the CA's webpage, we have submitted a detailed and professional tariff application, based on a building block model, which has been verified by international experts and is in compliance with the requirements set out in §14² (1) of the PWSSA, and which enables the CA in every way to perform the obligation imposed to it by the PWSSA, i.e. to check, whether the applied tariffs contain only the justified costs and justified profits as set out in PWSSA § 14(2)."

[231] Ots 1st WS, ¶105.

[232] **R-173**, Letter from the ECA to ASTV (28 February 2011).

[233] **R-173**, Letter from the ECA to ASTV (28 February 2011), p 43 of the pdf.

to forecast costs over such a long period.[234] The ECA also refused to consider the privatisation value in the determination of ASTV's RAB[235] and held that tariff increases could not be set solely as a function of the CPI, but must be fact-based.[236] The ECA further informed ASTV that justified profitability is to be assessed according to the "*capital invested*" and disagreed with ASTV's use of the "*ordinary*" WACC, as opposed to nominal WACC. Finally, the ECA requested that ASTV comply with its guidelines published in January 2011.[237]

287. On 29 March 2011, ASTV communicated to the ECA an updated application, in which it restated that the determination of its tariffs ought to consider the privatisation agreements as well as the privatisation value.[238]

2) The ECA's Rejection of the 2011 Tariff Application, and the ECA Prescription

288. On 2 May 2011, the ECA dismissed the 2011 Tariff Application on the ground that the tariff increases sought by ASTV did not comply with the 2010 PWSSA.[239]

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[234] **R-173**, Letter from the ECA to ASTV (28 February 2011), p 45 of the pdf: "The KA has the opinion that the approval of the water service price for the period of 2011 to 2015 with a prescribed specific annual price increase does not comply with the ÜVVKS because the ÜVVKS prescribes neither the approval of the price for a certain period nor an annual price increase. The expenses prescribed by ÜVVKS § 14 (2) as the basis for calculating the water service price are dynamic in time, due to both the undertaking's activities and factors beyond the undertaking's control (for example, the pollution charge rates or the water resource charge rates). An undertaking cannot forecast its expenses so clearly in long term, the more so that some of the changes related to expenses may stem from law amendments. An undertaking cannot foresee the long-term changes in the economy that may affect the water service price, particularly concerning the expenses, the rates of which depend on the legislator's will (the pollution charge rates or the water resource charge rates). Due to that and pursuant to ÜVVKS § 14^2 (6), a water undertaking is required to monitor the circumstances which are independent of its activities and affect the price of water services and is required to notify the Competition Authority of any circumstance that may affect the price of water services by more than 5 per cent no later than thirty days as of the occurrence thereof. Therefore, the approval of the water service price for a longer period, in this case for the years 2011-2015, and the prescribing of a specific increase of the water service price by the water undertaking are excluded for objective reasons."

[235] **R-173**, Letter from the ECA to ASTV (28 February 2011), p 57 of the pdf: "ASTV's approach where the value of regulated assets is derived from the undertaking's value agreed between two parties cannot be considered justified. If following ASTV's principle, the aforementioned transaction would cause an increase of the water service price for consumers because the value of regulated assets increases. Yet, no improvements were made in ASTV's public water supply and sewerage system (no new investments were made), only the owner changed. Pursuant to ÜVVKS § 14 (2), a change in the water service price can take place only on the basis of expenses made for the public water supply and sewerage system. Thus there is no basis for changing the water service price only for the reason that the owner changes, i.e. it is not compliant with the law to base the calculation of the water service price on the amount paid upon privatising ASTV."

[236] **R-173**, Letter from the ECA to ASTV (28 February 2011), p 58 of the pdf.

[237] **R-173**, Letter from the ECA to ASTV (28 February 2011), p 61 of the pdf.

[238] **R-243**, Letter of ASTV to the ECA (29 March 2011).

[239] **C-42**, ECA's Decision No. 9.1-3/11-002 (2 May 2011).

289. In its rejection letter, the ECA valued ASTV's RAB at EUR 135.116 million, as compared with the EUR 353 million value calculated by ASTV.[240] According to the ECA, the RAB was to be calculated by determining the NBV and could not be derived from a contract or from privatisation value. The ECA also raised the following issues:

- Even if the privatisation value method were adopted, ASTV's RAB calculation was inflated by EUR 44 million by not accounting for the funds invested in 2001 to reduce its debt;
- ASTV's application unduly adjusted the RAB annually by the change of CPI;
- The calculations of the WACC;
- ASTV's failure to comply with the requirement to progressively eliminate price discrimination between private and commercial clients;
- ASTV's application of pollution charges, which it claimed were a result of ASTV's breach of environmental law;
- ASTV's operating costs included write-offs of receivables resulting from non-paying customers.[241]

290. On 26 June 2011, the Ministry of Economic Affairs and Communication addressed a letter to ASTV's shareholders stating that (i) neither the Ministry nor the ECA had been involved in the privatisation, and (ii) the statutory regime in force at the time of the privatisation only allowed the setting of tariffs to the level necessary for ensuring a reasonable return on capital invested. The Ministry also invited the shareholders to stop depicting Estonia as an unsafe country for foreign direct investment and to bring their claim to a third party, should they believe that they were the victims of some illegality.[242]

291. On 10 October 2011, the ECA concluded its investigation into ASTV's tariffs. It issued an order, Prescription No. 9.2-3/11/11-001 (the "**ECA Prescription**"), compelling ASTV to apply for tariffs 29% lower than its 2010 tariffs.[243]

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[240] **C-42**, ECA's Decision No. 9.1-3/11-002 (2 May 2011), pp 957 and 959.

[241] **C-42**, ECA's Decision No. 9.1-3/11-002 (2 May 2011); Ots 1st WS, ¶¶107-111.

[242] **C-217**, Letter from the Ministry of Economic Affairs and Communications to ASTV's shareholders (6 June 2011).

[243] **C-44**, ECA's Prescription No. 9.2-3/11-001 (10 October 2011). The ECA then acted pursuant to sections 16(6) and $15^5(1)$ of the 2010 PWSSA.

S) THE ESTONIAN PROCEEDINGS

292. On 1 June 2011, ASTV challenged the rejection by the ECA of its 2011 Tariff Application before the Tallinn Administrative Court (the "**Main Estonian Case**"), and sought the following remedies:[244]

1) to annul the ECA's decision of 2 May 2011 rejecting the 2011 Tariff Application;

2) to declare that s. 14 (2)5) of the 2010 PWSSA is unconstitutional and that it does not apply to ASTV in the context of these judicial proceedings;

3) to find that the ECA violated the Services Agreement in rejecting the 2011 Tariff Application by way of its 2 May 2011 decision;

4) to compel the ECA to fulfil the Services Agreement;

5) to compel the ECA to review the 2011 Tariff Application.

293. On 10 October 2011, the day that the ECA Prescription was issued, ASTV also challenged the legality of the ECA Prescription before the Tallinn Administrative Court. On 11 November 2011, the Court granted a temporary interim injunction suspending the ECA Prescription.[245] On 6 February 2012, the same court issued an interim injunction suspending the ECA Prescription pending the outcome of the Main Estonian Case, and this proceeding was merged with the Main Estonian Case.[246]

294. On 31 May 2012, the Tallinn District Court ruled in the Main Estonian Case that the provisions of the Services Agreement regarding tariff setting constitute an administrative act under Estonian law.[247]

295. On 10 September 2012, ASTV filed a complaint with the Ministry of Economic Affairs and Communication claiming that the ECA and its general director, Mr Ots, discriminated against ASTV in its tariff review as compared to its review of tariffs of Kunda Elamu ("**Kunda**"), a heating company in the city of Kunda:[248] whereas the ECA refused to consider the privatisation value in ASTV's application, it factored in the investment made in connection with Kunda's privatisation. ASTV also alleged that Mr Ots had a personal interest in Kunda.[249] ASTV's claim was dismissed on 18 December 2012. The Ministry found no conflict of interest and explained

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[244] Case No. 3-11-1355; **RL-167**, Tallinn Administrative Court Decision in the Main Estonian Case on the Merits of 12 October 2015 ["**Tallinn Administrative Court Decision of 12 October 2015**"].

[245] **R-197**, Order of the Tallinn Administrative Court in case No. 3-11-2632 (11 November 2011).

[246] **RL-167**, Tallinn Administrative Court Decision of 12 October 2015.

[247] **C-228**, Decision of the Tallinn District Court in administrative matter No. 3-11-1355, "AS Tallinna Vesi's complaint requesting the court to annul the 02.05.2011 decision No 9.1-3/11-002 of the Competition Authority" (31 May 2012).

[248] **C-230**, Letter from ASTV to the Ministry of Economic Affairs and Communications (10 September 2012).

[249] **C-231**, Directive issued by the Ministry of Economic Affairs and Communications (18 December 2002).

that Kunda was privatised through an asset purchase, which warrants a different treatment than a share-purchase transaction such as ASTV's privatisation.[250]

296. In 2013,[251] 2014[252] and 2015, ASTV made further applications for water tariffs to the ECA. The ECA refused to review those applications, and ASTV sought the annulment of the decisions pertaining to the 2013 and 2014 tariffs before the Tallinn Administrative Court. ASTV further filed a claim for compensation for the damages incurred or to be incurred as a result of the rejection of ASTV's applications, in the amount of EUR 10.8 million for damages already incurred, and EUR 80.8 million for future damages.[253]

297. On 5 June 2015, the Tallinn Court of Administration dismissed all of ASTV's claims in the Main Estonian Case [254] and released its reasons on 12 October 2015.[255] The Court found that:

- ASTV had not raised the issue of whether the ECA was bound by the Services Agreement during the application process, and the ECA did not have to consider the obligations arising out of the Services Agreement;[256]

- The Services Agreement had not been transferred to the ECA, and the ECA was not party to said contract. Accordingly, the ECA had no obligation towards ASTV under the Services Agreement;[257]

- The Tallinn City Council had failed to set a proper method to determine tariffs because the 22 December 1999 Regulation No. 47 merely repeated the 1999 PWSSA wording and the Tallinn City Government did not have the authority to adopt the formula set out in the Services Agreement as the method for setting tariffs;[258]

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[250] **C-231**, Directive issued by the Ministry of Economic Affairs and Communications (18 December 2002), p 3710: "When approving the maximum price for a company that has purchased the necessary assets for producing heat or providing water services, the value of the assets on the balance sheet of the company that bought the assets as stated before shall be proceeded from. Usually for the buyer of assets, the purchase cost of the assets is equal to the book value of the assets (which must not get confused with the so-called historic, earlier book value of assets). In case of such transactions as the CA has explained the reasonableness of asset value is checked based on ratios in the similar manner with other price components (ratio of asset value to the volume of sld heat, comparison with different companies)."

[251] Case No. 3-14-363.

[252] Case No. 3-14-51519.

[253] Case No. 3-14-403.

[254] **R-174**, Decision of the Tallinn Administrative Court in case No. 3-11-1355 (5 June 2015).

[255] **RL-167**, Tallinn Administrative Court Decision of 12 October 2015.

[256] **RL-167**, Tallinn Administrative Court Decision of 12 October 2015, ¶18, p 29.

[257] **RL-167**, Tallinn Administrative Court Decision of 12 October 2015, ¶¶20-25.

[258] **RL-167**, Tallinn Administrative Court Decision of 12 October 2015, ¶26, p 35.

- The AMB only clarified the principles applicable to the determination of tariffs;[259]

- The AMB was introduced for the purposes of enhancing consumers' protection and due to substantial public interest;[260]

- ASTV had failed to demonstrate that the price formula of the Services Agreement was cost-based and to refute the ECA's reasons for rejecting its application.[261]

298. The Court refrained from making any finding on the ECA's allegations that the Services Agreement was unlawful and null.[262]

299. On 11 November 2015, ASTV lodged an appeal of this decision, which was dismissed by the Tallinn Circuit Court on 26 January 2017.[263]

300. The Tallinn Circuit Court found that:

- The tariff part of the Services Agreement constituted a regulation of specific application directed at a particular undertaking and was governed by the provisions on public law contract;[264]

- ASTV and the City of Tallinn could only have had for legitimate expectation a level of justifiable profitability protected by law and there was no evidence that calculating justified profitability by using the capital invested did not ensure ASTV's justified profitability;[265]

- There was no ground to establish the nullity of the tariff part of the Services Agreement, as suggested by the ECA, the Services Agreement could be performed until the entry into force of the AMB;[266]

- Further to the entry into force of the AMB, the justified profitability could no longer be calculated by reference to the privatisation value since the phrase "justified profitability" had been qualified with the phrase "of the capital invested by the undertaking";[267]

- The ECA was not bound by the terms of the Services Agreement and ASTV could no longer demand performance of the Services Agreement after the amendment of the

[259] **RL-167**, Tallinn Administrative Court Decision of 12 October 2015, ¶27.

[260] **RL-167**, Tallinn Administrative Court Decision of 12 October 2015, ¶37.

[261] **RL-167**, Tallinn Administrative Court Decision of 12 October 2015, ¶31, p 39.

[262] **RL-167**, Tallinn Administrative Court Decision of 12 October 2015, ¶25, p 35.

[263] **C-432**, Tallinn Circuit Court Decision of 26 January 2017.

[264] **C-432**, Tallinn Circuit Court Decision of 26 January 2017, ¶18.

[265] **C-432**, Tallinn Circuit Court Decision of 26 January 2017, ¶21.

[266] **C-432**, Tallinn Circuit Court Decision of 26 January 2017, ¶19.

[267] **C-432**, Tallinn Circuit Court Decision of 26 January 2017, ¶¶22 and 26.

PWSSA in 2010 as it would run afoul the predominant public interest that the 2010 PWSSA seeks to protect;[268]

- The ECA had implicitly terminated the Services Agreement by virtue of its rejection of the 2011 Tariff Application and the Services Agreement could not be enforced because it contradicted the terms of the Methodology;[269]

- The Estonian legislator had granted the ECA the discretion to set the recommended principles for the calculation of water tariffs. As such, it was not open to interfere with the ECA's choice of methodology and the Methodology could not violate specific rights if it provides for cost-based tariff and allows justified profitability;[270]

- ASTV had been provided with the opportunity to express its opinion in the elaboration of the Methodology and the ECA did not have to account for the Services Agreement in that respect;[271]

- To accept the 2011 Tariff Application would have required deviating from the Methodology in several respects and the ECA did not use its discretion unjustifiability by rejecting it.[272]

301. ASTV appealed from the District of Tallinn Court's decision[273] and, as mentioned above, the Supreme Court of Estonia issued its decision on 12 December 2018.

302. The Supreme Court partly reversed the District of Tallinn Court's decision by only allowing ASTV's complaint with respect to clause 6 of the ECA Prescription, which conditions the application of the order to the ECA's approval of ASTV's novel application.[274] The Supreme Court's judgment leaves intact the remainder of the ECA Prescription.

303. The Supreme Court further found as follows:

- The Services Agreement is a public law contract, which has been entered into *in lieu* of an administrative act and Schedule E Part I of the Services Agreement is part of the resolution contained in a public law contract.[275]

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[268] **C-432**, Tallinn Circuit Court Decision of 26 January 2017, ¶20.

[269] **C-432**, Tallinn Circuit Court Decision of 26 January 2017, ¶20.

[270] **C-432**, Tallinn Circuit Court Decision of 26 January 2017, ¶22.

[271] **C-432**, Tallinn Circuit Court Decision of 26 January 2017, ¶23.

[272] **C-432**, Tallinn Circuit Court Decision of 26 January 2017, ¶24.

[273] Claimants informed the Tribunal of ASTV's intention in their post-hearing brief, Cl. PHB, ¶579a.

[274] Supreme Court Decision (12 December 2017), ¶¶48-51.

[275] Supreme Court Decision (12 December 2017), ¶17.

- The Services Agreement continued to be effective after the entry into force of the amendments to the 1999 PWSSA.[276]

- The Services Agreement cannot be deemed void from its inception.[277]

- The ECA did not legally succeed to the City of Tallinn since the 1999 PWSSA modified the duties of the water tariffs regulator.[278] As of consequence, the ECA would have terminated the Services Agreement.[279]

- The 1999 PWSSA further rendered the compliance with the Services Agreement impossible because the 1999 PWSSA introduced a change by forbidding reference to the privatisation value for calculating justified profitability.[280]

- The amendments to the 1999 PWSSA neither breached ASTV's legitimate expectations,[281] nor EU law.[282]

- The Methodology is an administrative regulation, for the purpose of which the ECA was afforded a wide discretion. Since the tariff calculation it sets out constitutes one (1) of the possible options, the Methodology is valid.[283]

- The ECA rightfully rejected ASTV's 2011 Tariff Application and issued the Prescription due, *inter alia*, to the impossibility to calculate water tariffs based on the privatisation value.[284]

T) ASTV'S COMPLAINT BEFORE THE EUROPEAN COMMISSION

304. As mentioned above,[285] ASTV filed a complaint before the European Commission on 10 December 2010 on the grounds that, by enacting the AMB, Estonia breached the principles of freedom of establishment (Art. 49 TFEU) and of free movement of capital (Art. 63 TFEU).

305. On 26 September 2011, the European Commission issued a pre-closure letter stating that the AMB did not violate the principles of freedom of establishment or freedom of movement of

[276] Supreme Court Decision (12 December 2017), ¶18.

[277] Supreme Court Decision (12 December 2017), ¶19.

[278] Supreme Court Decision (12 December 2017), ¶20.1.

[279] Supreme Court Decision (12 December 2017), ¶20.3.

[280] Supreme Court Decision (12 December 2017), ¶24.

[281] Supreme Court Decision (12 December 2017), ¶25.

[282] Supreme Court Decision (12 December 2017), ¶27.

[283] Supreme Court Decision (12 December 2017), ¶¶29-34.

[284] Supreme Court Decision (12 December 2017), ¶¶35-43.

[285] See above at paragraph 273.

capital.[286] According to the Commission, Estonia had discretion to change the water tariff regime, the AMB did not affect the stability of regulatory regime and was not discriminatory, ASTV's investors could not have had any legitimate expectation regarding the changeability of the regulatory system since the Services Agreement had to comply with the PWSSA, and, even if the Services Agreement was binding on the ECA, it could not take precedence over the PWSSA as amended.

306. On 14 May 2014, the Commission issued a closure letter confirming its previous assessment that the AMB was not contrary to EU law.[287]

V. SUMMARY OF THE PARTIES' CLAIMS AND REQUESTS FOR RELIEF

A) CLAIMANTS' POSITION

307. It is Claimants' principal case that Estonia has breached a number of Claimants' legitimate expectations arising out of the privatisation, and as such, has breached its obligation under the BIT to afford them fair and equitable treatment ("**FET**").[288] Claimants also claim that Estonia's failure to afford them due process and the negative publicity campaign against them in which Estonia engaged constitute further FET breaches. Claimants claim as well that Estonia has breached its obligation under the BIT to not impair their investment by unreasonable or discriminatory measures and has also breached the BIT's umbrella clause.[289]

308. According to Claimants, Estonia's breaches prevented and prevent Claimants from recouping their investment of EUR 85 million made at the time of ASTV's privatisation in 2001.

1) The Breach of Claimants' Legitimate Expectations Arising Out of the Privatisation

309. According to Claimants, as of 2001, they had for legitimate expectations that the privatisation agreements would be observed and that water tariffs for the years after 2005 would be set by reference to the 2001 Business Plan or, alternatively, that these tariffs would be determined by following the tariff methodology set out in the Services Agreement.[290]

310. These expectations arose in the course of and against the backdrop of ASTV's privatisation, including the negotiation, drafting process and terms of the privatisation agreements as well as the involvement of the EBRD and the Estonia Central Government in the privatisation.

311. Claimants argue that the purpose of ASTV's privatisation was to secure long-term investment, which had become necessary due to the dire state of the water and sewerage system in Tallinn, and that the City of Tallinn was seeking to bring in an experienced international

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[286] **C-219**, Pre-closure letter issued by the European Commission in response to ASTV's Complaint (26 September 2011).

[287] **R-198**, Closure letter of the Commission (14 May 2014).

[288] Cl. Mem., ¶¶109-113; Cl. Reply, ¶¶ 59-65.

[289] Cl. Mem., ¶¶216-225; Cl. Reply, ¶¶299-320, 324-391.

[290] Cl. Reply, ¶¶59-68.

operator to remediate to the situation. The privatisation also had as its objective the release of the State Guarantee, to the benefit of the Central Government of Estonia. Claimants also rely on the structure of the bidding process: since bidders were required to bid on only two (2) elements, the share price and the K-coefficients, and UUTBV's bid linked these elements, it was entirely legitimate for Claimants to expect that the proposed tariff increases would be followed. Also material to Claimants' case is what they assert was the express approval of the 2001 Business Plan by the City of Tallinn and the City's recognition that UUTBV was investing on this basis.[291]

312. More specifically with regards to the tariffs for the years beyond 2005, Claimants state that the Central Government of Estonia expressly granted an extended licence period on the understanding that such extended period was required for UUTBV to earn a return on its investment. Claimants rely also on the discussion and negotiations pertaining to "*justified profitability*" and the detailed provisions on same included in the 2001 Business Plan.[292]

313. In their Post-Hearing Brief, Claimants particularise their legitimate expectations as of 2001 as follows:

> a. that the contracts entered into by the City of Tallinn with the Government's knowledge on 12 January 2001, in reliance on which UUTBV invested €85 million in ASTV, would be respected;
>
> b. in the five year Initial Period, that ASTV's tariffs would be set by reference to the specific K factors bid by UUTBV and incorporated into the Services Agreement;
>
> c. that in setting the K factors for subsequent Operating Periods any consideration of justified profitability would be by reference to the tariff methodology in the Services Agreement and the Business Plan submitted at the time of UUTBV's bid, not on the basis of a clean slate which took no account of the Services Agreement, the privatisation, or the €85 million investment UUTBV made on the basis of them; and
>
> d. the key principles of the regulatory framework applicable to ASTV, as set out in the Services Agreement, would not be radically overturned during its term. In spite of the absence of an express stabilisation clause in the Services Agreement, the Claimants could legitimately expect that the fundamental basis of the tariff methodology envisaged in the Services Agreement would be maintained and would not be unreasonably and arbitrarily undone during the term of that agreement. This is so regardless of the existence of certain provisions in the Services Agreement relating to future regulatory change.[293] [Footnotes omitted]

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[291] Cl. Mem., ¶110; Cl. Reply, ¶60.

[292] Cl. Mem., ¶111.

[293] Cl. PHB, ¶97.

314. These expectations were reinforced, if not strengthened, in the course of ASTV's operations over the 2001-2009 period.[294] Reference is made to the reconfirmation of the Services Agreement's tariff methodology through its various amendments, the 2002 EBRD Loan and the EBRD's involvement in ASTV as an indirect investor from 2003 to 2010, and the delivery by ASTV of the required improvement to the Service Levels. Claimants further stress that ASTV achieved lower profitability in eight (8) years than it had been projected to achieve in the first five (5) years.

315. Estonia breached these expectations by adopting the AMB, by the rejection by the ECA of the 2011 Tariff Application and, later, by ordering ASTV to lower its tariff by 29% pursuant to the ECA Prescription. These breaches amount to a violation of FET.[295]

2) The Other Alleged FET Breaches, and Unreasonable and Discriminatory Measures

316. Claimants also assert that Estonia failed to afford them due process, and thus breached its obligation to provide FET, and adopted unreasonable and discriminatory measures in contravention to its international law obligations. The key elements of Estonia's unfair treatment would lie in:

a) the negative campaign against ASTV instigated by the EOKL;

b) the ECA's market investigation in 2009, in the course of which the ECA allegedly did not afford ASTV due process;

c) alleged flaws in the ECA Analysis;

d) the alleged targeting of ASTV in the adoption of the AMB.

317. With respect to the EOKL's conduct, Claimants emphasise that the organisation focused on ASTV's profitability as opposed to the affordability of its services.[296]

318. Concerning the ECA's conduct, Claimants argue that the agency wrongly disregarded the privatisation agreements and the privatisation as a whole in its analysis. The ECA also failed to address the flaws in its approach identified by Claimants at the relevant times and by relying on a flawed methodology.[297]

319. Claimants assert that the adoption of the AMB was specifically directed at ASTV, with the intention of forcing it to lower its tariffs.[298] This is evidenced by the fact that the AMB was sponsored by two (2) IRL members who were also members of the EOKL's management board, by the fact that the preliminary calculations of the ECA were used to justify the AMB,

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[294] Cl. PHB, ¶¶217-225.

[295] Cl. Mem., ¶¶193-197; Cl. PHB, ¶¶366-386.

[296] Cl. PHB, ¶¶302-305.

[297] Cl. PHB, ¶¶323-332, 362-365.

[298] Cl. PHB, ¶¶310-319.

and by the specific references to ASTV in the AMB's preparatory works. Furthermore, the modification of the term "justified profitability" was specifically directed at ASTV so as to prevent any consideration of the capital invested in ASTV by its shareholders. The reliance by the ECA on the modified wording of "justified profitability" in rejecting the 2011 Tariff Application also demonstrated that the Estonian authorities targeted ASTV by means of the regulatory reform of water tariffs.[299]

320. It is also Claimants' case that the AMB as adopted and applied to ASTV did not in fact derive from the concerns and reform proposals regarding the country's water undertakings. Rather, the proposals predating the AMB expressly concerned the problem of tariffs that were *too low* to ensure the sustainability of water and sewerage services.[300]

3) The Breach of the Umbrella Clause

321. In addition to the aforementioned breaches, Claimants allege that Estonia breached its obligations under Article 3(4) of the BIT, an umbrella clause, by failing to observe:

a) The tariff methodology in the Services Agreement and the commitment in Clause 7 to calculate tariffs in accordance with this methodology;

b) The contractual commitment in s. 5.5.8 of the Shareholders' Agreement requiring the City of Tallinn to make reasonable efforts to ensure the fulfilment of the 2001 Business Plan;

c) The commitment in the Letter of Understanding by which the City of Tallinn agreed to make its best efforts to ensure the implementation of the 2001 Business Plan;

d) Article 4.1.2 of the 2007 Amendment to the Services Agreement, which required that the process for determining the K factors as the basis for ASTV's tariffs would not be applicable until 1 July 2020; and

e) Article 6.2 of the 2007 Amendment which required the Parties to ensure that the conclusion of the 2007 Amendment will not reduce the shareholder value of ASTV.[301]

4) The Claimants' Prayer for Relief

322. As articulated in their Reply and updated in their Post-Hearing Brief, Claimants seek the following remedies:

a) A declaration that the Tribunal has jurisdiction over the claims brought by both ASTV and UUTBV in these proceedings;

b) A declaration that Estonia has breached Article 3(1) of the BIT by failing to ensure fair and equitable treatment to the Claimants' investments;

[299] Cl. PHB, ¶¶341-354, 370-372.

[300] Cl. PHB, ¶¶294-297.

[301] Claimants' Skeleton Argument, ¶92; Cl. Mem., ¶¶224 and 225; Cl. Reply, ¶¶361-399.

c) A declaration that Estonia has breached Article 3(1) of the BIT by taking unreasonable and/or discriminatory measures that have impaired the Claimants' operation, management, maintenance, use, enjoyment and/or disposal of their investments;

d) A declaration that Estonia has breached Article 3(4) of the BIT by failing to observe obligations entered into with regard to the Claimants' investments;

e) A declaration that Estonia's breaches of the BIT have caused loss and damage to both ASTV and UUTBV;

f) An order that Estonia compensate ASTV by payment of a sum equivalent to the value as at the date of the Tribunal's Award of the revenue that ASTV:

(i) has lost up to that date; and

(ii) assuming a continuation of the *status quo*, will lose, through to the end of the Services Agreement;

being a total of EUR 67.5 million as at December 2015 and a total of EUR 65 million as at December 2016;

g) In the alternative to (f) and in the event the Tribunal concludes it has no jurisdiction over ASTV, an order that Estonia compensate UUTBV by payment of a sum equivalent to the value as at the date of the Tribunal's Award of the appropriate proportion (that attributable to UUTBV's shareholding) of ASTV's residual cash flows which, but for Estonia's breaches of the BIT, would have been generated by ASTV;

h) An order requiring Estonia to pay interest on any sums it orders Estonia to pay pursuant to sub-paragraphs (f) and (g) above, from the date of the Tribunal's Award through to the date of payment;

i) An order that Estonia pay the cost of these arbitration proceedings, including the fees and expenses of the ICSID Secretariat, the Tribunal and costs of the Claimants' legal representation and interest thereon; and

j) An order that Estonia pay all other costs incurred by the Claimants as a result of its breaches of the BIT and interest thereon in accordance with the BIT.[302]

B) RESPONDENT'S POSITION

323. Respondent raises three (3) objections to the Tribunal's jurisdiction, and further denies having breached any of its international obligations.

1) Respondent's Objections to Jurisdiction[303]

324. First, Respondent contends that the Tribunal lacks *ratione personae* jurisdiction over the claims brought by ASTV, in that ASTV does not qualify as a Dutch national pursuant to the

[302] Cl. Reply, ¶608; Cl. PHB, ¶¶576-581.

[303] As further exposed below at paragraphs 339 and following, Claimants submit that the Tribunal has jurisdiction over their claims insofar that (i) ASTV benefits from the protection of the BIT since UUTBV has exercised a sufficient degree of control over ASTV during the relevant period, (ii) the Estonian proceedings commenced by ASTV do not seek the same remedies than the current arbitration and, as such, does not

BIT and the ICSID Convention. More specifically, Estonia claims that UUTBV never exerted sufficient control over the management, as opposed to the operations, of ASTV; alternatively, any such control would vest, not in UUTBV, but in its parent company, a UK national.[304]

325. Second, Respondent contests the Tribunal's *ratione voluntatis* jurisdiction. It alleges that Claimants are barred from bringing the current arbitral proceedings considering that ASTV seeks equivalent remedies before the Estonian courts. A finding of jurisdiction over Claimants' claims would thus violate Article 26 of the ICSID Convention, pursuant to which parties' consent to submit a dispute to the Centre is deemed to be consent to the exclusion of any other remedy.[305]

326. Third, Respondent argues that the Tribunal lacks jurisdiction because of the incompatibility of the BIT with EU law.[306]

2) Respondent Denies Having Breached any of its International Obligations

a) Claimants cannot Claim any Legitimate Expectations regarding Water Tariffs beyond 2005

327. According to Respondent, Claimants could not have had for legitimate expectations that ASTV's water tariff would be set by reference to the 2001 Business Plan, as said plan was intended only to set tariffs for the years of 2001-2005. Respondent particularly stresses that the Services Agreement did not benefit from any insulation from regulatory changes: the terms of the Services Agreement were subordinated to the applicable law, which was defined as including any amendments to the existing regulatory regime, and envisioned the transfer of authority over water tariffs to an entity other than the City of Tallinn. The 2001 Business Plan also could not ground any legitimate expectation since bidders were informed that the business plan included in the bid would not be evaluated in determining the winning bidder, and the Services Agreement referred to a business plan as only one of three (3) factors to be weighed in ascertaining justified profitability.[307]

328. Respondent further notes the distinction between the various privatisation agreements. It underlines that only the City of Tallinn and ASTV, but not UUTBV, executed the Services Agreement. Moreover, although the City executed the Services Agreement in its capacity as the local government regulator of water tariffs, its intervention in the other agreements, including the Shareholders' Agreement to which was appended the 2001 Business Plan, was

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preclude the Tribunal from ascertaining its jurisdiction and (iii) the arbitration agreement contained in the BIT is not incompatible with EU law.

[304] Resp. Rej., ¶¶226-296.

[305] Resp. Rej., ¶¶297-323.

[306] Resp. Rej., ¶¶324-352.

[307] Resp. Rej., ¶¶115-120.

as a commercial party, and the terms of those agreements did not involve and could not preclude the City from using its regulatory powers.[308]

329. Respondent also disputes the materiality of any involvement by the Central Government of Estonia or the EBRD in ASTV's privatisation.[309] The Central Government was not involved in the tender process and did not review the terms of the privatisation, the objectives of which in any case did not include the release of the State Guarantee given the good financial standing of ASTV at time.

330. In any event, says Estonia, any of Claimants' legitimate expectations arising from the privatisation were undermined by subsequent events. These include the 2001 dividend payment and capital restructuring, by which UUTBV largely recouped its investment, and the fact that ASTV never made any application for tariffs relying on the Services Agreement's tariff mechanism. In addition, Estonia emphasises that both the 2002 Amendment and the 2007 Amendment increased ASTV's profitability. Respondent further contends that these amendments were illegal under Estonian law.[310]

b) The AMB's Regulatory Reform and the ECA's Measures Do Not Violate FET

331. Respondent submits that the amendments to the 1999 PWSSA introduced by the AMB and the ECA's decisions that ensued were all bona fide regulatory measures.

332. The proposed reforms and the AMB were aimed at depoliticising the setting of water tariffs, a nation-wide problem, notably by removing the larger cities' authority over this matter and transferring it to an independent State agency. Furthermore, the AMB did not modify, but merely clarified, the existing tariff-setting rules.[311]

333. According to Respondent, the measures adopted by the ECA were in accordance with the applicable law. The rejection of the 2011 Tariff Application and the adoption of the ECA Prescription merely sought to reduce ASTV's monopolistic profits to a reasonable level.[312] It explains that the ECA had discretion to specify a tariff mechanism in the Methodology and that such Methodology accords with Estonian law and international best practices.[313] As for the rejection of the 2011 Tariff Application, Respondent underscores that the application did not make any explicit reference to the Services Agreement and that it was economically flawed.[314]

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[308] Resp. C-M, ¶¶96-115; Cl. Reply, ¶¶87, 88, 95-99, 100-107, 117.

[309] Resp. C-M, ¶¶47-50; Resp. Rej., ¶¶20-38.

[310] Resp. Rej., ¶¶121-124, ¶¶132-135, ¶¶167-170.

[311] Resp. C-M, ¶¶217-221; Resp. Rej., ¶¶200-205.

[312] Resp. Rej., ¶¶353-442.

[313] Resp. PHB, ¶¶219-232.

[314] Resp. PHB, ¶¶233-247.

334. It is also Respondent's position that Claimants were afforded due process in their exchanges with the ECA as the latter complied with the applicable law.[315]

c) Estonia's Conduct did not Breach its International Obligations in any other Manner

335. Respondent denies having instigated any negative media or other campaign against Claimants, let alone one for which it could be held internationally liable.[316] According to Estonia, not only can the EOKL's conduct not be attributed to the Estonian State, but its statements regarding ASTV's tariffs themselves reflected growing public criticism long before the advent of the AMB.[317]

336. Finally, Respondent alleges that Claimants' umbrella law clause claims must fail for four reasons. First, the alleged contractual commitments of the City of Tallinn were subject to law and regulatory action and were not binding on the ECA. Second, the 2007 Amendment was unlawful to the extent that it is interpreted as fixing tariffs for a period of thirteen (13) years. Third, the 2007 Amendment did not create international obligations for Estonia because the City of Tallinn is distinct from the Estonian State. Fourth, the claim obviously fails with respect to UUTBV insofar that it is not privy to the Services Agreement.[318]

VI. JURISDICTION

337. As noted above at paragraphs 324-326, Respondent raises three (3) objections to the jurisdiction of the Tribunal:

a) ASTV is not a Dutch national under the BIT and the ICSID Convention;

b) The Tribunal lacks *ratione voluntatis* jurisdiction over Claimants' claims;

c) The BIT is incompatible with EU law.

338. Each of these objections is dismissed for the reasons set out below. Although these matters were not contested, the Tribunal also finds that all other conditions for it to have jurisdiction are met, including that the claims submitted to arbitration pertain to an investment and are directed against a party to the ICSID Convention, and that UUTBV is a Dutch national.

A) THE JURISDICTION OF THE TRIBUNAL OVER ASTV'S CLAIMS

339. Respondent posits that ASTV fails to meet the nationality requirements under the BIT and the ICSID Convention. ASTV (an Estonian entity) it says, is not actually controlled by UUTBV (a Dutch national); and, in any event, UUTBV could not be a source of jurisdiction because it is merely a shell company and is not the ultimate controller of ASTV.

[315] Resp. Rej., ¶¶433-439.

[316] Resp. Rej., ¶¶443-446.

[317] Resp. Rej., ¶¶190-199.

[318] Resp. Rej., ¶¶447-492.

340. After considering relevant texts (1), the Tribunal will identify the point(s) in time at which control of UUTBV over ASTV must be established (2), decide whether UUTBV indeed controlled ASTV (3) and then consider the impact of the fact that UUTBV is itself controlled by a non-Dutch entity (4).

1) The Relevant Texts

341. It is undisputed that, for the Tribunal to have jurisdiction over ASTV's claims, ASTV must fulfil the jurisdiction requirements of both the ICSID Convention and the BIT.

342. Art. 25 of the ICSID Convention sets out the nationality prerequisites for the Centre's jurisdiction:

> (1) The jurisdiction of the Centre shall extend to any legal dispute arising directly out of an investment, between a Contracting State (or any constituent subdivision or agency of a Contracting State designated to the Centre by that State) and a national of another Contracting State, which the parties to the dispute consent in writing to submit to the Centre. When the parties have given their consent, no party may withdraw its consent unilaterally.
>
> (2) "National of another Contracting State" means:
>
> […]
>
> (b) any juridical person which had the nationality of a Contracting State other than the State party to the dispute on the date on which the parties consented to submit such dispute to conciliation or arbitration and any juridical person which had the nationality of the Contracting State party to the dispute on that date and which, because of foreign control, the parties have agreed should be treated as a national of another Contracting State for the purposes of this Convention. [Emphasis added]

343. As for the BIT, the nationality requirement is addressed at Art. 1 and 9:

> Article 1
>
> For the purposes of the present Agreement: […]
>
> (b) the term "nationals" shall comprise with regard to either Contracting Party:
>
> […]
>
> iii. legal persons not constituted under the law of that Contracting Party but controlled, directly or indirectly, by natural persons as defined in (i) or by legal persons as defined in (ii) above.
>
> Article 9

> (1) Each Contracting Party hereby consents to submit any legal dispute arising between that Contracting Party and a national of the other Contracting Party concerning an investment of that national in the territory of the former Contracting Party to international conciliation or arbitration. […]
>
> (4) A legal person which has the nationality of one Contracting Party and which, before such a dispute arises, <u>is controlled by nationals of another Contracting Party, shall for the purpose of article 25 (2)(b) of the Convention referred to in paragraph (3) above be treated as a national of that Contracting Party</u>. [Emphasis added]

344. The Parties agree that, as regards jurisdiction over a legal person incorporated under the laws of the host State, Art. 25 of the ICSID Convention establishes a two-part test comprising a subjective prong and an objective prong:

345. <u>First</u>, the Contracting States to the ICSID Convention must have agreed to treat certain juridical persons as foreign nationals notwithstanding that these persons are nationals of the host State of an investment (*i.e.* the **subjective** test arising out of the phrase "which … the parties have agreed should be treated as a national of another Contracting State for the purposes of this Convention"). <u>Second</u>, the party bringing a claim against a Contracting State must meet the applicable nationality requirements (*i.e.* the **objective** test arising out of the phrase "*because of foreign control*").[319]

346. It is common ground that Art. 9(4) of the BIT, whereby Respondent consented to the jurisdiction of the Centre, combined with the submission by Claimants of their Request for Arbitration on 13 October 2014 fulfil the subjective test for jurisdiction.[320] The Parties further agree that Claimants bear the burden of demonstrating that ASTV should be deemed to be a foreign – *i.e.*, Dutch – national by virtue of its control by UUTBV.[321]

2) The Time when Foreign Control Must Be Established

347. The Parties disagree as to the moment when control over ASTV must be established.

348. Respondent contends that, for the Tribunal to have jurisdiction over ASTV's claims, UUTBV must have controlled ASTV uninterruptedly from the beginning of the alleged violations of the Treaty in 2009,[322] to the filing of Claimants' Request for Arbitration on 13 October 2014. Respondent further states that Claimants must offer evidence that ASTV was under UUTBV's control (i) before the dispute arose, (ii) at the time of each of the alleged breaches of Estonia's

[319] **RL-103**, *National Gas S.A.E. v Arab Republic of Egypt*, ICSID Case No. ARB/11/7, Award (3 April 2014), ¶¶131-133 [*National Gas*].

[320] Resp. C-M, ¶258.

[321] Cl. Reply, ¶404.

[322] Respondent refers to Claimants' allegations of unfair treatment starting in 2009 (Cl. Mem., ¶¶152 and ff.).

treaty obligations and (iii) at the date of the consent to arbitration (*i.e.* the date of the filing of the Request for Arbitration).[323]

349. Claimants posit that the critical date for establishing control is the date of consent. They do not specifically engage as to whether control must be established before this time. In their view, this issue is academic because UUTBV's control over ASTV would not have materially changed since the privatisation of ASTV.[324]

350. Construction of the relevant texts facilitates the resolution of this issue.

351. The ICSID Convention does not contain any specific requirement regarding the ratione temporis jurisdiction of the Centre, except that the wording of Art. 25 of the ICSID Convention makes clear that control must exist at least at the time of consent to submit a dispute to conciliation or arbitration.

352. For its part, the BIT specifies at Art. 9(4) that the relevant nationality must be established "before such dispute arises," without further precision.

353. A reading of the BIT nonetheless confirms that the benefits of the instrument, including its dispute settlements provisions, are inextricably tied to the nationality of the purported protected investor. Pursuant to Art. 2 of the BIT, the Contracting Parties undertake to foster and protect investments of "nationals of the other Contracting Party" within their respective territory. Similarly, the preamble states that the Treaty aims at intensifying the Contracting Parties' relationships "with respect to investments by the nationals of one Contracting Party in the territory of the other Contracting Party." Art. 9(1) also refers to disputes pertaining to the "investment of that national."

354. Not requiring from a purported foreign investor to demonstrate that it meets the nationality criterion at the time of the alleged breach of the Treaty would run afoul of the clear intent of the BIT's signatories, that is, to promote "investments by the nationals of one Contracting Party in the territory of the other Contracting Party." In other words, the phrase "before such dispute arises" should be tied to the alleged breach of the investment protections afforded by the BIT.

355. Claimants must thus establish that ASTV was a Dutch national not only at the time of consent to the October 2014 which is unchallenged, but also before the dispute arose, that is when the alleged breaches of the BIT first occurred.

356. Claimants allege that ASTV became the target of a negative public relations campaign by various Estonian stakeholders and authorities starting in 2009 and culminating in the adoption of the AMB in 2011 and ultimately in the ECA's rejection of ASTV's 2011 Tariff Application in May of that year.

[323] Resp. C-M, ¶267; Resp. Rej., ¶241.

[324] Cl. Mem., ¶¶262-268.

357. It is Claimants' case that Respondent failed to afford them due process and otherwise violated the FET standard, in breach of the BIT, beginning in 2009, which as mentioned culminated in the adoption of the AMB and subsequent rejection of ASTV's 2011 Tariff Application.[325]

358. Considering that the various alleged breaches are said to have begun in 2009, Claimants must demonstrate that UUTBV had control over ASTV as of that time as well as on 13 October 2014.

3) UUTBV's Control of ASTV

359. The Tribunal will first lay out the applicable legal standard (a) and the relevant facts (b). It will then consider the relevance of the Estonian law evidence pertaining to control presented by Respondent (c) before discussing its analysis and conclusions (d).

a) The Applicable Legal Standard

(i) Claimants' Position

360. Claimants are of the view that the notion of control under both the ICSID Convention and the BIT is broad: "control" was intentionally left undefined in the ICSID Convention, and the Treaty does not prescribe its ambit. They further stress that the determination of control consists in a factual inquiry to be made on the basis of all facts at hand.

361. According to Claimants, shareholding is not in and of itself dispositive of the issue of control; other factors, such as voting and management rights, must also be taken into account. Establishing control over an entity does not require demonstrating absolute control. Evidence of a "dominant influence" suffices.[326]

362. Claimants challenge the relevance for the notion of control of EU and Estonia law and submit that, in any event, ASTV meets the Estonian law test for control as elaborated by Respondent's Estonia law expert (addressed at paragraphs 402-410 below).[327]

(ii) Respondent's Position

363. Respondent criticises Claimants for failing to identify an objective standard for control and for failing to identify a case where factors other than shareholding formed the basis of a tribunal's assertion of jurisdiction over a domestic entity. In Respondent's contention, such other factors may be relied on merely to rebut or bolster a presumption of control where a foreign party holds a majority shareholding over the domestic entity.

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[325] Cl. Mem., ¶¶152-207.

[326] Cl. Reply, ¶¶411-416 and 465; see also: Cl. PHB, ¶¶522-525.

[327] Cl. Reply, ¶409.

364. Respondent submits that control must be defined by reference to general principles of company law[328] and that, for this purpose, reference should be made to Estonian and EU law.[329] Respondent relies on Mr Vallikivi's expert evidence in this regard.

b) Meaning of Control in International Investment Law

365. The ICSID Convention does not specify the meaning of control. Nor does the BIT contain an autonomous definition of control; its language mostly mirrors the ICSID Convention's. The BIT does, however, specify that, when the putative foreign investor is incorporated under the law of the host State, such control may be "direct or indirect."[330]

366. The Tribunal agrees with Claimants that control is a flexible concept, which can only be determined case by case in the light of the particular facts. This derives from the will of the drafters of the ICSID Convention not to constrain the notion of "foreign control."[331] This need for flexibility arises from the complexity of ascertaining control over a juridical person. As noted by Professor Schreuer, ICSID tribunals have adopted different approaches to determining whether a party controls a national of the host State.[332] By way of illustration, the tribunal in *Vacuum Salt v Ghana* noted that Art. 25(2)(b) does not specify any particular percentage of share ownership and concluded that each case "must be viewed in its own particular context."[333]

367. Attempting to circumscribe the meaning of control through the identification of essential factors, or bright-line rules, thus appears unnecessary, if not inappropriate. Doing so could prevent tribunals from fulfilling their duty to conduct a full factual and legal assessment of the case at hand and could unduly curtail the scope of their jurisdiction and thus deprive parties of the protections that the ICSID Convention and the relevant treaty intended would inure to their benefit.

368. Bearing in mind that the determination of control is context-specific, it is nonetheless appropriate to consider how international tribunals and scholars have approached the issue. Various principles can be gleaned from the authorities submitted by the Parties.

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[328] **RL-224**, Zachary Douglas, *The International Law of Investment Claims* (Cambridge: Cambridge University Press, 2012).

[329] See Resp. C-M, ¶¶270-286; Resp. Rej., ¶¶231-236.

[330] This will be commented when addressing whether UUTBV must be the ultimate controller of ASTV to ground the Tribunal's jurisdiction over the claims of ASTV (see ¶¶442 and ff.).

[331] **CL-113**, *History of the ICSID Convention*, Vol. II, pp 359, 360, 448, and 870.

[332] **CL-100**, Christoph H. Schreuer, *The ICSID Convention: A Commentary*, 2nd ed, ¶¶850-852 [Schreuer, *The ICSID Convention*].

[333] **CL-3**, *Vacuum Salt v Ghana*, ICSID ARB/92/1, Award (16 February 1996), ¶43 [*Vacuum Salt v Ghana*]. See also **CL-6**, *Autopista v Venezuela*, ICSID Case No ARB/00/5, Decision on Jurisdiction (7 September 2001), ¶113 [*Autopista v Venezuela*].

369. A majority shareholding may give rise to a presumption of control, but such presumption may be rebutted in the light of other circumstances.[334] Conversely, it was envisioned in the course of the ICSID Convention's drafting that a minority holding of as little as 25% or 15% might suffice to establish control if coupled with a capacity to block major changes.[335] That being said, not any substantial minority shareholding should be considered as "control."[336] Reference is also frequently made to other factors, including voting rights and contractual arrangements such as shareholders' agreements.[337]

370. The particular nature of the influence exerted by the foreign person over the domestic entity may be considered in the assessment. For instance, Professor Schreuer suggests that "a joint venture in which the foreign investor and local interests hold equal shares <u>may be under effective control of the foreign partner due to the latter's management and know-how</u>" [emphasis added].[338] On the other hand, in *Vacuum Salt v Ghana*, the tribunal stated that control over purely technical matters by a foreign minority shareholder did not suffice to attract jurisdiction under the relevant treaty. The reasons of the tribunal suggest that a "material influence" would be necessary to ground control.[339]

371. Professor Schreuer thus explains that what might be called a "holistic" approach is to be preferred:

> On the basis of the Convention's preparatory works as well as the published cases, it is possible to conclude that the existence of foreign control is a complex question requiring the examination of several factors such as equity participation, voting rights and management. In order to obtain a reliable picture, all these aspects must be looked at in conjunction.[340]

372. The paramount concern in conducting such an inquiry lies in ensuring that a domestic investor does not improperly avail itself of the protections offered foreign investors by the ICSID Convention and the relevant treaty.

373. As for joint control, the tribunal in *Sempra v Argentina* considered that joint control of a domestic entity by several foreign investors constitutes foreign control, whereas joint control

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[334] **RL-117**, *Aguas del Tunari, S.A. v Republic of Bolivia*, ICSID Case No. ARB/02/3, Decision on Respondent's Objections to Jurisdiction, ¶264 [*AdT v Bolivia*]; **CL-8**, *Caratube International Oil Company LLP v Republic of Kazakhstan*, ICSID Case No. ARB/08/12), Decision on the Annulment Application of Caratube International Oil Company LLP, ¶¶273-274 [*Caratube v Kazakhstan*].

[335] **CL-100**, Schreuer, *The ICSID Convention*, *supra* note 332, ¶851.

[336] **CL-100**, Schreuer, *The ICSID Convention*, *ibid*, ¶865.

[337] **CL-6**, *Autopista v Venezuela*, *supra* note 333, ¶113; **CL-8**, *Caratube v Kazakhstan*, *supra* note 334, ¶254.

[338] **CL-100**, Schreuer, *The ICSID Convention*, *supra* note 332, ¶850.

[339] **CL-3**, *Vacuum Salt v Ghana*, *supra* note 333, ¶53.

[340] **CL-100**, Schreuer, *The ICSID Convention*, *supra* note 332, ¶864.

by a foreign person and national of the host State is not foreign control and does not, as of consequence, give rise to jurisdiction:[341]

> 51. The pertinent question is whether a foreign investor can add to its own participation in a local company an additional percentage belonging to another foreign investor so that their combined weight will thereby achieve the necessary control. Of course, combination of the participation of a foreign investor with that of a local investor should be excluded, since in that case, although the combination could result in control, this would not be foreign control.

374. Similarly, Professor Schreuer opines that joint control of a domestic entity by foreign shareholders from different Contracting States to the ICSID Convention "should be admitted in principle." Where both foreign and host State nationals exercise a degree of control, he suggests that in order to find "foreign" control, "[t]he combined control of nationals of Contracting States other than the host State should, at least, outweigh the combined control of nationals of non-Contracting States and of the host State."[342]

c) The Relevant Facts regarding Control over ASTV

375. Respondent does not expressly deny that UUTBV enjoyed operational control over ASTV.[343] The matter in its view turns rather on whether UUTBV held strategic control over UUTBV at the relevant time and whether such control, if any, was joint with the City of Tallinn.

376. The Tribunal notes that Respondent argues that any alleged control by UUTBV over ASTV prior to 2009 has no bearing on the issue because nationality must be assessed at the time of the alleged violation.[344] The history of control over ASTV nonetheless provides relevant insight on the role played by UUTBV in the operation and management of ASTV, and will be reviewed below.

(i) <u>Control over ASTV as discussed and negotiated during the privatisation process</u>

377. It appears unchallenged that the privatisation of ASTV had as one key objective to bring in an international water and sewerage operator. This notably stems from the criteria set in the

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[341] **RL-115**, *Sempra Energy International v the Argentine Republic*, ICSID Case No. ARB/02/16, Decision on Objections to Jurisdiction (11 May 2005), ¶51; see also **RL-116**, *Camuzzi International S.A. v the Argentine Republic*, ICSID Case No. ARB/03/2, Decision on Objections to Jurisdiction (11 May 2005), ¶38.

[342] **CL-100**, Schreuer, *The ICSID Convention*, *supra* note 332, ¶865.

[343] Resp. PHB, ¶255; Mr Vallikivi, expert for Respondent, recognises that UUTBV enjoys operational control of ASTV through ASTV's management board, Vallikivi 2nd ER, ¶32.

[344] Respondent refers to **RL-108**, *Société Générale in respect of DR Energy Holdings Limited and Empresa Distribuidora de Electricidad del Este, S.A. v Dominican Republic*, UNCITRAL, Award on Preliminary Objections to Jurisdiction (19 September 2008), ¶106 and **RL-107**, *Guardian Fiduciary Trust, Ltd, f/k/a Capital Conservator Savings & Loan, Ltd v Former Yugoslav Republic of Macedonia*, ICSID Case No. ARB/12/31, Award (22 September 2015), ¶106, where an ICSID tribunal interpreted the Dutch-Macedonia BIT, which contains a provision similar to Art. 9(4) of the Treaty.

Tender Notice, which disqualified any domestic Estonian investor insofar as any bidder ought, at the date of its application, to:

> a. [Exercise] management control in a company (or itself a company) supplying water and sewerage services to at least 500,000 inhabitants.
>
> b. <u>[Exercise] management control in water and/or wastewater companies in at least four (4) different countries</u>, whereas at least in one of these companies the period of management control must have minimum three (3) years.
>
> c. [Have] had [an] annual average turnover from provision of water services or from activities directly related to water services of at least EEK 300,000,000 (three hundred million), or the equivalent amount thereof in local currency over the last three (3) years.[345] [Emphasis added]

378. Further, review of the history of the negotiations shows that the issue of control over ASTV by the foreign investor was material, indeed central, to the privatisation.

379. Under the proposed transaction, the City of Tallinn would detain the B-share and associated veto rights over certain matters at the General Meeting (ASTV's highest governing body).[346] On the other hand, the Information Memorandum also announced that the investor would gain management control over ASTV *via* a majority on the Supervisory Council and the right to appoint the Management Board of ASTV.[347]

380. In October 2000, and as mentioned at paragraph 163 above, UUTBV raised specific concerns regarding the veto rights provided in the Articles of Association and in the draft Shareholders' Agreement. UUTBV stressed the importance to it of enjoying and exercising control over ASTV's affairs.[348] These concerns were addressed by amendments to the draft Shareholders'

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[345] **C-12**, Notice of Tender (26 June 2000).

[346] **C-9**, Minutes of the meeting of the City of Tallinn committee for preparing and implementing the tender (20 April 2000) and Explanatory Memorandum (5 March 2000), p 152: "In addition to the shareholders' agreement, the City maintains control over the activities of the company through the issued preferred share or the so-called 'golden share'."; **C-11**, Tallinn City Council Resolution No. 210 – ASTV Articles of Association (15 June 2000), ss. 3.2.1.2 and 6.2.8; this understanding was confirmed by Mr Mõis during his cross-examination, Tr. Day 1 Mr Mõis 225:10-226:1.

[347] **C-10**, ASTV Information Memorandum (3 July 2000), p 165; see also p 223 ("It is envisaged that the Strategic Investor will have management and operational control in the Company, whilst some limited number of matters being subject to veto by the City of Tallinn.").

[348] **C-66**, Letter from UUTBV to Suprema (9 October 2000), pp 1413 and 1414; **C-70**, Letter from UUTBV to Suprema (23 October 2000), p 1432: "We would like to make it clear that, in our view, the Investor cannot be expected to make such a major investment in the Company if the Investor is not be allowed to control its operations, even if its future liability is limited. Particularly regarding contracts, IWUU would find it unacceptable for the City to block the placement of legitimate contracts, which would therefore put the Company in breach of its service and quality obligations – whether future liability were to be limited or not. As Investor, IWUU would need to have the freedom to run the Company as it sees fit. The City must trust the Company to a certain extent and not seek to involve itself in the normal management affairs of the Company. IWUU would find the original control requirements of the City, including many of the restrictions

Agreement, though the Articles of Association, including the rights attached to the B-share, remained unchanged in these respects.[349]

(ii) Control over ASTV after the Privatisation

381. ASTV is managed through three (3) directing bodies: the General Meeting (i), the Supervisory Council (ii), and the Management Board (iii).[350]

- *The General Meeting*

382. The General Meeting, the highest governing body of ASTV,[351] has jurisdiction over the most critical corporate matters, including approval of the company's annual reports, the distribution of profits and the appointment of the members of the Supervisory Council.[352]

383. The City holds the single B-share and, as a result, a veto right over certain matters decided at the General Meeting, pursuant to both the Articles of Association and the Shareholders' Agreement. The Articles of Association provide that the B-share grants to its holder a veto over the following matters:

- The amendment of the Articles of Association of ASTV;
- The increase or decrease of the share capital of ASTV;
- The issuing of convertible bonds;
- The acquisition of treasury shares by ASTV;
- The decision on the merger, division, transformation and/or dissolution of ASTV;
- The issues pertaining to the operation of ASTV submitted to the General Meeting by either the Management Board or the Supervisory Council.[353]

384. Pursuant to the Shareholders' Agreement, the City of Tallinn also holds a veto right regarding:

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imposed by the Articles of Association, to be quite unacceptable and would be unable to bid on that basis. We therefore urge you to ensure that the provisions for the City to veto Company management decisions are set at an acceptable (i.e. substantially reduced) level, and that the Articles of Association are amended accordingly."

[349] **C-71**, Email from Tim Lowe to David Kerr and others (24 October 2000); this also appears from a comparison of the Shareholders' Agreement in its final form, **C-20**, and the list of issues identified by UUTBV in its correspondence of 9 October 2000 to Suprema, **C-66**.

[350] **C-11**, Tallinn City Council Resolution No. 210 – ASTV Articles of Association (15 June 2000), s. 6.1.

[351] **C-11**, Tallinn City Council Resolution No. 210 – ASTV Articles of Association (15 June 2000), s. 6.2.1.

[352] **C-11**, Tallinn City Council Resolution No. 210 – ASTV Articles of Association (15 June 2000), s. 6.2.6.

[353] **C-11**, Tallinn City Council Resolution No. 210 – ASTV Articles of Association (15 June 2000), s. 6.2.8.

- The issue by ASTV of any securities giving their holder the right to vote and/or the right to acquire shares and/or other securities of ASTV in the future including any increase of ASTV's share capital or issue of convertible bonds;

- The distribution of ASTV's profits for the years of 2000, 2001 and 2002;

- Any transaction of a substantial nature or having a substantially similar effect to any of the above or any agreement or proposal to do any of the above.[354]

385. Yet, at the same time, the City of Tallinn undertook in the Shareholders' Agreement not to unreasonably withhold its consent regarding matters falling under the General Meeting's jurisdiction, provided that ASTV's affairs are conducted in compliance with certain standards.[355]

386. The evidence is that the City never sought to exercise the prerogatives attached to the B-share. According to Mr Plenderleith, who acted as ASTV's Chief Financial Officer from October 2004 to August 2007,[356] and Mr Gallienne, who held various executive positions at ASTV from 2002 to 2014,[357] the City always voted with UUTBV's representatives. At best, they say, the B-share would have allowed the City to prevent the passing of a resolution. Not only did the City never seek to exercise its B-share rights, it never even attempted to outvote UUTBV.[358]

- *The Supervisory Council*

387. The Supervisory Council is responsible for organising the management of the company and supervises the Management Board. Prior to the IPO, it was constituted of seven (7) members.[359]

388. Pursuant to ASTV's Articles of Association, a resolution of the Supervisory Council is considered as adopted if more than one-half of the participating members vote in its favour save for specified matters where a unanimous vote is required (such as the approval of the development plan and strategy of ASTV, the approval of the business plan as well as investments exceeding 10 million Kroons).[360]

389. Prior to the IPO, the Shareholders' Agreement provided, that UUTBV would appoint four (4) of the seven (7) members of the Supervisory Council.[361]

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[354] **C-20**, Shareholders' Agreement (12 January 2001), ss. 3.2.1 and 3.1.11.

[355] **C-20**, Shareholders' Agreement (12 January 2001), s. 5.1.

[356] Plenderleith 2nd WS, ¶¶38-42.

[357] Gallienne 2nd WS, ¶94.

[358] Plenderleith 2nd WS, ¶¶49 and 50.

[359] **C-11**, Tallinn City Council Resolution No. 210 – ASTV Articles of Association (15 June 2000), s. 6.3.

[360] **C-11**, Tallinn City Council Resolution No. 210 – ASTV Articles of Association (15 June 2000), s. 6.3.10.

[361] **C-20**, Shareholders' Agreement (12 January 2001), ss. 3.1.1 and 3.1.2(b).

390. According to Mr Plenderleith, who took his first position at ASTV in October 2004,[362] the dominant role played by the Chairman of the Management Board (*i.e.* ASTV's CEO, who has always been a UUTBV appointee[363]) regarding the strategic matters handled by the Supervisory Council more than offset any lack of majority on the Supervisory Council. Mr Plenderleith never witnessed a situation and there is no evidence of there ever having been a situation in which the Supervisory Council could not reach a unanimous decision whenever required by the Articles of Association.[364] Indeed, it appears that the City and ASTV developed the very useful practice of resolving any disagreements through negotiations outside ASTV's management structure.[365]

391. Similarly, Mr Gallienne testified that the Chairman of the Management Board always benefited from substantial autonomy in his management. During his tenure as ASTV's CEO, he has always considered obtaining the Supervisory Council's approval as to be, in effect, obtaining the approval of UUTBV.[366] It is of note that the Chairman of the Supervisory Council has always been an employee or consultant of UUTBV or another United Utilities entity.[367]

- *The Management Board*

392. The Management Board represents and manages ASTV as well as organises its accounting. The Management Board cannot, however, execute transactions beyond the scope of ordinary business without the Supervisory Council's approval.[368]

393. Prior to the IPO, the Shareholders' Agreement provided that the votes of the four (4) UUTBV members of the Supervisory Council would be sufficient for the election and/or removal of all of the members of the Management Board.[369]

(iii) <u>The EBRD's entry into ASTV</u>

394. A mentioned above at paragraphs 207 and 208, from 2003 to 2010, the EBRD held an indirect stake in ASTV through a 25% participation in UUTBV.

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[362] Plenderleith 1st WS, ¶6.

[363] Plenderleith 1st WS, ¶152.

[364] Plenderleith 2nd WS, ¶¶52-60.

[365] Plenderleith 2nd WS, ¶¶67-69. For instance, discussion and negotiation of amendments was undertaken through the exchange of correspondence, rather than through the Supervisory Board.

[366] Plenderleith 1st WS, ¶154v).

[367] Plenderleith 1st WS, ¶154i).

[368] **C-11**, Tallinn City Council Resolution No. 210 – ASTV Articles of Association (15 June 2000), s. 6.4.

[369] **C-20**, Shareholders' Agreement (12 January 2001), s. 3.1.12.

395. As a condition of its investment, the EBRD obtained the right to nominate two (2) of the representatives of UUTBV on ASTV's Supervisory Council. The EBRD consistently voted with UUTBV.[370]

(iv) The Impact of the 2005 IPO on control over ASTV

396. As a result of the 2005 IPO, UUTBV became a minority shareholder, holding 35.3% of ASTV's ordinary shares. The City of Tallinn held 34.7%.[371]

397. As stated above at paragraph 210, the City of Tallinn and UUTBV recorded their intention to maintain the *status quo* (described as UUTBV's "full operational control over the Company and responsibility related thereto") in the First 2005 Amendment:

> The City [of Tallinn] and [UUTBV] acknowledge that the amendments to be made in the Shareholders Agreement and other agreements executed between them should take into account the fact that the objective of the sale of 50.4% of shares in [ASTV] to [UUTBV] in 2001 was to transfer a full operational control over [ASTV] and responsibility related thereto to [UUTBV]. The amendments introduced by this Agreement are not intended to change this principle or the respective rights or obligations of [UUTBV] and the City [of Tallinn].[372]

398. Similarly, the 2005 Amendment recorded that UUTBV would not forfeit its ability to appoint all members of the Management Board. For this purpose, the City of Tallinn guaranteed that its representatives at the Supervisory Council would vote with UUTBV's appointees concerning the composition of the Management Board precisely "to ensure the continuing operational control of the Investor."[373]

399. During the negotiations of this amendment, the City of Tallinn had initially suggested that the Supervisory Council be constituted of eight (8) members and that UUTBV and the City of Tallinn would each nominate three (3).[374] The City of Tallinn nonetheless retracted and agreed to amend the Shareholders' Agreement so that the Supervisory Council be formed of nine (9) members, four (4) of which were to be appointed by UUTBV, three (3) by the City of Tallinn and two (2) were to be independent members.[375] Mr Plenderleith testified that the two (2)

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[370] Gallienne 1st WS, ¶50.

[371] In the proportion of 35.3%, whereas the City was holding 24.7% of the ordinary shareholding from thereon, **C-29**, Agreement on Amending the Project Agreements (10 March 2005).

[372] **C-29**, Agreement on Amending the Project Agreements (10 March 2005), recitals 2 & 3. General Principles 2.3 and 2.4.

[373] **C-29**, Agreement on Amending the Project Agreements (10 March 2005), Clause 4.5.

[374] **C-115**, Letter from LEXTAL (representing the City of Tallinn) to United Utilities International Ltd (12 January 2004), ¶¶4.1, 4.2 and 4.4.

[375] **C-29**, Agreement on Amending the Project Agreements (10 March 2005), Clause 4.1.

independent members were always nominated by either him or Mr Gallienne, and the City of Tallinn would have always supported their election.[376]

400. The Articles of Association of ASTV were also amended to notably reflect the changes in the number of members of the Supervisory Council.[377]

401. Lastly, it is noted that the prospectus issued for the purposes of the IPO (the "**Prospectus**") described ASTV as a joint venture by the City of Tallinn and UUTBV, controlled by the City of Tallinn and UUTBV.[378]

d) Estonian Law Expert Evidence

402. Respondent submitted two (2) legal expert reports from Mr Hannes Vallikivi that address the notion of control under Estonian and EU law. Although the applicable *international law* standard does not stem from either, this evidence nonetheless bears some relevance to the extent that it fleshes out how ASTV is structured and operates as an Estonian juridical person, That being said, Estonian law can only be of limited assistance since, as conceded by Mr Vallikivi during the Hearing,[379] even under Estonian law, the determination of control may vary depending on the context in which the issue is assessed and may be founded on a number of factors and considerations.

403. In Mr Vallikivi's opinion, ASTV is jointly controlled by the City of Tallinn and UUTBV. In his view, the acquisition by the City of Tallinn of veto rights through the privatisation of ASTV precludes a finding of control by UUTBV since any control depended on the City:[380]

> The City of Tallinn holds strategic control through a unanimous vote requirement for strategic decisions by the Supervisory Board and the Golden Share of the City of Tallinn allowing it to veto strategic decisions if referred to the General Meeting because consensus was not reached in the Supervisory Board. The Golden Share also allows the City of Tallinn to veto fundamental decisions of ASTV in the General Meeting such as amendment of the Articles of Association, change of capital and status of ASTV. UUTBV and the City of Tallinn also need to act in concert in order to appoint the Management Board of ASTV, elected by the Supervisory Board, since 2005.[381]

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[376] Plenderleith 1st WS, ¶149.

[377] **R-17**, Articles of Association of ASTV adopted on 27 April 2005 and registered with the Commercial Register on 6 May 2005, Art. 6.3.5.

[378] **C-113**, Prospectus for ASTV 2005 IPO (2005), pp 1874, 1890, 1891 and 1915. ASTV was also referred to as a joint venture in United Utilities 2006 annual report, **R-199**, Annual Reports of United Utilities Plc / UUG for years 2001- 2015, p 22, p 18 of the pdf.

[379] Tr. Day 5 Mr Vallikivi 115:4-18 and 115:25-119:1.

[380] Vallikivi 1st ER, ¶¶99-128; Vallikivi 2nd ER, ¶14.

[381] Vallikivi 2nd, ¶31.

404. For the purposes of his expert opinion, Mr Vallikivi elaborated a definition of control after having studied how control is defined in different sources of law, including Estonian company law, competition law, and securities law and related EU law. Mr Vallikivi's definition consists of three alternative scenarios:[382]

> All of the above definitions seem to have common features that allow proposing a general definition of "control". A direct or indirect shareholder is deemed to control a public limited company if on the basis of (i) the law, (ii) the Articles of Association, or (iii) a contract with the company or other shareholders, it:
>
> (a) has a majority of voting rights (>50%);
>
> (b) has the power to (i) appoint or remove a majority of the members of the Management Board or Supervisory Board, or (ii) control the financial and operating policies of the company, or (iii) determine the decision making of the Management Board and Supervisory Board, or (iv) use or dispose of all or significant proportion of assets of the company; or
>
> (c) is able to veto strategic decisions in the company (negative control).[383]

405. It appears from Mr Vallikivi's reports that his conclusion that ASTV is jointly controlled by UUTBV and the City of Tallinn is not affected by the voting conventions agreed to in the Shareholders' Agreement because these obligations are only contractual in nature. Such obligations would bear lesser importance since, should the City fail to abide by its contractual obligations, UUTBV's sole recourse would be an action in damages and would not affect the validity of a resolution adopted in contravention to the voting convention. Additionally, according to Mr Vallikivi, the members of the Supervisory Council appointed by the City of Tallinn are deemed independent and thus are not required to vote in accordance with the City of Tallinn's direction and/or the Shareholders' Agreement.[384]

406. That being said, Mr Vallikivi conceded during his cross-examination that a shareholder who can appoint or remove a majority of the Management Board's members pursuant to an agreement with another shareholder in fact meets his control test.[385]

407. Mr Vallikivi also acknowledged during the Hearing that the most important matters over which the City may impose its veto through the B-Share consists of issues for which minority shareholders are usually protected by the corporation's articles of association and which do

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[382] Tr. Day 5 Mr Vallikivi 117:16-22.

[383] Vallikivi 1st ER, ¶63.

[384] Tr. Day 5 Mr Vallikivi 128:11-129:10, 170:21-173:22, 177:17-23; Vallikivi 1st ER, ¶¶33 and 41.

[385] Tr. Day 5 Mr Vallikivi 117:10-118:16: "Q. To take an example, if a shareholder has the power through a shareholders' agreement with other shareholders to appoint or remove a majority of the members of the management board, then that's sufficient to fulfil control under your general definition? […] A. Yes, then it meets my test."

not have bearing on the issue of control.[386] In any event, considering that the passing of a resolution on these subjects requires a two-thirds majority, the B-share would not confer any practical advantage to the City since it has always held at least a third of the ordinary shareholding.[387]

408. As a result, according to Mr Vallikivi, the B-Share would only provide the City with the ability to block the passing of resolutions pertaining to two (2) matters: (i) the acquisition of treasury shares and (ii) issues referred to the General Meeting at the request of the Management Board or the Supervisory Council.

409. Regarding the first category of resolutions, Mr Vallikivi recognised that the inability for a shareholder to force the adoption of such a resolution does not necessarily indicate that this shareholder does not control the company.[388] Regarding the second category of resolutions, Claimants submit – and the Tribunal cannot help but agree – that it is unlikely that such a matter would be referred to the General Meeting by either the Supervisory Council or the Management Board considering that i) all members of the latter are appointed by UUTBV (pursuant to the Shareholders' Agreement) and ii) the decisions of the Supervisory Council are shaped by UUTBV, and the evidence is that UUTBV never failed to pass a resolution at the Supervisory Council.[389]

410. Claimants also downplay the importance of the duty of independence of the members appointed by the City (which according to Mr Vallikivi would trump the voting agreement contained in the Shareholders' Agreement). In Claimants' view, it would be unlikely that a UUTBV-sponsored resolution would be defeated on this basis because the UUTBV's members only need to secure another vote to pass a resolution at the Supervisory Council and could easily obtain the support of the two (2) independent members as *de facto* UUTBV appointees.[390]

e) Analysis of the Tribunal: Control of ASTV

411. The Tribunal is of the view that the evidence establishes that UUTBV controlled ASTV at the relevant points in time.

412. It is noted that UUTBV and the City of Tallinn carefully negotiated the provisions of the privatisation agreements regarding control over ASTV. The Parties appear to have struck a balance between the need for the foreign investor to assume effective control of ASTV and the desire to maintain the corporate structure set out in the company's Articles of Association. This outcome aligns with the statements in tender documents to the effect that the investor would gain both operational and management control of ASTV.

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[386] Namely the amendment to the articles of association, the increase and decrease of share capital, the issuing of convertible bonds, the dissolution, merger and other transformations of the company.

[387] Tr. Day 5 Mr Vallikivi 148:13-149:22.

[388] Tr. Day 5 Mr Vallikivi 150:13-21.

[389] Cl. PHB, ¶540.

[390] Cl. PHB, ¶534; **C-253**, ASTV Articles of Association, ss. 6.3.9 and 6.3.10.

413. As discussed above, it is not in dispute that UUTBV enjoyed operational control over ASTV. It should also be recalled that UUTBV has always been the most important private shareholder of ASTV.

414. Regarding strategic control, it is manifest that UUTBV exerted a dominant influence over ASTV management, notwithstanding that the City of Tallinn held certain special voting rights by virtue of the B-share.

415. First, UUTBV had the ability to nominate the members of the Management Board pursuant to the Shareholders' Agreement, both before and after the 2005 IPO, which Mr Vallikivi confirmed would meet even his control test.

416. Second, UUTBV effectively enjoyed dominant influence over the Supervisory Council pursuant to the voting convention agreed pursuant to the Shareholders' Agreement. Even if after the IPO these rights did not grant UUTBV a majority of appointees to the Supervisory Council, the evidence is that UUTBV was at all times the party directing and driving the Supervisory Council's activities and decisions. This is manifest not only from the fact of UUTBV's special management and technical expertise, the exercise of which was the *raison d'être* of ASTV's privatisation, but also from the uncontradicted evidence concerning the dominant role played by ASTV's CEO, a UUTBV appointee, in the management of ASTV's affairs. It bears repeating that UUTBV never failed to obtain the adoption of a resolution that it supported, including on issues requiring a unanimous vote, that UUTBV *de facto* nominated the independent members of the Supervisory Board, and that the chairman of the Supervisory Board has always been a person related to UUTBV (and not to the City of Tallinn).

417. Third, the powers attached to the B-share, when viewed in the overall context here, conferred only minimal advantage to the City of Tallinn, as appears from a review of the Estonian law evidence. The incidence of the B-share rights seems all the more accessory in the light of the City's undertaking to not exercise them, save in the extreme case where ASTV could not otherwise be properly managed. In the circumstances, those rights do not support the assertion that ASTV was jointly controlled by UUTBV and the City of Tallinn.

418. The fact that ASTV was referred to as a joint venture in the IPO documentation changes nothing in this regard. It certainly does not prevent a finding of control, considering how loosely joint ventures are defined and given the evidence of UUTBV's overwhelming control of the company. Furthermore, to the extent that the subjective understanding of the Parties bears relevance, it should be pointed out that, as of 17 September 2009, the Tallinn City Council itself declared that from its perspective the privatisation had deprived the City from making management decisions regarding ASTV.[391]

419. Finally, the fact that, from 2003 to 2010, two (2) UUTBV appointees to the Supervisory Council were nominated by the EBRD does not impact the Tribunal's assessment considering that this right was itself a consequence of the EBRD's stake in UUTBV. Furthermore, the evidence is to the effect that the EBRD's nominees always voted with UUTBV's representatives on the Council.

[391] **R-194**, Decision of the Tallinn City Council (17 September 2009), ¶1.2.

420. In sum, the evidence is that UUTBV controlled ASTV and dominated all aspects of the company's operational management and strategic decision-making throughout the period from 2009 until the rejection of the 2011 Tariff Application, as well as at the time of consent, the whole in accordance with one of the fundamental purposes of the privatisation over ASTV.

4) The Relevance of UUTBV's Corporate Structure

421. Having determined that UUTBV controlled ASTV, the Tribunal must nonetheless decide as to whether the fact that UUTBV became wholly owned by United Utilities, a UK corporation, has any bearing on the question of the "nationality" requirement under Art. 9 (4) of the BIT.

422. Respondent argues that UUTBV is nothing more than a "shell" company, and that any control exercised by UUTBV over ASTV actually rests with its UK parent company, United Utilities. This means, in Respondent's view, that any foreign control over ASTV, as required by the ICSID Convention, rests not with a Dutch national (UUTBV) but with a UK national (United Utilities) that is not covered by the Estonian-Dutch BIT.

423. The Tribunal will first review the relevant international investment law authorities and the position of the Parties (a), and after considering the relevant facts (b), will address the relevance and impact of United Utilities' control of UUTBV (c).

a) Positions of the Parties, and Relevant International Authorities

424. According to Respondent, several international tribunals have determined that a shell company may not ground a finding of control. A shell company merely channels control to the upstream entity.[392] Respondent relies heavily in this respect on *National Gas v Egypt* and on *TSA Spectrum v Argentina*.[393] Respondent also relies on the expert evidence of Mr Vallikivi, who opines that under Estonian law as well control is usually found to vest in the ultimate controller in a chain of corporate entities.[394]

425. As regards the international law authorities, Claimants emphasise that Respondent has not submitted a single case in which an international tribunal has pierced the veil of the second corporate layer (*e.g.,* in this case, the veil between UUTBV and United Utilities), and where the ultimate controller was found to be neither a national of the host State nor a national of a non-Contracting State of the ICSID Convention. The so-called ultimate controller in the present case – United Utilities – is neither; the *TSA Spectrum* and *National Gas* cases are distinguishable and of little assistance here.

426. In *TSA Spectrum v Argentina*, the tribunal indeed examined the claimant's "upstream" chain of ownership and control, and declined jurisdiction on the basis of its finding that TSA was ultimately controlled, not by a foreign entity, but by an Argentinian national through a Dutch holding. The tribunal noted that there is no consistent practice as to whether it is necessary to pierce the second corporate layer (beyond, in that case, the domestic entity) in identifying

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[392] Resp. PHB, ¶ 264.

[393] Resp. Rej., ¶¶276-282.

[394] Vallikivi 1st ER, ¶¶61 and 62; Vallikivi 2nd ER, ¶¶22-24.

control.[395] However, it determined that such an approach was especially warranted when the ultimate control is alleged to be in the hands of a national of the host State.[396]

427. In *National Gas v Egypt*, the tribunal also pierced the veil of the claimant entity, based on the reasoning of *TSA Spectrum*. It too emphasised that this approach is appropriate where there is a suggestion that the relevant entity might be controlled not by a foreign entity but by a national of the host State.[397] In that matter, the tribunal found that 90% of National Gas' shareholding was detained by an UAE company that was wholly owned by an Egyptian national.

428. According to Claimants, the notion of control is independent from the question of whether the entity claiming jurisdiction is a so-called shell company; the corporate nature of this entity is irrelevant to the "control" analysis. Precluding a shell company from claiming control would be contrary to the broad and liberal meaning of control under the ICSID Convention. Claimants also contend that the BIT here does not contain any language forbidding a shell company from benefitting from the Treaty's protections. Claimants further submit that the only exception to this rule – the only instances in which tribunals have "looked through" the corporate structure of a claimant – have been where there were suggestions that the claimant was ultimately controlled by local (host State) interests or from a non-Contracting State to the ICSID Convention. They refer to Professor Schreuer, who comments that looking at the ultimate controller in such a scenario is necessary for the purpose of "blocking access to the Centre for juridical persons that are controlled directly or indirectly by nationals of non-Contracting States or nationals of the host State."[398]

429. Two other cases also provide particularly relevant and compelling guidance.

430. In *Autopista v Venezuela*, the respondent argued that the alleged US control of the domestic entity, Aucoven, was a fiction and that claimant lacked jurisdiction accordingly. At its incorporation, 99% of Aucoven's shareholding was held by ICA, a subsidiary of a Mexican conglomerate, ICA Holding. A few days after the start of its operations, Aucoven requested authorisation to transfer 75% of its shares to Icatech, an American subsidiary of ICA Holding. This authorisation was obtained 15 months later, after ICA Holding submitted a guarantee and accepted to be jointly responsible for Icatech's obligations. The relevant concession agreement defined control as ownership of a majority of Aucoven's shares. The tribunal refused to interfere with the parties' definition and declined to look beyond the immediate control of Aucoven. According to the tribunal, the agreement of the parties fell within the ambit of Art. 25 of the Convention, which does not require a demonstration of what the tribunal called "effective *control*."[399]

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[395] **RL-114**, *TSA Spectrum de Argentina S.A. v Argentine Republic*, ICISD Case No. ARB/05/5, Award (19 December 2008), ¶¶148-149 and 152 [*TSA Spectrum v Argentina*].

[396] **RL-114**, *TSA Spectrum v Argentina*, *ibid*, ¶¶145 and 153.

[397] **RL-103**, *National Gas*, *supra* note 319, ¶¶136 and 137.

[398] Cl. PHB, ¶¶566-573; **CL-100**, Schreuer, *The ICSID Convention*, *supra* note 332, ¶849.

[399] **CL-6**, *Autopista v Venezuela*, *supra* note 333, ¶112.

431. In *AdT v Bolivia*, although there was no question that AdT was controlled by a foreign entity, the parties disagreed on the locus of this foreign control. Bolivia notably submitted, as does Estonia in the present case, that control can only be said to lie with the ultimate controlling entity. The applicable treaty, The Netherlands-Bolivia bilateral investment treaty, contained a definition of foreign nationals substantially identical to the BIT in this case.[400] A majority of the tribunal found that there were no indications from the various definitions of "*control*" and "*controlled*" that control necessarily entails a degree of active exercise of powers or direction. It further dismissed Bolivia's argument that it should refer to the notion of control under international law for the purposes of defining corporate nationality.

432. Construing the phrase "*directly or indirectly controlled*," the majority ruled that foreign-controlled entities could avail themselves of the treaty's protections even if there existed several links in the chain of control:

> The phrase, "directly or indirectly," in modifying the term "controlled" creates the possibility of there simultaneously being a direct controller and one or more indirect controllers. The BIT does not limit the scope of eligible claimants to only the "ultimate controller."[401]

b) Relevant Facts

433. UUTBV became wholly owned by United Utilities in November 2010,[402] and there is no question that UUTBV's ultimate parent companies have always been UK companies.[403]

434. Estonian and Dutch authorities have confirmed that UUTBV is a Dutch resident.404 Upon International Water's exit from UUTBV, UUTBV applied to the Northern Tax Centre of the Tax Customs Board of Estonia for a confirmation that the Estonia-Netherlands Double Taxation Treaty would apply. The Estonian authorities declared that UUTBV was a Dutch resident as per the definition of the applicable treaty.[405]

435. The Respondent points out, however, that as a matter of Dutch law, all Dutch B.V.s are considered to be Dutch residents for tax purposes, and the requirements to maintain Dutch

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[400] The Netherlands-Bolivia treaty defines nationals as: "(ii) without prejudice to the provisions of (iii) hereafter, legal persons constituted in accordance with the law of that Contracting Party; (iii) legal persons controlled directly or indirectly, by nationals of that Contracting Party, but constituted in accordance with the law of the other Contracting Party," **RL-117**, *AdT v Bolivia*, *supra* note 334, ¶80.

[401] **RL-117**, *AdT v Bolivia*, *ibid*, ¶237.

[402] Cl. Mem., ¶303.

[403] Tr. Day 1, Claimants' Opening Statement, 110:24-111:11.

[404] **C-309**, UUTBV Tax Residency Declaration (30 January 2003); **C-311**, UUTBV Tax Residency Declaration (24 July 2003); **C-315**, UUTBV Tax Residency Declaration (1 April 2004); **C-316**, UUTBV Tax Residency Declaration (13 August 2004); **C-321**, UUTBV Tax Residency Declaration (16 February 2005); **C-352**, UUTBV Tax Residency Declaration (20 July 2010); **C-357**, UUTBV Tax Residency Declaration (29 September 2011) and **C-369**, UUTBV Tax Residency Declaration (10 September 2014).

[405] **C-324**, Letter from Northern Tax Centre of the Tax and Customs Board to AS PricewaterhouseCoopers LLP (3 May 2005).

residence are minimal.[406] Moreover, both the Estonia-Netherlands and the UK-Netherlands double taxation treaties allow a Dutch shell company to claim Dutch residency for tax purposes.[407]

436. It appears from Mr van Rooijen's evidence that of the thirteen managing directors of UUTBV, seven resided in the UK, one in The Netherlands, one in Ukraine and four (4) in Estonia.[408] There is no evidence as to the location from which the UUTBV directors who remotely attended UUTBV's board meetings (e.g., by telephone) participated in these meetings.[409]

437. The Dutch director of UUTBV is Orangefield (now Vistra), a company that provided and provides to UUTBV domiciliation services as well as management, accounting, reporting and legal administration services.[410]

438. Mr van Rooijen, an Orangefield employee, testified that UUTBV is managed independently from the other entities of the United Utilities group. He testified that UUTBV, as opposed to other entities of the United Utilities group, received reports and took key commercial decisions regarding ASTV.[411] Mr van Rooijen also affirmed that UUTBV maintains other commercial activities beyond holding and financial activities, though he did not particularise those activities.[412] His evidence also contains reference to the minutes of UUTBV's board meetings. These minutes mostly refer to a "*business update*" on ASTV's activities, which would be based on a report distributed beforehand,[413] and the appointment of the members of the Supervisory Council.[414]

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[406] **RL-246**, Dutch Corporate Income Tax Act 1969.

[407] **RL-225**, The Convention between the Republic of Estonia and the Kingdom of The Netherlands for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to taxes on Income and capital and **RL-226,** UK/Netherlands Double Taxation Convention and Protocol, signed on 26 September 2008, entered into force on 25 December 2008; Resp. Rej., ¶¶293 and 294.

[408] van Rooijen 1st WS, ¶30.

[409] Tr. Day 3 van Rooijen 112:9-13; Resp. PHB, ¶270.

[410] Tr. Day 3 van Rooijen 90:12-21.

[411] van Rooijen 1st WS, ¶13.

[412] van Rooijen 1st WS, ¶15.

[413] van Rooijen 1st WS, ¶37; see **C-330**, ASTV 2006 Q4 update dated 2006; **C-337**, ASTV 2007 Q4 update dated 2007; **C-339**, ASTV 2008 Q4 update dated 2008 and **C-350** ASTV 2009 Q4 update dated 2009.

[414] van Rooijen 1st WS, ¶¶38-40; see **C-331**, Minutes of UUTBV Management Board Meeting (19 January 2007), which refers to the appointment of member of the Supervisory Council; **C-338**, Minutes of UUTBV Management Board Meeting (11 September 2008), which refers to the appointment of member of the Supervisory Council; **C-340**, Minutes of UUTBV Management Board Meeting (23 January 2009), which refers to an update on ASTV's affairs and the issuance of a power of attorney for the purposes of ASTV's annual general meeting; **C-351**, Minutes of UUTBV Management Board Meeting (22 January 2010), which refers to an update on ASTV's affairs, the issuance of a power of attorney for the purposes of ASTV's annual general meeting; **C-354**, Minutes of UUTBV Management Board Meeting (28 January 2011), which refers to an update on ASTV's affairs; **C-358**, Minutes of UUTBV Management Board Meeting (20 January 2012), which refers to an update on ASTV's affairs; **C-361**, Minutes of UUTBV Management Board Meeting (18 January 2013), which refers to an update on ASTV's affairs; **C-368**, Minutes of UUTBV Management

439. Mr Plenderleith, who was ASTV's CFO from October 2004 to August 2007, and its CEO from October 2008 to June 2014, testified that he was a United Utilities employee from 1988 to 2014.[415] During his tenure, the UUTBV appointees to ASTV's Supervisory Council were either directors of UUTBV or of another entity within the United Utilities group.[416] These include Simon Gardiner, who was the secretary of United Utilities, and Brendan Murphy,[417] who was the head of the treasury of United Utilities.[418] Mr Plenderleith testified that he communicated with high-ranking executives of United Utilities almost exclusively through UUTBV.[419] He is not aware of, and he never experienced any pressure exerted by United Utilities regarding ASTV, and he would be surprised if ASTV had been discussed at United Utilities' board meetings.[420]

440. Mr Plenderleith explained that United Utilities and its related entities play a contractual role as technical advisors.[421] This was formalised through the conclusion of the Technical Services Agreement, referred above at paragraph 193.[422] United Utilities also provided legal, public relations and treasury functions to ASTV.[423] In the latter respect, the Prospectus made explicit references to the fact that ASTV benefitted from United Utilities' technical know-how.[424]

441. The Tribunal notes that other connections between UUTBV and the United Utilities stem from the latter's intervention in certain agreements pertaining to ASTV's privatisation. For example, United Utilities guaranteed the performance of UUTBV's monetary obligations under the

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Board Meeting (29 July 2014), which refers to an update on ASTV's performance; **C-370**, Minutes of UUTBV Management Board Meeting (13 October 2014), which refers to the issuance of a power of attorney to an Estonian attorney; **C-373**, Minutes of UUTBV Management Board Meeting (5 November 2014), which refers to an update on ASTV's performance and the current arbitration, as well as the appointment of a member of ASTV's Supervisory council; **C-378**, Minutes of UUTBV Management Board Meeting (30 April 2015), which refers to an business update regarding ASTV, including the distribution of profit and the election of a member of the Supervisory Council and the issuance of a power of attorney to an Estonian lawyer to represent UUTBV at ASTV's annual general meeting and to vote in favour of all the items of the agenda; **C-380**, Minutes of UUTBV Management Board Meeting (28 October 2015), appointment of a member of the Supervisory Council.

[415] Plenderleith 1st WS, ¶¶5 and 6.

[416] Plenderleith 1st WS, ¶154(iii).

[417] The Tribunal notes that Mr Murphy is not listed by Mr van Rooijen as a UUTBV's managing director, van Rooijen 1st WS, ¶30.

[418] Tr. Day 2 Mr Plenderleith 25:10-23.

[419] Tr. Day 2 Mr Plenderleith 26:4-22; Plenderleith 1st WS, ¶¶85 and 86.

[420] Plenderleith 2nd WS, ¶¶85-88. According to Mr Plenderleith, this was due to the strategy of United Utilities plc to move away from its international investments towards domestic UK investments. He notes that it is in that view that United Utilities attempted to sell its interest in ASTV to Veolia. This transaction was not authorised by the Estonian Financial Supervision Authority. The latter determined that United Utilities plc had a dominant influence over ASTV and that Veolia would need to make an offer to other ASTV's shareholders.

[421] Plenderleith 1st WS, ¶ 154(viii).

[422] **C-113**, Prospectus for ASTV 2005 IPO (2005), p 1885; **C-49**, Closing Memorandum.

[423] Plenderleith 1st WS, ¶ 154(ix).

[424] **C-113**, Prospectus for ASTV 2005 IPO (2005), p 1885.

Shareholders' Agreement,[425] which was one of the conditions set out in the Closing Memorandum.[426] As well, United Utilities was a signatory of the Share Retention and Subordination Agreement of 8 November 2002, pursuant to UUTBV agreement on share retention and debt subordination to the EBRD.[427]

c) Analysis of the Tribunal: Relevance of the Ultimate Controller of UUTBV

442. In view of the Tribunal's conclusion regarding UUTBV's control of ASTV, the nature of the relationship between UUTBV and its parent United Utilities is irrelevant to the question of jurisdiction under the ICSID Convention. Whether control of ASTV is said to reside in one or the other, control clearly vests in a national of a Contracting State to the ICSID Convention other than the host State. The question is whether, and how, that relationship affects the issue of jurisdiction under the BIT.

443. The preamble of the Treaty and its provisions establish that it aims to promote economic cooperation between The Netherlands and Estonia by encouraging investment in each State by nationals of the other.[428] In defining nationals, the parties introduced the important qualification of "*direct or indirect*" control, and elected not to define the meaning of control.

444. As in *AdT v Bolivia*, a majority of the Tribunal concludes that the signatories of the Treaty did not exclude the possibility that multiple sources of foreign control of a domestic entity could be identified, as well as the very real possibility that a person having direct or indirect – though not necessarily the "ultimate" – control could bring a claim under the Treaty so long as that person is a national of the non-host State party. It is not for the Tribunal to limit or curtail such an intentionally broad and open-ended definition.

445. The facts at hand demonstrate that UUTBV clearly forms part of the chain of control – it is in fact the first, direct link in that chain. There is no question that there is interaction between ASTV and other members and employees of the broader United Utilities group with respect to ASTV. That being said, the Tribunal is satisfied that UUTBV, a Dutch corporate vehicle, is the converging point within the group at which the management of ASTV is addressed. Indeed, the minutes of UUTBV record not only that UUTBV's directors were appraised of ASTV activities but that they were also entrusted with the appointment of the members of the Supervisory Council, the very entity responsible for ASTV's strategic management. That certain decision-making regarding ASTV might also have occurred at so-called upstream links in the corporate chain is irrelevant under the BIT.

446. The Tribunal thus concludes that United Utilities' control of UUTBV does not preclude a finding of jurisdiction by the Dutch intermediary company over ASTV's claims, under The Netherlands-Estonia BIT.

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[425] **C-92**, Performance Guarantee provided by United Utilities International Limited (22 January 2001).

[426] **C-49**, Closing Memorandum, Clause 2(v).

[427] **C-25**, Share Retention and Subordination Agreement (8 November 2002).

[428] **C-1**, BIT, preamble and Art.1.

B) THE *RATIONE VOLUNTATIS* JURISDICTION OF THE TRIBUNAL

447. By way of its second objection to jurisdiction, Respondent submits that the Tribunal lacks jurisdiction because the current arbitral proceedings are essentially the same as the Estonian proceedings commenced by ASTV. As noted above at paragraphs 292-301 and following, ASTV is currently seeking before the Estonian courts various remedies in relation to the rejection of the 2011 Tariff Application. According to Respondent, a finding of jurisdiction would thus violate Art. 26 of the ICSID Convention.

448. After discussing the authorities submitted by the Parties on this point (1), the Tribunal will review the position of the Parties on the application of Art. 26 of the ICSID Convention (2) and then proceed with its own analysis (3).

1) The Breadth and Effect of Art. 26 of the ICSID Convention

449. Art. 26 of the ICSID Convention reads:

> Consent of the parties to arbitration under this Convention shall, unless otherwise stated, be deemed consent to such arbitration to the exclusion of any other remedy. A Contracting State may require the exhaustion of local administrative or judicial remedies as a condition of its consent to arbitration under this Convention. [Emphasis added]

450. Estonia argues that its consent to the ICSID Convention was premised on the exclusivity of ICSID proceedings and that this exclusivity principle operates as a pre-requisite for ICSID's jurisdiction in any given case. A breach of Art. 26 of the ICSID Convention would thus deprive the Centre of any jurisdiction.[429] Respondent does not rely on any ICSID-specific authority on this precise point.

451. Claimants argue that Art. 26 of the ICSID Convention boils down to a *rule of interpretation* aimed at clarifying the nature of parties' consent to arbitration, as opposed to a condition to consent *per se*. In their view, unless the parties have expressed otherwise, consent to refer a dispute to the Centre is understood to exclude other types of remedies concerning this same dispute.[430] They refer to Professor Schreuer's commentaries, according to which this rule operates only from the moment of valid consent, and not before:

> The first sentence of Art. 26 has two main features. The first is that, once consent to ICSID arbitration has been given, the parties have lost their right to seek relief in another forum, national or international, and

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[429] Resp. C-M, ¶¶320-332.

[430] Cl. Reply, ¶547, referring to **CL-100**, Schreuer, *The ICSID Convention*, *supra* note 332, p 351, ¶ 2, ¶17; **CL-10**, *Lanco v Argentina*, ICSID Case No. ARB97/6, Decision on Jurisdiction (8 December 1998), ¶38: "Article 26 is merely a standard for interpretation, a presumption that arbitration is the exclusive remedy, but that the parties may require exhaustion of domestic remedies"; **CL-11**, *SGS v Philippines*, ICSID Case No. ARB/02/6, Decision on Jurisdiction (29 January 2004), ¶146, where the tribunal noted that the ICSID Convention's *travaux préparatoires* make clear that Art. 26 was intended as a rule of interpretation.

> are restricted to pursuing their claim through ICSID. This principle operates from the moment of valid consent.[431] [Emphasis added]

452. Claimants further posit that a breach of Art. 26 of the ICSID Convention does not in any event invalidate a party's consent or otherwise vitiate the jurisdiction of the Tribunal.[432] They find support in certain decisions on provisional measures issued in the *Tokios Tokelès v Ukraine* and *Perenco v Ecuador* cases.[433]

453. In *Tokios Tokelès v Ukraine*, the claimant sought diplomatic protection concerning a tax investigation commenced by Ukraine. The arbitral tribunal held that the claimant's efforts in that respect were inconsistent with Art. 26 of the ICSID Convention. It nonetheless refrained from discontinuing the arbitral proceedings, finding that abstention from diplomatic proceedings is not a condition for the Centre's or a tribunal's jurisdiction.

454. In *Perenco v Ecuador*, the claimant sought the tribunal's assistance further to Ecuador's effort to enforce certain rights pursuant to Ecuadorean domestic law. The tribunal held that Ecuador's conduct was inconsistent with Art. 26 of the ICSID Convention; it did not, however, comment on the impact of Ecuador's conduct on the tribunal's or the Centre's jurisdiction.

455. According to Respondent, reliance on these two (2) cases is inapposite since they do not concern situations where parallel proceedings have been commenced before domestic courts. Respondent submits that *Pantechniki S.A. Contractors & Engineers (Greece) v Albania* would be the most relevant authority.

456. In that matter, the tribunal held that the claimant could not simultaneously seek recourse for losses incurred in the performance of contracts before domestic courts and in arbitral proceedings.[434] The tribunal (comprised of a sole arbitrator) applied the "fundamental basis" test, which calls for a determination of whether the fundamental basis of the dispute submitted to arbitration is the same as in the dispute pursued in the other forum. He emphasised that this inquiry is context-dependent and that no definite guidance may be ascertained:

> The same facts can give rise to different legal claims. The similarity of prayers for relief does not necessarily bespeak an identity of causes of action. What I believe to be necessary is to determine whether claimed entitlements have the same normative source. But even this abstract statement may hardly be said to trace a bright line that would permit rapid decision. The frontiers between claimed entitlements are not always distinct. Each situation must be regarded with discernment.[435]

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[431] **CL-100**, Schreuer, *The ICSID Convention*, *supra* note 332, p 351, ¶2.

[432] Cl. Mem., ¶321.

[433] **CL-14**, *Tokio Tokelès v Ukraine*, Order No. 3 (18 January 2006), ¶¶7, 23; **CL-12**, *Perenco v Ecuador*, Decision on Provisional Measures (8 May 2009), ¶61.

[434] **RL-119**, *Pantechniki S.A. Contractors & Engineers (Greece) v Albania*, ICSID Case No. ARB/07/21, Award (30 July 2009), ¶31, ¶¶67-68 [*Pantechniki v Albania*].

[435] **RL-119**, *Pantechniki v Albania*, *ibid*, ¶62.

457. The arbitrator found that the claims asserted in the arbitration were substantially the same as those for breach of contract brought before the Albanian courts. It was not sufficient for claimant to assert that the tribunal's jurisdiction was based on the BIT, as opposed to the contract – the claims submitted to arbitration must have an autonomous existence outside the contract. Conversely, the sole arbitrator found that the bringing of domestic proceedings did not prevent claimant from seizing the arbitral tribunal of its denial of justice claim.[436]

458. Respondent also invites the Tribunal to consider the second award on jurisdiction issued in *EURAM v Slovakia*,[437] an *ad hoc* arbitration. The tribunal there held that the claimant's conduct before the Slovakian courts amounted to a waiver to arbitrate pursuant to Swedish law, the *lex arbitri*. As such, the claimant was precluded from bringing arbitral proceedings. The claimant had initially commenced proceedings before Slovakian courts in order to preserve its rights. Those proceedings included its claims under the relevant BIT. The tribunal found that not only did the domestic and arbitral proceedings share the same factual basis and were "substantially the same," but that claimant was effectively treating the domestic proceedings as a simple precautionary measure, and not as a means to obtain a substantive remedy.[438]

459. In the same vein, Respondent refers to *Commerce Group v El Salvador*, in which an ICSID tribunal declined jurisdiction on the basis that claimant had not complied with the waiver provision under the CAFTA.[439] It so held on the basis that the impugned "measures" referred to arbitration were substantially the same as those referred to the domestic courts.

2) Positions of the Parties on the Application of Art. 26 to the Facts at Hands

460. Respondent argues that Claimants seek the same remedies before the Estonian courts and in the present arbitral proceedings. Respondent concludes that both the domestic and arbitral proceedings pertain to a claim for damages flowing from the ECA's alleged failure to comply with the Services Agreement and the 2007 Amendment.[440]

461. Respondent alleges that, should the Tribunal find a breach of Art. 26 of the ICSID Convention, such breach would impact both Claimants, even if UUTBV is not a party to the Estonian proceedings. Respondent submits that the "fundamental basis" test referred to above relates to the "claims" at issue, as opposed to the relevant domestic proceedings. It adds that, due to ASTV's corporate structure, UUTBV would benefit from any award of damages to be rendered

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[436] **RL-119**, *Pantechniki v Albania*, *ibid*, ¶¶63-68.

[437] **RL-120**, *European American Investment Bank AG v Slovakia*, PCA Case No. 2010-17, Second Award on Jurisdiction (4 June 2014) [*EURAM v Slovakia*].

[438] **RL-120**, *EURAM v Slovakia*, *ibid*, ¶¶238 and 264.

[439] **RL-121**, *Commerce Group Corp and San Sebastian Gold Mines Inc. v. El Salvador*, ICSID Case No. ARB/09/17, Award (14 March 2011), ¶¶101 and 115.

[440] Resp. Rej., ¶314.

in favour of ASTV.[441] Finally, Respondent submits that the risk of double recovery by ASTV remains extant until the Estonian proceedings become final.[442]

462. Claimants, for their part, argue that their claims in the present arbitration differ from ASTV's Estonian court claims because the former only relate to claims under the BIT. Claimants do not dispute that both sets of claims arise from the same factual background. Yet, they say, each proceeding rests on a distinct legal basis: the arbitration claims relate to breaches of international investment norms, such as the fair and equitable treatment, as opposed to a contravention to Estonian administrative law in the national courts.[443]

463. Moreover, should the Tribunal be minded to find in favour of Estonia in this regard, it could bar only ASTV, but not UUTBV from pursuing its claims in this arbitration since UUTBV is not a party to the Estonian proceedings.[444]

3) Analysis of the Tribunal: *Ratione Voluntatis* Jurisdiction

464. The Tribunal considers that it is unnecessary to engage in an exercise of construction of Art. 26 of the ICSID Convention. This flows from the Tribunal's conclusion, discussed further below, that the present proceedings and the matter before the Estonian domestic courts are not substantially the same. As a result, Art. 26 of the ICSID Convention simply does not enter into play.

465. The remedies sought in this arbitration derive from a different normative source than those articulated before the domestic courts. The thrust of Claimants' case consists of alleged breaches by Respondent of the fair and equitable treatment standard and of due process, as well as other international obligations. It is unchallenged that the Estonian courts have considered facts that are also before the Tribunal, including most notably the rejection of the 2011 Tariff Application. Yet, a review of the decisions issued by the Estonian courts[445] establishes clearly that those courts considered ASTV's and the ECA's respective rights and obligations solely through the prism of Estonian law. At no point were the rights of ASTV as a foreign investor in Estonia pursuant to the BIT and international public law considered or adjudicated. That the Estonian courts were seized of claims sharing much of the same factual

[441] Resp. C-M, ¶344.

[442] Resp. PHB, ¶277.

[443] Cl. Reply, ¶564b.

[444] Cl. Reply, ¶567, referring to **CL-86**, *Occidental Exploration and Production Company v Ecuador*, LCIA Case No. UN3467, Final Award (1 July 2004), ¶52, which states that distinction between treaty-based claims and contractual claims are differentiated based on the triple-identity test and **CL-83**, *CMS Gas Transmission Company v Argentina*, ICSID ARB/01/8, Decision of the Tribunal on Objections to Jurisdiction (17 July 2003), ¶80, where the tribunal dismisses Argentina's objection that it had no jurisdiction because the "*fork in the road*" clause would have been triggered by the Argentinian entity in which the investor was a shareholder at the commencement of domestic proceedings. The tribunal recalled the differences between contractual and treaty-based claims and held that this distinction was all the more applicable here considering that the investor had not instituted any recourse before the domestic courts.

[445] **RL-167**, Tallinn Administrate Court Decision of 12 October 2015; **C-432**, Tallinn Circuit Court Decision of 26 January 2017; Supreme Court Decision (12 December 2017).

basis as the present arbitration cannot prevent a finding of jurisdiction by the Tribunal. Moreover, Claimants' contentions before the Tribunal, as set out above at paragraphs 307-322, cannot be said to amount to a mere international window-dressing of the claims brought by ASTV before the Estonian Courts.

C) The Alleged incompatibility of the BIT with EU Law

466. The Parties have commented at length on the alleged incompatibility of Article 9 of the BIT with EU law in numerous submissions either general or specific to the *Achmea* Judgment.[446]

467. Whereas Respondent adopts an approach primarily focused on EU law, Claimants adopt the framework of the Vienna Convention on the Law of Treaties ("**VCLT**") as the starting point for the relevant analysis.[447]

468. In a nutshell, Respondent argues that Claimants' claims are barred due to the incompatibility of the BIT with EU law. Respondent contends that Estonia's accession to the EU on 1 May 2004, or the entry in force of the Lisbon Treaty, had the effect of terminating the BIT and of "[conferring] upon investors and investments from other EU Member States a vast array of rights of free establishment, free movement of capital and services, and post-establishment treatment and operations."[448] According to Respondent, "[t]hese rights are directly enforceable before Member State courts and prevail over conflicting provisions of Estonian domestic law."[449] Alternatively, it argues that, should the analysis be conducted pursuant to the VCLT, the outcome would remain unchanged.

469. Considering the several procedural developments reported above and the extensive submissions by the Parties, as well as by the European Commission, the Tribunal will review and comment on those submissions chronologically, before closing with its overall conclusion regarding this important question.

1) Respondent's Counter-Memorial and Rejoinder

470. For the Respondent, "[t]he degree of incompatibility between the Treaty and EU law is so great that the Treaty (including its Article 9) must be considered as having been terminated by virtue

[446] Namely: Resp. C-M, ¶¶347-380; Cl. Reply, ¶¶570-601; Resp. Rej., ¶¶324-352; Resp. PHB, ¶279; Cl. PHB, ¶575; Respondent's Submission on Jurisdiction of the Tribunal in Light of the Judgment of the CJEU in *Achmea* ("**Respondent's Observations on the *Achmea* Judgment**") (29 March 2018); Claimants' Observations on the *Achmea* Judgment (29 March 2018); *Amicus Curiae* Brief of the European Commission (10 October 2018) ("**European Commission *Amicus Curiae***"); Claimants' Comments on the European Commission's *Amicus Curiae* (1 November 2018); Respondent's Comments on the European Commission's *Amicus Curiae* (1 November 2018); Estonia Comments on the EU Majority Declaration (8 February 2019); Claimants Comments on the EU Majority Declaration, (8 February 2019).

[447] Cl. Reply, ¶¶570-601.

[448] Resp. C-M, ¶348.

[449] Resp. C-M, ¶¶347-349.

of Estonia's accession to the EU Treaties, or the entry into force of the Lisbon Treaty, at the latest."[450]

471. As mentioned above, Respondent premises its reasoning on the proposition that since EU law forms part of international law, the Tribunal must apply EU law. While there is no doubt that EU law is international law, the Tribunal considers that Respondent's position overlooks the existence of sub-sets of international law, as discussed more fully below.

472. Respondent relies on the first paragraph of Art. 351 of the Treaty on the Functioning of the European Union ("**TFEU**"), which provides:

> The rights and obligations arising from agreements concluded before 1 January 1958 or, for acceding States, before the date of their accession, between one or more Member States on the one hand, and one or more third countries on the other, shall not be affected by the provisions of the Treaties.[451]

473. According to Respondent, the application of the *pacta sunt servanda* principle enshrined in Art. 351 TFEU is limited to agreements between, on the one hand, EU Member States and, on the other hand, non-EU countries. This principle does not, in Respondent's view, apply to intra-EU treaties, over which EU law takes precedence.[452]

474. Respondent contends accordingly that Art. 9 of the BIT, which provides that disputes arising out of the Treaty may be submitted to international arbitration, is incompatible with Art. 344, 267 and 18 TFEU. Furthermore, Estonia submits that under both EU law and public international law (as per the VCLT, addressed below), the BIT is inoperable as a result of this incompatibility to the extent that disputes falling under the BIT involve the application of Estonian law, which in turns includes EU law.[453]

475. First, Respondent posits that Art. 9 BIT runs afoul Art. 344 and 267 TFEU, which address the settlement of disputes regarding the interpretation/application of EU law:[454]

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[450] Resp. C-M, ¶349.

[451] **RL-125**, Treaty on Functioning of the European Union (2009), Art. 351.

[452] Resp. C-M, ¶¶368 and 369. Respondent refers to the CJEU decision *Commission v Italy*, where the Court commented on the interaction of the GATT treaty and EU customs rules: "In fact, in matters governed by the EEC Treaty, that Treaty takes precedence over agreements concluded between Member States before its entry into force, including agreements made within the framework of GATT," **RL-136**, CJEU, Case 10/61, *Commission v Italy* (1962), p 10. Respondent also notes that this interpretation was recognised by the ICSID tribunal in *Electrabel S.A. v Republic of Hungary*, ICSID Case No. ARB/07/19, Decision on Jurisdiction (30 November 2012), ¶4.183 (**CL-107**) [*Electrabel* (Decision on Jurisdiction)].

[453] Resp. C-M, ¶¶365-380.

[454] Resp. C-M, ¶¶356-360; Resp. Rej, ¶¶337-340.

> Article 344 (ex Article 292 TEC)
>
> Member States undertake not to submit a dispute concerning the interpretation or application of the Treaties to any method of settlement other than those provided for therein.
>
> Article 267 (ex Article 234 TEC)
>
> The Court of Justice of the European Union shall have jurisdiction to give preliminary rulings concerning:
>
> (a) the interpretation of the Treaties;
>
> (b) the validity and interpretation of acts of the institutions, bodies, offices or agencies of the Union;
>
> Where such a question is raised before any court or tribunal of a Member State, that court or tribunal may, if it considers that a decision on the question is necessary to enable it to give judgment, request the Court to give a ruling thereon.
>
> Where any such question is raised in a case pending before a court or tribunal of a Member State against whose decisions there is no judicial remedy under national law, that court or tribunal shall bring the matter before the Court.
>
> If such a question is raised in a case pending before a court or tribunal of a Member State with regard to a person in custody, the Court of Justice of the European Union shall act with the minimum of delay.

476. These provisions have been interpreted as providing exclusive competence to the CJEU over the interpretation of EU treaties.[455] Respondent also refers to Opinion 1/09 of the CJEU, which deemed the creation of a unified patent litigation system through international agreement incompatible with EU law.[456] The CJEU reasoned that this system would infringe its monopoly over the rendering of judgements concerning significant issues of EU law.[457]

477. Second, Respondent argues that Art. 9 BIT is incompatible with Art. 18 TFEU, which prohibits discrimination among EU nationals:[458]

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[455] **RL-131**, *Iron Rhine Railway* (Belgium/Netherlands), PCA, Award (24 May 2005), ¶201.

[456] **RL-128**, CJEU, Opinion 1/09 [2011] ECR I-0137, ¶89.

[457] **RL-128**, CJEU, Opinion 1/09 [2011] ECR I-0137, ¶¶63 and 78.

[458] Resp. C-M, ¶¶361-364; Resp. Rej, ¶¶331-336.

> Article 18 (ex Article 12 TEC)
>
> Within the scope of application of the Treaties, and without prejudice to any special provisions contained therein, any discrimination on grounds of nationality shall be prohibited.
>
> The European Parliament and the Council, acting in accordance with the ordinary legislative procedure, may adopt rules designed to prohibit such discrimination.

478. Respondent refers then to the *amicus curiae* observations of the European Commission in the *Achmea v Slovakia* matter, where it submitted that intra-EU BITs lead to discrimination among EU State Members.[459]

479. As to consequence of this alleged incompatibility between Art. 9 of the BIT and the EU law provisions reported above, Respondent asserts: "As a result of the conflict between Article 9 of the Treaty and mandatory provision of EU law, Article 9 is inoperative."[460] It is unclear whether Respondent refers here, implicitly, to a peremptory norm of general international law (or *jus cogens*) – being the only norm that can render a treaty automatically void pursuant to Article 64 VCLT.[461] In any case, in the Tribunal's view it can hardly be argued that EU law rules constitute rules of *jus cogens*.

480. In order to canvass all possible avenues, Respondent also contends that even if Articles 30(3) VCLT, which addresses the application of successive treaties relating to the same subject matter, and 59 VCLT, which addresses the termination or suspension of a treaty implied the conclusion of a later treaty, were to apply, the result would be the same: EU law having the same subject-matter and being incompatible with the earlier BIT, EU law - not the Treaty – would apply.

2) Claimants' Reply Memorial

481. Adopting what the Tribunal itself considers to be the correct approach, that is, the application of general international law, Claimants argue that "[t]he BIT is not 'implicitly abrogated' by Art. 59(1) VCLT because (a) the operation of that provision is subject to the provisions of Art. 65 VCLT that prevents automatic termination by operation of law, and (b) the requirements of Article 59(1) VCLT itself are not met."[462]

482. The Tribunal agrees with Claimants that – as already mentioned – a treaty can only terminate automatically where the instrument contravenes a norm of *jus cogens*, and that the EU law rules at issue are not of such imperative nature. In all other situations of conflict between

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[459] **RL-133**, Observations by the European Commission in the arbitration between *Eureko BV (The Netherlands) v The Slovak Republic* (7 July 7. 2010), ¶33. See also **RL-228**, European Commission, Commission Staff Working Document on the Free Movement of Capital in the EU (April 2013), p 11.

[460] Resp. C-M, ¶365.

[461] Art. 64 VCLT reads: "If a new peremptory norm of general international law emerges, any existing treaty which is in conflict with that norm becomes void and terminates."

[462] Cl. Reply, ¶576.

treaties, including where Art. 59 VCLT apply, the VCLT mandates the following of the procedures set out at its Art. 65 to 68.

483. Claimants correctly point out that, before these procedures can be applied, two (2) conditions precedent must be met: "(1) the later treaty must relate to the 'same subject-matter' as the earlier treaty; and (2) 'the provisions of the later treaty are so far incompatible with those of the earlier one that the two treaties are not capable of being applied at the same time'."[463] [Emphasis in original omitted]

484. The Tribunal agrees with Claimants that none of these conditions are fulfilled: the TFEU does not share the "same subject-matter" as the BIT; and there is no incompatibility between Article 9 of the BIT and the EU treaties, including Art. 18, 267 and 344 TFEU. As Claimants convincingly explain, there is no incompatibility between the BIT and Article 18, as the BIT does not discriminate on the basis of nationality since it in no way prevents rights being granted to nationals of other Member States. There is also no incompatibility between the BIT and Art. 267 TFEU, as there exist a variety of means by which the CJEU can be seized of a request to redress any misapplication or misinterpretation of EU law.[464] And there is no incompatibility with Article 344 TFEU, as this article only applies to inter-State arbitrations.

485. Furthermore, Claimants argue that the BIT cannot be rendered inoperative by application of Art. 30(3) VCLT or Art. 351 TFEU, for the same reasons already indicated, *i.e.* the absence of the existence of the "same subject-matter" and of an incompatibility.

3) The *Achmea* Judgment

486. After the exchange of the Parties' submissions discussed above, the CJEU rendered the *Achmea* Judgment. As mentioned above at paragraphs 86 and 87, Respondent obtained leave to file a copy of this judgement, and the Parties were granted the opportunity to provide their observations on the relevance or non-relevance of this development.

487. The *Achmea* Case results from the referral by the German Federal Court of Justice to the CJEU for a preliminary ruling under Art. 267 TFEU in the context of the *Achmea v Slovakia* arbitration, commented below at paragraphs 549-551, and opposing Slovakia to Achmea BV, a Dutch national. The CJEU was asked to interpret Art. 18, 267 and 244 TFEU, all of which provisions are relied on by Estonia in the present proceeding. More specifically, the *Achmea* Judgment addresses whether (1) Art. 344 TFEU precludes the application of a dispute resolution provision contained in an intra-EU BIT and, alternatively, (2) whether Art. 267 TFEU precludes the application of such a provision.[465]

488. In brief, the CJEU held that the arbitration provisions contained in intra-EU BITs are incompatible with EU law. It found that arbitral tribunals constituted under such instruments

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[463] Cl. Reply, ¶581.

[464] The tribunal in *Electrabel* makes an exhaustive list of these means, **CL-107**, *Electrabel* (Decision on Jurisdiction), *supra* note 452.

[465] **RL-251**, *Achmea* Judgment, *supra* note 17, ¶23. The CJEU was also requested to consider Art. 18 TFEU but this issue became superfluous considering the responses to the two (2) first questions.

might be called on to interpret and/or apply EU law, given that that EU law forms part of the law of the contracting parties to the BIT[466] and in view of the nature of EU law.[467] The CJEU also concluded that such arbitral tribunals are not situated within the EU judicial system and, more specifically, cannot be regarded as a court within the meaning of Art. 267 TFEU.[468] The CJEU next inquired whether an intra-EU BIT arbitral tribunal is subject to control by a court of a Member State, and would allow the referral of issues of EU law to the CJEU. It concluded that this was not the case because the controlling authority by a court depends on the locus of the seat of arbitration, which may not be in the European Union. Additionally, control over an arbitral award, as opposed to the conduct of the arbitral tribunal itself, would be too limited to be considered as sufficient.[469] In the light of the foregoing, the CJEU held that intra-EU BIT arbitrations are not compatible with EU law:

> 58 In the present case, however, apart from the fact that the disputes falling within the jurisdiction of the arbitral tribunal referred to in Article 8 of the BIT may relate to the interpretation both of that agreement and of EU law, the possibility of submitting those disputes to a body which is not part of the judicial system of the EU is provided for by an agreement which was concluded not by the EU but by Member States. Article 8 of the BIT is such as to call into question not only the principle of mutual trust between the Member States but also the preservation of the particular nature of the law established by the Treaties, ensured by the preliminary ruling procedure provided for in Article 267 TFEU, and is not therefore compatible with the principle of sincere cooperation referred to in paragraph 34 above.
>
> 59 In those circumstances, Article 8 of the BIT has an adverse effect on the autonomy of EU law.

[466] On this latter point, the CJEU found that "EU law is characterized by that fact that it stems from an independent source of law, the Treaties, by its primacy over the laws of the Member States, and by the direct effect of a whole series of provisions which are applicable to their nationals and to the Member States themselves. Those characteristics have given rise to a structured network of principles, rules and mutually interdependent legal relations binding the EU and its Member States reciprocally and binding its Member States to each other," *Achmea* Judgment, *supra* note 17, ¶33.

[467] **RL-251**, *Achmea* Judgment, *supra* note 17, ¶¶40-42.

[468] **RL-251**, *Achmea* Judgment, *supra* note 17, ¶¶43-49. Intra-EU BITs tribunals would not form part of the EU judicial system because they would not be connected to the judicial systems of the Member States.

[469] **RL-251**, *Achmea* Judgment, *supra* note 17, ¶¶50-56. On this latter point, the CJEU distinguished commercial arbitrations and investor-state proceedings as follows: "However, arbitration proceedings such as those referred to in Article 8 of the BIT are different from commercial arbitration proceedings. While the latter originate in the freely expressed wishes of the parties, the former derive from a treaty by which Member States agree to remove from the jurisdiction of their own courts, and hence from the system of judicial remedies which the second subparagraph of Article 19(1) TEU requires them to establish in the fields covered by EU law (see, to that effect, judgment of 27 February 2018, Associação Sindical dos Juízes Portugueses, C-64/16, EU:C:2018:117, paragraph 34), disputes which may concern the application or interpretation of EU law. In those circumstances, the considerations set out in the preceding paragraph relating to commercial arbitration cannot be applied to arbitration proceedings such as those referred to in Article 8 of the BIT." (at ¶55).

60 Consequently, the answer to Questions 1 and 2 is that Articles 267 and 344 TFEU must be interpreted as precluding a provision in an international agreement concluded between Member States, such as Article 8 of the BIT, under which an investor from one of those Member States may, in the event of a dispute concerning investments in the other Member State, bring proceedings against the latter Member State before an arbitral tribunal whose jurisdiction that Member State has undertaken to accept.[470]

4) Respondent's Observations on the *Achmea* Judgment[471]

489. On the one hand, Respondent argues that the *Achmea* Judgment confirms that the Tribunal lacks jurisdiction. It first submits that the judgement applies to the current proceeding since the CJEU's reasoning does not hinge on the particulars of the dispute at play, but rather on the mere possibility that a tribunal constituted under an intra-EU BIT may be asked to interpret or apply EU law, and that the judgement does not distinguish between the various procedural avenues for investor-state arbitration.[472] Considering that the *Achmea* Judgment does not specify any temporal limitation to the incompatibility between investor-state dispute resolution and EU law, Respondent also posits that such incompatibility arose as of Estonia's EU accession on 1 May 2004.[473]

490. Respondent further argues that the *Achmea* Judgment is binding on the Tribunal because: (i) it forms part of public international law, (ii) the CJEU has exclusive authority to adjudicate on the EU law matters pursuant to Art. 19 TEU and (iii) the Tribunal has a duty to avoid issuing an unenforceable award, which risk would likely materialise (should the Tribunal find that it has jurisdiction) considering the principle of supremacy of EU law.[474] Finally, Respondent restates that the incompatibility between Art. 9 of the BIT and Art. 4(3) TEU and Art. 267 and 344 TFEU renders the former inapplicable.[475]

491. Respondent also reiterates that Art**.** 351 TFEU is the applicable conflict rule,[476] including with respect to pre-accession instruments such as the BIT, and automatically renders Art. 9 of the BIT inapplicable. As a result, the offer to arbitrate contained in Art. 9 of the BIT would have been invalidated upon Estonia's accession to the EU in 2004.

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[470] **RL-251**, *Achmea* Judgment, *supra* note 17, ¶¶58-60.

[471] Dated 29 March 2018.

[472] Respondent's Observations on the *Achmea* Judgment, ¶¶5-16.

[473] Respondent's Observations on the *Achmea* Judgment, ¶¶17-19.

[474] Respondent's Observations on the *Achmea* Judgment, ¶¶20-31.

[475] Respondent's Observations on the *Achmea* Judgment, ¶¶32-51.

[476] Respondent's Observations on the *Achmea* Judgment, ¶36.

5) Claimants' Observations on the *Achmea* Judgment[477]

492. For their part, Claimants submit that the *Achmea* Judgment fails to address the nature of the particular arbitration agreement at issue here insofar as Art. 9 of the BIT only contains an offer to arbitrate.[478] Claimants emphasise that this arbitration agreement was concluded upon the filing of their Request of Arbitration and that the parties' consent may not be withdrawn.[479] Claimants also argue that the Tribunal is not bound by the *Achmea* Judgment considering that it is not appointed pursuant to the EU Treaties and, indeed, investment treaty-based tribunals have rejected similar jurisdiction objections in other cases.[480] Furthermore, Claimants contend that the *Achmea* Judgment is not relevant given *inter alia* the most favourable treatment clause contained at Art. 3(5) of the BIT.[481]

6) The European Commission *Amicus Curiae* Submission[482]

493. The Tribunal authorised the intervention of the European Commission by way of the filing of an *amicus curiae* brief limited to "the legal consequences of the judgment of the Court of Justice in *Achmea* for the case before your Arbitral Tribunal."[483]

494. The main contention of the European Commission is that "the offer of Estonia and the corresponding offer of the Netherlands to investors from the other Contracting Party to enter into investment arbitration is no longer valid since 1 May 2004, when Estonia acceded to the European Union […]."[484]

495. This statement is based on two (2) premises: the retroactive application of the *Achmea* Judgment; and its binding effect on an international arbitral tribunal.

496. First, the Commission contends that the *Achmea* Judgment applies retroactively because this decision, "just like any judgment of the Court of Justice, applies, as a matter of principle, from the date of its entry into force (*ex tunc*), because the Court only interprets the law, and does not create new law."[485]

497. Second, the Commission posits that the *Achmea* Judgment binds international arbitral tribunals because these bodies must apply international law, which includes EU law.

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[477] Dated 29 March 2018.

[478] Claimants' Observations on the *Achmea* Judgment, ¶¶10 and 11.

[479] Claimants' Observations on the *Achmea* Judgment, ¶¶13-16.

[480] Claimants' Observations on the *Achmea* Judgment, ¶¶17-22.

[481] Claimants' Observations on the *Achmea* Judgment, ¶¶23-40.

[482] Dated 18 October 2018.

[483] Decision on the Application for Leave to Intervene as a Non-Disputing Party Submitted by the European Commission (2 October 2018), ¶¶12 and 17 3).

[484] European Commission *Amicus Curiae*, ¶2.

[485] European Commission *Amicus Curiae*, ¶10.

498. The European Commission, however, appears to disregard the CJEU's reasoning on Article 8,[486] where the Court rightly (in the Tribunal's view) indicates that EU law has a dual nature[487] in the sense that it "must be regarded both as forming part of the law in force in every Member State and as deriving from an international agreement between the Member States."[488] The CJEU did not qualify EU law as "general principles of international law" and, although not explicitly mentioned by the CJEU, EU law clearly derives from international law agreements (the EU treaties). What should be added, as far as the Tribunal is concerned, is that EU law and the BIT belong to two (2) distinct subsystems of international law. The *Achmea* Judgment cannot, as of consequence, bind an international entity asserting its jurisdiction based on the BIT.

499. The Commission goes further by stating that even when considering EU law solely in its domestic facet (*i.e.* as part of Estonian national law), it would also be applicable and binding on the Tribunal. This, however, disregards the principle that national law cannot trump international law, as recorded at Art. 27 VCLT.[489]

500. The European Commission also purports to apply EU law conflict rules that would, in its view, prevail over international law rules (*i.e.* Art. 30(3) to (5) VCLT).[490] The first of these is said to be embodied in Declaration 17 to the Lisbon Treaty, which the Commission says establishes the primacy of EU law. The second conflict rule referred to is Art. 351(1) TFEU, reproduced above at paragraph 472 above.

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[486] Article 8 of the Netherlands-Slovakia BIT reads: "1. All disputes between one Contracting Party and an investor of the other Contracting Party concerning an investment of the latter shall if, possible, be settled amicably.

2. Each Contracting Party hereby consents to submit a dispute referred to in paragraph 1 of this Article to an arbitral tribunal, if the dispute has not been settled amicably within a period of six months from the date on which either party to the dispute requested amicable settlement. […]

6. The arbitral tribunal shall decide on the basis of the law, taking into account in particular though not exclusively:

– the law in force of the Contracting Party concerned;

– the provisions of this Agreement, and other relevant agreements between the Contracting Parties;

– the provisions of special agreements relating to the investment;

– the general principles of international law."

[487] This was for example explicitly mentioned by the tribunal in *AES Summit Generation Limited and AES-Tisza Erömü Kft v The Republic of Hungary*, ICSID Case No. ARB/07/22, Award (23 September 2010) (**RL-154**) [*AES v Hungary*]: "7.6.6 Regarding the Community competition law regime, it has a dual nature: on the one hand, it is an international law regime, on the other hand, once introduced in the national legal orders, it is part of these legal orders."

[488] **RL-251**, *Achmea* Judgment, *supra* note 17, ¶41.

[489] Art. 27 VCLT reads: "A party may not invoke the provisions of its internal law as justification for its failure to perform a treaty."

[490] European Commission *Amicus Curiae*, ¶32.

501. The Commission argues that "in matters governed by the EU Treaties, EU law takes precedence over international treaties concluded between Member States, regardless of whether they were concluded before or after EU accession."[491] It relies not only on the positive interpretation of this article, but also what has been called its negative interpretation as notably articulated in the *Electrabel* award.[492]

502. As further discussed below, the Tribunal does not consider that *Electrabel* supports such reasoning. The *Electrabel* tribunal found that Art. 351 TFEU, under both its negative and positive interpretation, only applies if the TFEU and the other treaty have the same subject-matter and are incompatible. It concluded that none of these two (2) conditions were met in that case.

503. In the Tribunal's view, the Commission's reasoning also disregards the fact that while Art. 351(1) TFEU might well govern conflicts of laws within the European legal order, the Tribunal is not situated within that legal system. Rather, it is situated in the international legal order stemming from the BIT and the ICSID Convention, where conflicts are resolved pursuant Articles 30 and 59 VCLT.

504. Finally, the European Commission argues that the Tribunal is bound by the *Achmea* Judgment's pronouncement to the effect that EU law precludes investment arbitration clauses, such as the one at Art. 9 (1) of the BIT. Again, however, while this reasoning might be correct on a strict EU law point of view, it does not apply outside the EU legal order.

505. In the alternative, the European Commission argues that even if, as this Tribunal considers to be the case, the conflict rules of the VCLT (*i.e.* Articles 59 and 30(1)) apply, EU law would still prevail. The European Commission in fact concentrates its analysis on Art. 30(1), which addresses the application of successive treaties.[493]

506. While Art. 30 VCLT clearly treats the identity of subject-matter and the incompatibility as two (2) distinct conditions, the European Commission argues that "'same subject matter' and 'conflict' are one and the same thing." Art. 30 VCLT would therefore apply owe to the alleged conflict between EU law and the BIT. In the Tribunal's view, this can be explained by the fact that, although the CJEU indeed found a conflict between EU law and arbitration clauses in intra-EU BITs, it did not analyse whether EU treaties and intro-EU BITs share the same subject-matter, which is far from evident.

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[491] European Commission *Amicus Curiae*, ¶34.

[492] The European Commission explicitly refer to the articulation of this interpretation by the *Electrabel* tribunal: "If Article 307 EC [now Article 351(1) of TFEU] provides that treaty rights between Non-EU Members cannot be jeopardised by the subsequent entry of a Non-EU State into the European Union, it appears logical, taking into account the integration processes of the European Union, that the opposite consequence should be implied, i.e. the non-survival of rights under an earlier treaty incompatible with EU law as between Member States," **CL-107**, *Electrabel* (Decision on Jurisdiction), *supra* note 452, ¶4.183.

[493] The text of Art. 30 VCLT is reproduced below at paragraph 537.

7) Respondent's Comments on the European Commission *Amicus Curiae*[494]

507. According to Respondent, the European Commission *Amicus Curiae* confirms that the *Achmea* Judgment applies to the present case since (i) it declares an incompatibility between EU law and the arbitration agreement of the Netherlands-Slovakia BIT, which closely mirrors Art. 9 of the BIT, and (ii) the BIT was entered into prior to Estonia's accession to the EU, on 1 May 2004. The BIT has thus been invalid from the moment Estonia became an EU member and, as of consequence, the BIT has not, from that time, included a valid offer to arbitrate from Estonia that Claimants could have accepted.

508. Respondent reiterates that the *Achmea* Judgement binds the Tribunal as it forms part of international law. This argument has already been addressed: it ignores that international law is composed of various sub-systems and that the EU legal system is different than that in which the ICSID Convention and the BIT are situated.

509. Respondent also submits that because of the stated conflict, "[t]he immediate consequence of this conflict was that the arbitration clause in Article 9 of the Treaty became automatically inapplicable on the same day."[495] Respondent insists on this point stating: "The Commission confirms that the effect of such incompatibility between EU law and an inter se international agreement – such as the Treaty – is that conflicting provisions of the latter are automatically inapplicable even if the relevant EU Member States – such as Estonia and the Netherlands – have not yet formally removed the conflicting instrument from their legal order."[496] [Emphasis omitted] Yet, as already indicated by the Tribunal, the only instance of automatic annulment of an international treaty is where the instrument in question is in conflict with a rule of *jus cogens*, which is not the situation here.

510. In the Tribunal's view, all of Respondent's arguments bear the same flaw, being that they are confined to the EU legal order and the so-called primacy of EU law within that order. Whereas this hierarchy of norms certainly apply within the EU law system, it has no reach is beyond its limits.

511. Respondent, following the European Commission, accepts for the sake of argument to analyse the issues under international law and to apply Art. 30(3) VCLT. Contrarily to the European Commission, it does not conflate the conditions of "same subject-matter" and "conflict" but limits itself to asserting that EU law and the BIT do have the same subject-matter.

8) Claimants' Comments on the European Commission *Amicus Curiae*[497]

512. Claimants are highly critical of the European Commission *Amicus Curiae*. They state:

> As was to be expected, given the political campaign the Commission has waged against intra-EU BITs, the Commission's Brief takes the

[494] Dated 1 November 2018.

[495] Respondent's Comments on the European Commission *Amicus Curiae*, ¶29.

[496] Respondent's Comments on the European Commission *Amicus Curiae*, ¶35.

[497] Dated 1 November 2018.

> position that the legal consequences of *Achmea* are that the Tribunal does not have jurisdiction. However, the Commission's Brief overstates the effect of and significance of *Achmea*, fails to engage properly with the decisions of arbitration tribunals since *Achmea* which have made clear that its effect is much more limited that [sic] the Commission would like, and misrepresents the position of the parties to the BIT and legal authority to support its campaign. The Commission's arguments should be rejected by this Tribunal.[498]

513. Claimants – rightly in the Tribunal's view – consider the issue from the perspective of international law, from which the two (2) sources of the arbitration agreement, *i.e.* the ICSID Convention and the BIT, originate. Upon review of these two (2) agreements, it is beyond doubt in their view that a valid ICSID arbitration was concluded between Estonia and Claimants.

514. Claimants submit that "[t]he Commission's Brief overstates the significance of *Achmea* in order to claim that the Tribunal in this case lacks jurisdiction."[499] Claimants' criticism is directed principally to certain elements of the *Achmea* Judgment: first, they mention that "the CJEU draws a confused (and misplaced) distinction in *Achmea* between commercial arbitrations on the one hand, and investment treaty arbitrations on the other […]"[500]; second, they claim that "the CJEU's decision in *Achmea* does not explain the consequence of its finding that Article 8 of the NL-SK BIT is incompatible with the TFEU, in terms of the validity of the arbitration agreement […]"[501]; and they conclude that the European Commission's opinion on the consequence on the *Achmea* Judgment is merely a "view" of the latter.[502]

515. In order to refute the European Commission argument that the BIT must be considered as automatically void because such it would contravene the common will of the BIT's parties as expressed further to the *Achmea* Judgment, Claimants point out that the declaration of the Dutch minister referred to by the European Commission indicates The Netherlands' intent to terminate the Dutch intra-EU BITs, which necessarily implies that these treaties could not have been automatically terminated.[503]

516. Claimants also rely on the award rendered in the *UP and CD Holding v Hungary* case, which was strongly criticised by Respondent, and approve its reasoning to the effect that the case at hand and the *UP and CD Holding v Hungary* arbitration proceed under the ICSID Convention, whereas the underlying arbitration to the *Achmea* Case was governed by the UNCITRAL rules.[504]

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[498] Claimants' Comments on the European Commission *Amicus Curiae*, ¶2.

[499] Claimants' Comments on the European Commission *Amicus Curiae*, ¶8.

[500] Claimants' Comments on the European Commission *Amicus Curiae*, ¶10.

[501] Claimants' Comments on the European Commission *Amicus Curiae*, ¶11.

[502] Claimants' Comments on the European Commission *Amicus Curiae*, ¶12.

[503] Claimants' Comments on the European Commission *Amicus Curiae*, ¶13.

[504] Claimants' Comments on the European Commission *Amicus Curiae*, ¶¶14-18.

517. With regards to the application of conflict rules, Claimants do not deny that international law is applicable and that EU is part of international law. But contrary to the European Commission, which considers international law as an undifferentiated body of international law, Claimants present a more subtle analysis, with which the Tribunal agrees. According to Claimants, "elements of EU law do form part of international law, in the sense that EU law, as a system established by treaty, is one legal system that sits within the broader framework of international law, alongside multiple other elements of international law, such as investment treaties […]."[505]

518. The existence of different sub-systems of international law requires the application of conflict rules. In that respect, Claimants criticise the European Commission's reliance on the EU law primacy principle, in the following terms, with which the Tribunal agrees:

> The Commission's argument as to the primacy of EU law is made from the perspective of the CJEU, and in reliance upon a concept that in itself is a construct of the CJEU. The fact that the CJEU may be of the opinion that EU law has primacy over other treaties is not determinative of the position of EU law in the hierarchy of different legal systems from an international law perspective.[506]

519. Claimants also contest the alternative analysis of the European Commission of the VCLT conflict rules, explaining that the European Commission misapplied these rules in trying to conflate the two (2) conditions of "same subject-matter" and "conflict." According to Claimants, "the TFEU and the BIT do not relate to the same subject matter. As a result, neither Article 30 nor Article 59 VCLT is applicable."[507] Claimants, for the sake of completeness, add that even if the TFEU and the BIT would be considered as relating to the same subject matter, they would not be incompatible and, should they be incompatible, this would either automatically terminate the BIT or invalidate the Parties' ICSID arbitration agreement.

520. Claimants conclude that, even if their international law argument fail and Estonia's accession to the EU had for effect that Art. 9 of the BIT become in breach of EU law from thereon, Estonia did not, as both a matter of fact and international law, withdraw its consent to arbitrate under Art. 9 of the BIT. As a consequence, the Tribunal has jurisdiction over the Claimants' claim.

9) The Declaration of the Majority of EU Member States of 15 January 2019[508]

521. On 15 January 2019, a majority of EU Member States, including Estonia and The Netherlands, adopted a declaration seeking to address the consequences of the *Achmea* Judgment (the "**EU Majority Declaration"**), which states *inter alia*:

> In its judgment of 6 March 2018 in Case C-284/16, Achmea v Slovak Republic *(*'the *Achmea* judgment'), the Court of Justice of the

[505] Claimants' Comments on the European Commission *Amicus Curiae*, ¶20.

[506] Claimants' Comments on the European Commission *Amicus Curiae*, ¶23.

[507] Claimants' Comments on the European Commission *Amicus Curiae*, ¶31.

[508] Declaration of the Representatives of the Governments of the Member States of 15 January 2019 on the legal consequences of the judgment of the Court of Justice in Achmea and on investment protection in the European Union, **RL-276** [the "**EU Majority Declaration**"]. Two (2) other declarations were adopted on 16 January by a minority of EU Member States.

European Union held that "*Articles 267 and 344 [... of the Treaty on the Functioning of the European Union] must be interpreted as precluding a provision in an international agreement concluded between Member States, [...] under which an investor from one of those Member States may, in the event of a dispute concerning investments in the other Member State, bring proceedings against the latter Member State before an arbitral tribunal whose jurisdiction that Member State has undertaken to accep*t" ("investor-State arbitration clauses").

Member States are bound to draw all necessary consequences from that judgment pursuant to their obligations under Union law.

Union law takes precedence over bilateral investment treaties concluded between Member States. As a consequence, all investor-State arbitration clauses contained in bilateral investment treaties concluded between Member States are contrary to Union law and thus inapplicable. They do not produce effects including as regards provisions that provide for extended protection of investments made prior to termination for a further period of time (so-called sunset or grandfathering clauses). An arbitral tribunal established on the basis of investor-State arbitration clauses lacks jurisdiction, due to a lack of a valid offer to arbitrate by the Member State party to the underlying bilateral investment Treaty. […]

Taking into account the foregoing, Member States declare that they will undertake the following actions without undue delay:

1. By the present declaration, Member States inform investment arbitration tribunals about the legal consequences of the *Achmea* judgment, as set out in this declaration, in all pending intra-EU investment arbitration proceedings brought either under bilateral investment treaties concluded between Member States or under the Energy Charter Treaty.

2. In cooperation with a defending Member State, the Member State, in which an investor that has brought such an action is established, will take the necessary measures to inform the investment arbitration tribunals concerned of those consequences. Similarly, defending Member States will request the courts, including in any third country, which are to decide in proceedings relating to an intra-EU investment arbitration award, to set these awards aside or not to enforce them due to a lack of valid consent.

3. By the present declaration, Member States inform the investor community that no new intra-EU investment arbitration proceeding should be initiated.

4. Member States which control undertakings that have brought investment arbitration cases against another Member State will take steps under their national laws governing such undertakings, in compliance with Union law, so that those undertakings withdraw pending investment arbitration cases.

> 5. In light of the *Achmea* judgment, Member States will terminate all bilateral investment treaties concluded between them by means of a plurilateral treaty or, where that is mutually recognised as more expedient, bilaterally.
>
> 6. Member States will ensure effective legal protection pursuant to the second subparagraph of Article 19(1) TEU under the control of the Court of Justice against State measures that are the object of pending intra-EU investment arbitration proceedings.
>
> 7. Settlements and arbitral awards in intra-EU investment arbitration cases that can no longer be annulled or set aside and were voluntarily complied with or definitively enforced before the *Achmea* judgment should not be challenged. Member States will discuss, in the context of the plurilateral Treaty or in the context of bilateral terminations, practical arrangements, in conformity with Union law, for such arbitral awards and settlements. This is without prejudice to the lack of jurisdiction of arbitral tribunals in pending intra-EU cases.
>
> 8. Member States will make best efforts to deposit their instruments of ratification, approval or acceptance of that plurilateral treaty or of any bilateral treaty terminating bilateral investment treaties between Member States no later than 6 December 2019. They will inform each other and the Secretary General of the Council of the European Union in due time of any obstacle they encounter, and of measures they envisage in order to overcome that obstacle.
>
> 9. Beyond actions concerning the Energy Charter Treaty based on this declaration, Member States together with the Commission will discuss without undue delay whether any additional steps are necessary to draw all the consequences from the Achmea judgment in relation to the intra-EU application of the Energy Charter Treaty. [Footnotes omitted]

10) Respondent's Comments on the EU Majority Declaration[509]

522. Estonia explains at the outset that its comments are intended to fulfil its obligation in the EU Majority Declaration to "inform investment arbitration tribunals about the legal consequences of the *Achmea* Judgment," as provided in the EU Majority Declaration.[510]

523. Respondent relies on the political statements of the Member States to support its objection to the Tribunal's jurisdiction. Again, in its view the Tribunal's lack of jurisdiction results from the principle of the primacy of EU law as enshrined in Declaration 17 to the Lisbon Treaty and Art. 351 TFEU and, alternatively, from Art. 30(3) VCLT. According to Estonia, this conclusion

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[509] Dated 8 February 2019.

[510] **RL-276**, EU Majority Declaration, *supra* note 508; Respondent's Comments on the EU Majority Declaration, pp 2-3.

stands notwithstanding the so-called sunset or grandfathering clause of the Treaty, as indicated in the EU Majority Declaration.

524. Respondent argues that the EU Majority Declaration is binding on the Tribunal, as it reflects the common understanding of both signatories to the BIT, The Netherlands and Estonia. It derives from this that the Tribunal was never presented with a valid arbitration agreement. It further explains that the constitution of the Tribunal predates the *Achmea* Judgment has no impact on this conclusion since the CJEU did specify any temporal limitation to the incompatibility of intra-EU investment arbitration clauses and EU law.

525. Last but not least, the EU Majority Declaration confirms, according to Respondent, that an award upholding the Tribunal's jurisdiction would be unenforceable. The Tribunal is not convinced by the relevance of such an argument, a will be developed below.

11) Claimants Comments' on the EU Majority Declaration[511]

526. Claimants submit that "[t]he Tribunal should base its decision on legal analysis and the rule of law, not on retroactive political statements made by the majority of EU Member States."[512] Claimants invite the Tribunal to consider the EU Majority Declaration into its European political context:

> As the Tribunal will be aware, the [European] Commission has, for many years, pursued a policy agenda favouring the removal of intra-EU BITs. However, up until the decision in *Achmea*, it has been unsuccessful in obtaining the support of EU member States. The Majority Declaration (and the declarations issued by the other Member States) represent a turning point in this process, with all EU Member States now agreeing to terminate the intra-EU BITs.[513] [Footnote omitted]

527. Claimants points out that, the Member States merely undertake to "inform" investment arbitral tribunals and the investor community of their interpretation of the *Achmea* Judgment, which denotes that the Member States had no intention of binding these tribunals.[514]

528. Moreover, Claimants do not agree with the statements in the EU Majority Declaration to the effect that there was never a valid arbitration clause. To the contrary, they argue that "Estonia's offer to arbitrate in the Netherlands-Estonia BIT was valid at the time it was accepted by the investor."[515] But even if Estonia offer to arbitrate is considered invalid under EU law by virtue of the *Achmea* Judgment, this indeed does not imply that this offer would be invalid under the ICSID Convention and the BIT.

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[511] Dated 8 February 2019.

[512] Claimants' Comments on the EU Majority Declaration, ¶2iii.

[513] Claimants' Comments on the EU Majority Declaration, ¶¶20-21.

[514] Claimants' Comments on the EU Majority Declaration, ¶3ii.

[515] Claimants' Comments on the EU Majority Declaration, ¶8.

529. Finally, Claimants also criticise the EU Majority Declaration for introducing a discrimination between ongoing arbitral proceedings, which would ought to be terminated, and "arbitral awards in intra-EU investment arbitration cases that can no longer be annulled or set aside and were voluntarily complied with or definitely enforced before the *Achmea* Judgment, [which] should not be challenged."[516]

530. Claimants' conclusion is straightforward: "The approach advocated in the Majority Declaration is contrary to the Rule of law, and should not be accepted by this Tribunal."[517]

12) Analysis of the Tribunal: the Tribunal's Jurisdiction and the Irrelevance of the *Achmea* Judgment

531. Although the Tribunal has made a number of comments in its review of the Parties' submissions, above, it considers it appropriate to wrap up its analysis, which it does here.

532. While EU law forms part of both Dutch and Estonian law and is relevant to public international law, the jurisdiction of the Tribunal arises from and is founded on the BIT and the ICSID Convention, as well as on the Parties' consent as required by these instruments. As a result, the question of jurisdiction is properly to be approached by analysing those agreements and the relevant facts from a public international law perspective.

533. It is useful to recapitulate the applicable rules of international law dealing with the invalidation, termination and suspension of the operation of treaties as embodied in the VCLT.

534. Art. 59(1) VCLT addresses those situations where a treaty is implicitly terminated or suspended. It reads:

> Article 59. Termination or suspension of the operation of a treaty implied by conclusion of a later treaty
>
> 1. A treaty shall be considered as terminated if all the parties to it conclude a later treaty relating to the same subject-matter and:
>
> (a) It appears from the later treaty or is otherwise established that the parties intended that the matter should be governed by that treaty; or
>
> (b) The provisions of the later treaty are so far incompatible with those of the earlier one that the two treaties are not capable of being applied at the same time.

535. Thus, three (3) conditions must be met for Art. 59 VCLT to apply: (1) identity of the parties to the treaties in question, (2) identity of "subject-matter" of those treaties, and (3) an incompatibility so great that the treaties cannot be applied concurrently.

536. Art. 65 VCLT concerns the procedure to be followed with respect to, *inter alia*, the termination or suspension of a treaty:

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[516] Claimants' Comments on the EU Majority Declaration, ¶23.

[517] Claimants' Comments on the EU Majority Declaration, ¶24.

Article 65. Procedure to be followed with respect to invalidity, termination, withdrawal from or suspension of the operation of a Treaty

(1) A party which, under the provisions of the present Convention, invokes either a defect in its consent to be bound by a treaty or a ground for impeaching the validity of a treaty, terminating it, withdrawing from it or suspending its operation, must notify the other parties of its claim. The notification shall indicate the measure proposed to be taken with respect to the treaty and the reasons therefor.

(2) If, after the expiry of a period which, except in cases of special urgency, shall not be less than three months after the receipt of the notification, no party has raised any objection, the party making the notification may carry out in the manner provided in article 67 the measure which it has proposed.

(3) If, however, objection has been raised by any other party, the parties shall seek a solution through the means indicated in Article 33 of the Charter of the United Nations.

537. Art. 30 VCLT addresses the application of successive treaties having the same subject-matter but which are not incompatible as a whole:

Article 30. Application of successive treaties relating to the same subject matter

(1) Subject to Article 103 of the Charter of the United Nations, the rights and obligations of States parties to successive treaties relating to the same subject-matter shall be determined in accordance with the following paragraphs.

(2) When a treaty specifies that it is subject to, or that it is not to be considered as incompatible with, an earlier or later treaty, the provisions of that other treaty prevail.

(3) When all the parties to the earlier treaty are parties also to the later treaty but the earlier treaty is not terminated or suspended in operation under article 59, the earlier treaty applies only to the extent that its provisions are compatible with those of the later treaty.

(4) When the parties to the later treaty do not include all the parties to the earlier one:

(a) As between a State party to both treaties the same rule applies as in paragraph 3;

(b) As between States parties to both treaties and a state party to only one of the treaties, the treaty to which both States are parties governs their mutual rights and obligations. [Emphasis added]

538. The Tribunal's analysis is based on these rules. Nothing argued by Estonia in this case persuades the Tribunal to adopt a different approach, or to reach a different conclusion than that arrived at by other investment arbitration tribunals, discussed below. As in those cases, the Tribunal finds that it cannot be said that Art. 9 of the Treaty (let alone the Treaty as a whole) is incompatible with the TFEU or EU law or has become inoperative. Moreover, absent the triggering of the termination process laid out at Art. 65 VCLT, it cannot be contended that the BIT terminated upon the accession of Estonia to the EU.

539. Furthermore, as hinted above and after due deliberation, the Tribunal respectfully considers that the CJEU's analysis rests on a different foundation, and so proceeds from a different premise than that which is applicable here. The arguments made by Estonia and the reasoning of the CJEU in the *Achmea* Judgment all assume that the issue must be considered through, and only through, the lens of EU law. Yet, for the reasons set out above, the Tribunal considers that the question before it must be approached from a public international law perspective.

540. The Tribunal also considers that it is not authoritatively bound by the *Achmea* Judgment, notwithstanding that the decision may form part of public international law. First, unlike the BIT interpreted by the CJEU, the Treaty on the basis of which Claimants instituted these proceedings does not refer to the domestic law of the Parties.[518] Second, the *Achmea* Judgment does not comment on the impact of instituting arbitral proceedings under the ICSID Convention. Third, the Tribunal is not convinced that Art. 19 TEU provides exclusive authority to the CJEU on the issue at play. Rather, in the Tribunal's view Art. 19 TEU arguably applies only to the extent that the interpretation and the application of the EU Treaties are required. This is not, however, the case in the matter at hand.

541. Lastly, the Tribunal is not persuaded by Estonia's argument concerning the potential difficulties of enforcement. Not only does the present award not require interpreting and/or applying EU law, more importantly, the prospect of potential difficulties enforcing an arbitral award should not prevent a tribunal from assuming rightful jurisdiction over a dispute.[519] The Tribunal is of course aware that it is preferable to render an award that will be easily enforceable. But it does not agree with the proposition that it is limited in its jurisdiction if potential issues exist that might arise at the enforcement stage. For example, ICSID tribunals routinely make awards against States, although Art. 55 of the ICSID Convention warns that "[n]othing in Article 54 [relating to enforcement of an ICSID award] shall be construed as derogating from the law in force in any Contracting State relating to immunity of that State or of any foreign State from execution." This Tribunal's jurisdiction is not determined by national rules governing the enforceability of arbitral awards, but by the Treaty, the ICSID Convention and international law. It will be up to the courts at the enforcement stage, if called upon, to draw the necessary

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[518] **RL-251**, *Achmea* Judgment, *supra* note 17, ¶4, quoting Art. 8(6) of the Slovakia-Czech Republic-Netherlands BIT: "The arbitral tribunal shall decide on the basis of the law, taking into account in particular though not exclusively: - <u>the law in force of the Contracting Party concerned</u>; - the provisions of this Agreement, and other relevant agreements between the Contracting Parties; - the provisions of special agreements relating to the investment; the general principles of international." [Emphasis added]

[519] In addition, as noted in a commentary filed by Respondent, most awards are voluntarily executed: **RL-255**, Martin Platte, An Arbitrator's Duty to Render Enforceable Awards, Vol. 20, Issue 3, Kluwer Law International (2003), p 310.

consequences from the *Achmea* judgment and their national laws with respect to the enforceability of this Award.

542. The only remaining question is whether, pursuant to Art. 30 VCLT, Art. 9 of the BIT can operate notwithstanding the accession of Estonia to the EU.

543. In applying Art. 30 VCLT, it must first be determined whether the TFEU and the BIT share the "same subject-matter." For the same reasons as discussed in *Oostergetel v Slovakia*, the Tribunal finds that the two do *not* concern the same subject-matter or address the same rights and obligations, primarily because the TFEU does not provide any mechanism for adjudicating disputes between EU Member States and private investors.

544. In any event, the Tribunal further agrees with Claimants that no incompatibility arises as between Art. 9 of the BIT and the TFEU.

545. Regarding the alleged incompatibility of the BIT with Art. 267 and 344 TFEU, the Tribunal adopts as its own the reasoning developed by the tribunal in *Electrabel v Hungary*: no rule of EU law explicitly or implicitly forbids the application of the arbitral mechanism set out in the Treaty and the ICSID Convention. Such a mechanism does not interfere with the jurisdiction of the CJEU and is not incompatible with the TFEU.

546. Regarding the alleged incompatibility of the BIT with Art. 18 TFEU, the Tribunal is not convinced that, as a matter of public international law, potential discrepancies as between the protections offered to the nationals of different EU State Members amounts to an incompatibility between the two (2) regimes. As submitted by Claimants, the BIT does not preclude nationals of other EU State Members being granted the same rights, and, by the same token, the BIT may be applied concurrently with the TFEU.

547. The Tribunal is comforted in its conclusions by decisions of other investment arbitral tribunals, which arrived at the same findings.

548. The issue of the compatibility of intra-EU BITs and EU law has indeed been discussed by several arbitral tribunals. Their most salient findings are canvassed below.

549. In *Achmea v Slovakia*, after noting that it does not derive its authority from EU law,[520] the tribunal proceeded by first deciding whether the BIT under consideration was terminated or otherwise incompatible with the EU Treaties by application of Art. 59 or 30 VCLT. It then addressed the issue of whether or not the BIT was inapplicable under EU law. In proceeding to its analysis, the tribunal discussed the respective scope of application of Art. 59 and 30 VCLT as follows:

> 239. The second main reason for dismissing this objection to jurisdiction is that the application of VCLT Article 59 is expressly limited to situations where there are successive treaties "relating to the same subject-matter" (see Article 59(1) cited above). The same phrase appears in VCLT Article 30 in a different context; but while the notion

[520] **RL-123**, *Achmea B.V. v. The Slovak Republic*, UNCITRAL, PCA Case No. 2008-13 (formerly *Eureko B.V. v. The Slovak Republic*), Award on Jurisdiction, Arbitrability and Suspension (26 October 2010), ¶225 [*Achmea v Slovakia*].

of "sameness" may be common to those two instances, the manner in which the overlap between the treaties is approached is manifestly not common. This is evident from the roles accorded by the VCLT to Articles 30 and 59.

240. Article 59 is concerned only with the termination of the entire treaty. Article 30, in contrast, is concerned with the priority between particular provisions of earlier and later treaties relating to the same subject-matter. While Article 30 is, therefore, focused on particular provisions, the question under Article 59 is whether the entire treaty should be terminated by reason of the adoption of a later treaty relating to the same subject-matter. The very fact that these situations are treated separately in the VCLT points to the need under Article 59 for a broader overlap between the earlier and later treaties than would be needed to trigger the application of Article 30.

241. This conclusion is borne out by a comparison of the terms of Article 30 and Article 59. Under Article 30 the test is whether the two successive treaty provisions are "compatible." Under Article 59 the test is whether the provisions of the later treaty are "so far incompatible with those of the earlier one that the two treaties are not capable of being applied at the same time." Article 30 may be triggered by the slightest incompatibility between the provisions of the earlier and later treaties. Article 59 clearly requires a broader incompatibility between the two treaties. [Emphasis added and omitted; Footnotes omitted]

550. The tribunal concluded that the two (2) provisions do not address the same type of overlap and, as such, the corresponding incompatibility required to trigger their application cannot be the same.[521] Art. 30 VCLT applies where Art. 59 does not, *i.e.*, where the provisions of successive are not such that *the two (2) treaties as a whole* are not capable of being applied at the same time.

551. Moreover, although Art. 59 VCLT speaks of termination or suspension of the operation of a treaty implied by the conclusion of a later instrument, the tribunal in *Achmea v Slovakia* found, and the point is restated here by Claimants,[522] that Art. 59 VCLT does not provide for the automatic termination of treaties, but rather describes the circumstances in which termination can be invoked "according to the Art. 65 procedure." The Tribunal agrees with this analysis.

552. In *Eastern Sugar v The Czech Republic*, a SCC tribunal analysed the issue exclusively pursuant to Art. 59 and 30 VCLT, implicitly excluding the possibility that EU law, on its own, could have the effect of rendering a BIT inoperable. The tribunal concluded that the BIT regime significantly differs from TFEU framework and that they do not cover the same subject-matter:[523]

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[521] On this point, see also **RL-233**, Mark E. Villiger, *Commentary on the 1969 Vienna Convention on the Law of Treaties*, BRILL (2009), pp 725-726.

[522] Cl. Reply, ¶579.

[523] **RL-132**, *Eastern Sugar v The Czech Republic*, SCC Case No. 088/2004, Partial Award (27 March 2007) [*Estern Sugar v The Czech Republic*].

> 159. First, the Arbitral Tribunal does not accept the Czech Republic's argument that the EU treaty as the later treaty (as between the Czech Republic and the Netherlands) covers the same subject matter as the BIT, the earlier treaty.
>
> 160. While it is true that European Union law deals with intra-EU cross-border investment, say between the Netherlands and the Czech Republic, as does the BIT, the two regulations do not cover the same precise subject-matter.
>
> 161. The European Union guarantees the free movement of capital. Thus, it guarantees to non-Czech investors from other EU member countries the right to invest in the Czech Republic on a par with any Czech investor.
>
> 162. The precedents cited by the Czech Republic concern impediments to the free movement of capital such as cases where one EU Member country – France – retained a "golden share" which allows the host state to assume, when it suits it, control over the company, thereby making it unattractive for investors from fellow EU Countries to invest in such companies in the host state.
>
> 163. Similarly, the European Union guarantees the free movement of capital outwards, thus, the investor may take out profits and even the investment as such out of the host country.
>
> 164. By contrast, the BIT provides for fair and equitable treatment of the investor during the investor's investment in the host country, prohibits expropriation, and guarantees full protection and security and the like. The BIT also provides for a special procedural protection in the form of arbitration between the investor state and the host state and, especially arbitration of a "mixed" or "diagonal" type between the investor and the host state, as in the present case.
>
> 165. From the point of view of the promotion and protection of investments, the arbitration clause is in practice the most essential provision of Bilateral Investment Treaties. Whereas general principles such as fair and equitable treatment or full security and protection of the investment are found in many international, regional or national legal systems, the investor's right arising from the BIT's dispute settlement clause to address an international arbitral tribunal independent from the host state is the best guarantee that the investment will be protected against potential undue infringements by the host state. EU law does not provide such a guarantee. [Emphasis added and omitted]

553. In addition, the tribunal rejected the Czech Republic's argument, similar to the position advocated by Estonia, that the BIT discriminates as between the citizens of different EU Member States. According to the tribunal, that some nationals of the EU could benefit from some protections unavailable to others does not render the BIT incompatible with EU law:

> If the EU Treaty gives more rights than does the BIT, then all EU parties, including the Netherlands and Dutch investors, may claim

> those rights. If the BIT gives rights to the Netherlands and to Dutch investors that it does not give other EU countries and investors, it will be for those other countries and investors to claim their equal rights. But the fact that these rights are unequal does not make them incompatible.[524] [Emphasis omitted]

554. The tribunal in *Oostergetel v Slovakia* reached a similar conclusion.[525] The tribunal first recalled that to be considered as relating to the "same subject matter," two (2) treaties must bear the same overall objective and "share a degree of general compatibility."[526] With regards to the BIT at hand, it concluded that the treaty did not have the same subject-matter as the Treaty establishing the European Community (the "**EC Treaty**"), noting that the EC Treaty offers no investor-State dispute mechanism:

> As to the first condition, the Tribunal agrees with the argument advanced by the Claimants that the EC Treaty's objective to create a common market between all EU Member States is different from the objectives of a BIT, which provides for specific guarantees for the investor's investment in the host country pursuant to a bilateral agreement made between two countries (Tr. J., pp. 16-17). The EC Treaty provisions on the fundamental freedoms are aimed at all types of cross-border economic activity. The BIT, on the other hand, is mostly concerned with providing a set of guarantees for protection of a long-term investment in the host state.
>
> Furthermore, it is at least questionable whether the substantive protection afforded to the foreign investor under the BIT is indeed comparable to the safeguards found under the EC Treaty. In other words, irrespective of a certain degree of overlap between the two regimes in terms of substantive provisions applicable to any potential investment disputes, this Tribunal is not convinced that the safeguards offered by the two are identical.
>
> Without going into further detail in determining the exact differences between the substantive safeguards provided to foreign investors under the two regimes, there is at least one fundamental distinction between the two, which renders them incomparable: the EC Treaty provides no equivalent to one of, if not the most important feature of the BIT regime, namely, the dispute settlement mechanism providing for investor-State arbitration.[527] [Emphasis omitted; Footnote omitted]

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[524] **RL-132**, *Eastern Sugar v The Czech Republic*, *ibid*, ¶170.

[525] **CL-103**, *Jan Oostergetel & Theodora Laurentius v The Slovak Republic*, UNCITRAL, Decision on Jurisdiction (30 April 2010) [*Oostergetel v Slovakia*].

[526] **CL-103**, *Oostergetel v Slovakia*, *ibid*, ¶79.

[527] **CL-103**, *Oostergetel v Slovakia*, *ibid*, ¶¶75-77.

555. Finally, the award on jurisdiction in *Electrabel v Hungary,*[528] which rejected the argument that the Energy Charter Treaty (the "**ECT**") is incompatible with EU law, also provides helpful assistance.

556. The *Electrabel* tribunal first found that EU law "has a multiple nature: on the one hand, it is an international legal regime; but on the other hand, once introduced in the national legal orders of EU Member States, it becomes also part of these national legal orders," and that in its international law dimension, "there is no fundamental difference in nature between international law and EU law."[529] It further dismissed the contention that Art. 234 TFEU excludes mixed dispute settlements arrangements, such as investor-State arbitration. A better view of EU law, the tribunal found, is that the TFEU forbids recourse to arbitration as between EU Members States.[530] According to the tribunal, no rule of EU law prevents, "expressly or impliedly," recourse to arbitration between a national of an EU Member State and another EU Member State; should EU Members State have intended otherwise, the absence of a clear provision to this effect would amount to "an extraordinary omission."[531] The tribunal thus summarised:

> 4.175. First, it is necessary to note again that the EU law is not incompatible with the provision for investor-state arbitration contained in Part V of the ECT, including international arbitration under the ICSID Convention. <u>The two legal orders can be applied together as regards the Parties' arbitration agreement and this arbitration, because only the ECT deals with investor-state arbitration; and nothing in EU law can be interpreted as precluding investor-state arbitration under the ECT and the ICSID Convention</u>.
>
> 4.176. <u>As regards the substantive protections in Part III of the ECT, the Tribunal does not consider that the ECT and EU law share the same subject-matter</u>; and, accordingly, it considers that Article 16 ECT is inapplicable.[532] [Emphasis added]

557. The tribunal also noted that an objection under Art. 351 TFEU, such as articulated by Estonia here, and an objection based on Art. 30(3) VCLT have the same consequences.[533]

558. The Tribunal cannot end without noting one particular aspect of the EU majority Declaration which in fact would seem to support the Tribunal's own conclusion. The Declaration states:

> Member States will make best efforts to deposit their instrument of ratification, approval or acceptance […] of any bilateral treaty

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[528] **CL-107**, *Electrabel* (Decision on Jurisdiction), *supra* note 452, ¶4.192.

[529] **CL-107**, *Electrabel* (Decision on Jurisdiction), *ibid*, ¶¶4.118 and 4.126.

[530] **CL-107**, *Electrabel* (Decision on Jurisdiction), *ibid*, ¶¶4.150 and 4.151.

[531] **CL-107**, *Electrabel* (Decision on Jurisdiction), *ibid*, ¶4.153.

[532] **CL-107**, *Electrabel* (Decision on Jurisdiction), *ibid*, ¶¶4.175 and 4.176.

[533] **CL-107**, *Electrabel* (Decision on Jurisdiction), *ibid*, ¶4.190.

> terminating bilateral investment treaties between Member States no later than 6 December 2019.[534]

559. This necessarily implies, in the Tribunal's view, that the BIT remains in force and that its Article 9 can therefore constitute a valid offer to arbitrate, which Claimants accepted.

560. The unavoidable consequence is that the Tribunal has jurisdiction to decide the case. The objection based on the incompatibility of the BIT with EU law is rejected.

VII. LIABILITY

561. Claimants' claims may be divided into three (3) categories:

   (i) A breach of the FET standard by Estonia consisting in the violation by Respondent of Claimants' legitimate expectations arising out of the privatisation of ASTV;

   (ii) Other breaches by Respondent of the FET standard and due process as well as the taking of discriminatory measures against Claimants;

   (iii) Breaches of the umbrella clause contained in the Treaty.

562. These alleged breaches of the Treaty are assessed below.

A) CLAIM OF BREACH OF FET BASED ON LEGITIMATE EXPECTATIONS

563. Claimants' first claim consists in the alleged breach by Estonia of the FET standard, primarily through the violation of Claimants' legitimate expectations related to the privatisation of ASTV.[535] Claimants divide the analysis of this claim into two (2) distinct periods: (1) their expectations at the time of the privatisation (*i.e.* in 2001) and (2) their expectations as of 2009 (*i.e.* at the beginning of the process by which Respondent allegedly breached these expectations).

564. Regarding the first period, Claimants explain in their post-hearing submissions that:

> [their] key legitimate expectation at the time of the privatisation was that, if UUTBV made the investments agreed in the privatisation and through its management of ASTV achieved the ambitious quality and service level improvements required by the privatisation, the contracts entered into as a result of the privatisation would be respected, with tariffs set by reference to the tariff methodology in the Services Agreement for its full 15 year term.[536]

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[534] **RL-276**, EU Majority Declaration, *supra* note 508, ¶8.

[535] In their post-hearing submissions (¶3), Claimants assert that "not only has Estonia acted in breach of the Claimants' legitimate expectations, the way in it has done so – and its treatment of UUTBV and ASTV since 2009 – has not been fair and equitable." It is unclear what precisely this means. In any event, the Tribunal does not understand that Claimants intend to introduce a new or different claim from those previously asserted.

[536] Cl. PHB, ¶18.

565. They identify four constituent elements of this expectation, as follows:

> a. that the contracts entered into by the City of Tallinn with the Government's knowledge on 12 January 2001, in reliance on which UUTBV invested €85 million in ASTV, would be respected;
>
> b. in the five-year Initial Period, that ASTV's tariffs would be set by reference to the specific K factors bid by UUTBV and incorporated into the Services Agreement;
>
> c. that in setting the K factors for subsequent Operating Periods any consideration of justified profitability would be by reference to the tariff methodology in the Services Agreement and the Business Plan submitted at the time of UUTBV's bid, not on the basis of a clean slate which took no account of the Services Agreement, the privatisation, or the €85 million investment UUTBV made on the basis of them; and
>
> d. the key principles of the regulatory framework applicable to ASTV, as set out in the Services Agreement, would not be radically overturned during its term. In spite of the absence of an express stabilisation clause in the Services Agreement, the Claimants could legitimately expect that the fundamental basis of the tariff methodology envisaged in the Services Agreement would be maintained and would not be unreasonably and arbitrarily undone during the term of that agreement. This is so regardless of the existence of certain provisions in the Services Agreement relating to future regulatory change.[537] [Footnotes omitted]

566. Claimants have confirmed that these expectations do not turn on a pre-defined level of profitability[538] but relate instead to the overall framework governing the parties' conduct as set out in the privatisation agreements. This framework, they say, gives rise to legitimate expectations as recognized in international investment law in the light of the overall context, purpose and circumstances of the privatisation. Claimants nonetheless acknowledge that they do not benefit from a stabilisation clause or any other explicit assurance as to the stability of the legal and regulatory framework governing their investment. To the contrary, they recognise that the privatisation agreements clearly anticipated certain regulatory changes.[539]

567. According to Claimants, and as indicated above, Respondent breached their legitimate expectations by its conduct primarily in relation to the rejection of ASTV's 2011 Tariff Application and the adoption of the Prescription.

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[537] Cl. PHB, ¶97.

[538] Claimants have confirmed that they were not entitled to a guaranteed return or any guaranteed tariffs, Cl. PHB, ¶¶117-121.

[539] See for instance Cl. PHB, ¶19, where Claimants recognise that the Services Agreement anticipated some regulatory changes, and ¶¶49-51, where Claimants argue that the lack of a stabilisation agreement does not undermine their claim.

568. Respondent challenges the notion that Claimants could have formed any expectation protected under international law in the circumstances. According to Estonia, Claimants fail to demonstrate any specific assurances by the host State, most notably because it was not reasonable for them to expect that ASTV's tariffs would be insulated from the law, its changes and its enforcement, and because, in any event, the privatisation agreements did not provide for an expected range of profitability.[540]

569. The Tribunal will first review the relevant authorities pertaining to the protection of legitimate expectations in international investment law (1). It will next assess whether Claimants have demonstrated, on the facts, that they formed any legitimate expectations at the time of the privatisation (2) and then will assess the impact, if any, of events after the privatisation (3). The Tribunal will then determine whether Respondent's conduct breached Claimants' legitimate expectations, in violation of the BIT and customary international law (4).

1) A General Approach to FET

570. Any claim related to the FET standard, including a claim for breach of legitimate expectations, must find its source in Art. 3(1) of the Treaty:

> Each Contracting Party shall ensure fair and equitable treatment of the investments of nationals of the other Contracting Party and shall not impair, by unreasonable or discriminatory measures, the operation, management, maintenance, use, enjoyment or disposal thereof by those nationals. [Emphasis added]

571. The parties to the Treaty specified in its preamble that the FET standard "is desirable" but refrained from defining it. Guidance may however be obtained from the many tribunals which have elaborated upon the nature and the breadth of the FET standard.

572. The need to distinguish between the FET standard and other more specific international wrongs is clearly acknowledged by the case law. For instance in *PSGE v Turkey* it was held that:

> Because the role of fair and equitable treatment changes from case to case, it is sometimes not as precise as would be desirable. Yet**,** it clearly does allow for justice to be done in the absence of the more traditional breaches of international law standards. This role has resulted in the concept of fair and equitable treatment acquiring a standing on its own, separate and distinct from that of other standards, albeit many times closely related to them, and thus ensuring that the protection granted to the investment is fully safeguarded.[541] [Emphasis added]

573. An often-relied general statement of the content of FET is the one made by the Tribunal in *Waste Management*:

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[540] Resp. PHB, ¶¶303-322; Resp. C-M, ¶¶126-130; Resp. Rej., ¶¶115-120 and 389-391.

[541] *PSEG Global, Inc., The North American Coal Corporation, and Konya Ingin Electrik Üretim ve Ticaret Limited Sirketi v Republic of Turkey*, ICSID Case No. ARB/02/5, Award (19 January 2007), ¶239.

> [T]he minimum standard of treatment of fair and equitable treatment is infringed by conduct attributable to the State and harmful to the claimant if the conduct is arbitrary, grossly unfair, unjust or idiosyncratic, is discriminatory and exposes the claimant to sectional or racial prejudice, or involves a lack of due process leading to an outcome which offends judicial propriety—as might be the case with a manifest failure of natural justice in judicial proceedings or a complete lack of transparency and candour in an administrative process. In applying this standard it is relevant that the treatment is in breach of representations made by the host State which were reasonably relied on by the claimant.[542] [Emphasis omitted]

574. This is not to stay, however, that the protection afforded to investors under this standard finds its source in investors' expectations. The protection derives from the terms of the applicable treaty; the expectations of an investor do not constitute a standalone source of obligations for the host State.[543] Although the investor's expectations will be at the heart of the analysis, they are not to be assessed on a purely subjective basis, nor without due consideration of the State's sovereign right to regulate:

> [L]egitimate expectations cannot be solely the subjective expectations of the investor, but have to correspond to the objective expectations than [sic] can be deduced from the circumstances and with due regard to the rights of the State. In other words, a balance should be established between the legitimate expectation of the foreign investor to make a fair return on its investment and the right of the host State to regulate its economy in the public interest.[544]

575. Absent an express commitment to that effect by the host State, it is not reasonable for an investor to expect that its investment will enjoy a static legislative and regulatory regime; foreign investors must anticipate changes and adapt accordingly:

> 332. It is each State's undeniable right and privilege to exercise its sovereign legislative power. A State has the right to enact, modify or cancel a law at its own discretion. Save for the existence of an agreement, in the form of a stabilisation clause or otherwise, there is nothing objectionable about the amendment brought to the regulatory framework existing at the time an investor made its investment. As a matter of fact, any businessman or investor knows that laws will evolve

[542] **CL-115**, *Waste Management, Inc. v United Mexican States* ("Number 2"), ICSID Case No. ARB(AF)/00/3, Award (30 April 2004) [*Waste Management v Mexico*], ¶98.

[543] It is noted that the tribunal in MTD v Chile found similarly. See *MTD Equity Sdn. Bhd. and MTD Chile S.A. v Chile*, ICSID Case No. ARB/01/7, Decision on Annulment (21 March 2007), ¶¶67-71.

[544] **RL-145**, *El Paso Energy International Company v Argentine Republic*, ICSID Case No. ARB/03/15, Award (31 October 2011), ¶358 [*El Paso v Argentina*]. Similarly, a tribunal may conclude to a breach of the FET even if there is no evidence of the State's subjective bad faith (¶357). See also *Electrabel*, where the tribunal explained: "Consequently, the requirement of fairness must not be understood as the immutability of the legal framework, but as implying that subsequent changes should be made fairly, consistently and predictably, taking into account the circumstances of the investment," **RL-124**, *Electrabel SA. v Republic of Hungary*, ICSID Case No. ARB/07/19, Award (30 November 2012), ¶7.77 [*Electrabel* (Award)].

over time. What is prohibited however is for a State to act unfairly, unreasonably or inequitably in the exercise of its legislative power.

333. In principle, an investor has a right to a certain stability and predictability of the legal environment of the investment. The investor will have a right of protection of its legitimate expectations provided it exercised due diligence and that its legitimate expectations were reasonable in light of the circumstances. Consequently, an investor must anticipate that the circumstances could change, and thus structure its investment in order to adapt it to the potential changes of legal environment.[545] [Emphasis added and omitted]

576. The Tribunal nonetheless recognises, as noted in *Parkerings*, inter alia, that legitimate expectations do not arise solely from explicit promises by the State. The State may also have made implicit assurances or representations reasonably relied on by the investor, and the circumstances surrounding the conclusion of an investment may be decisive to determine if the expectation of the investor was legitimate.[546] Yet, these statements cannot be applied so broadly as to relieve foreign investors from their burden of both articulating precise expectations and establishing that they are objectively reasonable.[547]

577. Indeed, the precise delineation of an investor's expectations and their origin(s) in the circumstances of a given case is essential to any claim. As stated by the tribunal in *El Paso v Argentina*:

375. A reasonable general regulation can be considered a violation of the FET standard if it violates a specific commitment towards the investor. The Tribunal considers that a special commitment by the State towards an investor provides the latter with a certain protection

[545] **RL-157**, *Parkerings-Compagniet AS v Republic of Lithuania*, ICSID Case No. ARB/05/8, Award (11 September 2007) [*Parkerings*], ¶¶331-333. See also **RL-155**, *EDF (Services) Limited v Romania*, ICSID Case No. ARB/05/13, Award (8 October 2009), ¶¶217 and 218. See also **RL-144**, *Saluka Investments B.V. v The Czech Republic*, UNCITRAL, Partial Award (17 March 2006), ¶¶305-307 [*Saluka v Czech Republic*]: "No investor may reasonably expect that the circumstances prevailing at the time the investment is made remain totally unchanged. In order to determine whether frustration of the foreign investor's expectations was justified and reasonable, the host State's legitimate right subsequently to regulate domestic matters in the public interest must be taken into consideration as well."

[546] **RL-157**, *Parkerings*, *ibid*, ¶331: "The expectation is legitimate if the investor received an explicit promise or guaranty from the host-State, or if implicitly, the host-State made assurances or representation that the investor took into account in making the investment. Finally, in the situation where the host-State made no assurance or representation, the circumstances surrounding the conclusion of the agreement are decisive to determine if the expectation of the investor was legitimate. In order to determine the legitimate expectation of an investor, it is also necessary to analyse the conduct of the State at the time of the investment." [Footnotes omitted]. In the same vein, the tribunal in *Electrabel* noted that specific assurances may not be indispensable to prove a breach of legitimate expectations, although such assurances have undoubtedly great bearing, **RL-124**, *Electrabel* (Award), *supra* note 544, ¶7.78: "While specific assurances given by the host State may reinforce the investor's expectations, such an assurance is not always indispensable […] Specific assurances will simply make a difference in the assessment of the investor's knowledge and of the reasonability and legitimacy of its expectations."

[547] See **RL-124**, *Electrabel* (Award), *supra* note 544, ¶155: "Even in the absence of a specific representation, however, the investor must establish a relevant expectation based upon reasonable grounds, which Electrabel has failed to do so."

> against changes in the legislation, but it needs to discuss more thoroughly the concept of "specific commitments." In the Tribunal's view, no general definition of what constitutes a specific commitment can be given, as all depends on the circumstances. However, it seems that two types of commitments might be considered "specific": those specific as to their addressee and those specific regarding their object and purpose.
>
> 376. First, in order to prevent a change in regulations being applied to an investor or certain behaviour of the State, there can indeed exist specific commitments directly made to the investor – for example in a contract or in a letter of intent, or even through a specific promise in a person-to-person business meeting – and not simply general statements in treaties or legislation which, because of their nature of general regulations, can evolve. The important aspect of the commitment is not so much that it is legally binding – which usually gives rise to some sort of responsibility if it is violated without a need to refer to FET – but that it contains a specific commitment directly made to the investor, on which the latter has relied.
>
> 377. Second, a commitment can be considered specific if its precise object was to give a real guarantee of stability to the investor. Usually general texts cannot contain such commitments, as there is no guarantee that they will not be modified in due course. However, a reiteration of the same type of commitment in different types of general statements could, considering the circumstances, amount to a specific behaviour of the State, the object and purpose of which is to give the investor a guarantee on which it can justifiably rely.[548] [Emphasis added and omitted]

578. As a result, should an investor fail to demonstrate sufficient specificity with respect to the commitment on which it relies, the FET standard would subject States to the impossible task of meeting constantly moving targets.[549]

579. The assessment of alleged legitimate expectations thus requires balancing these expectations against the State's legitimate regulatory interest.[550] As put by the tribunal in *El Paso v Argentina*:

> […] FET is linked to the objective reasonable legitimate expectations of the investors and that these have to be evaluated considering all circumstances. As a consequence, the legitimate expectations of a foreign investor can only be examined by having due regard to the general proposition that the State should not unreasonably modify the

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[548] **RL-145**, *El Paso v Argentina*, *supra* note 544, ¶¶375-377.

[549] It is noted that the tribunal in *Arif v Moldova* arrived at a similar conclusion. See *Franck Charles Arif v Republic of Modolva*, ICSID Case No. ARB/11/23, Award (8 April 2013), ¶¶534 and 535 [*Arif v Moldova*].

[550] **CL-111**, *Perenco Ecuador Limited v Republic of Ecuador*, ICSID Case No. ARB/08/6, Decision on the Remaining Issues of Jurisdiction and on Liability (12 September 2014), ¶560 [*Perenco v Ecuador*].

> legal framework or modify it in contradiction with a specific commitment not to do so […].[551] [Emphasis omitted]

580. Furthermore, in assessing objectively ASTV's and UUTBV's alleged expectations, the Tribunal must have due regard not only to the context of the investment but also to the relevant socio-economic and historical background.[552]

2) The Distinction between Contractual Commitments and Legitimate Expectations

581. In addition to the factors noted above, the present case requires a consideration of the relationship between purely contractual rights that do not on their own entail a guarantee of stability of the regulatory regime, and the formation of legitimate expectations.[553]

582. Although Respondent does not expressly deny that contractual rights may inform the analysis of a FET claim, the parties diverge as to how and when contractual entitlements (alone or coupled with other factual elements) give rise to legitimate expectations.

583. Claimants argue that legitimate expectations may rest on a contractual relationship, and that contractual arrangements may inform the analysis of a FET claim.[554] They further posit that neither an express stabilisation clause nor an explicit undertaking of legal stability by the State is essential to obtain redress.[555] Claimants draw a distinction between "pure" contractual breaches, which would not attract international liability, and cases where the existence and breach of an investor's legitimate expectations arise from a broader factual matrix, such as the case at hand. According to them, only a sovereign acting *qua* sovereign, and not as a commercial party, could have performed the actions (including the amendment of PWSSA's provisions on justified profitability, the change of regulator and the decisions adopted by the new regulator) which comprise the basis of Claimants' treaty claims, thereby removing this case from any purely commercial setting.[556]

584. Respondent takes the position that contractual rights *per se* cannot give rise to legitimate expectations; should this be otherwise, umbrella clauses would be redundant.[557] Absent a stabilisation clause, Respondent submits that an investor must identify a precise and clear representation by the State, in the form of statements or conduct, concerning the stability of

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[551] **RL-145**, *El Paso v Argentina*, *supra* note 544, ¶364.

[552] **RL-159**, *Duke Energy Electroquil Partners and Electroquil S.A. v Republic of Ecuador*, ICSID Case No. ARB/04/19, Award (18 August 2008), ¶340 [*Duke Energy v Ecuador*].

[553] The Tribunal requested that the Parties address this issue in their respective post-hearing submissions, letter of the Tribunal to the Parties of 24 January 2017, question No. 2.

[554] Cl. PHB, ¶¶139-151.

[555] Cl. Reply, ¶¶164-191.

[556] Cl. PHB, ¶¶145-148; 151.

[557] Resp. PHB, ¶321.

the regulatory system. "Implicit assurances," unless sufficiently specific, cannot ground a FET claim.[558]

585. The *Parkerings v Lithuania* tribunal made a clear distinction between contractual obligations and expectations and legitimate expectations under international law:

> It is evident that not every hope amounts to an expectation under international law. The expectation a party to an agreement may have of the regular fulfilment of the obligation by the other party is not necessarily an expectation protected by international law. In other words, <u>contracts involve intrinsic expectations from each party that do not amount to expectations as understood in international law</u>. Indeed, the party whose contractual expectations are frustrated should, under specific conditions, seek redress before a national tribunal.[559] [Emphasis added and omitted]

586. The same position was adopted in *Hamester*:

> It is important to emphasise that the existence of legitimate expectations and the existence of contractual rights are two separate issues. This has been highlighted by the *Parkerings v. Lithuania* tribunal […]
>
> Christoph Schreuer also explains that contractual rights are not to be equated with legitimate expectations:
>
> "Taken to its logical conclusion this argument would put all agreements between the investor and the host State under the protection of the FET standard. If this position were to be accepted, the FET standard would be nothing less than a broadly interpreted umbrella clause."
>
> The Tribunal fully endorses this comment, and concludes that it is not sufficient for a claimant to invoke contractual rights that have allegedly been infringed to sustain a claim for a violation of the FET standard.[560]
> [Emphasis added; Footnotes omitted]

587. In other words, the Tribunal agrees with Respondent that, should "every contractual right amounted to a legitimate expectation protected under international law, umbrella clauses would be completely redundant."[561]

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[558] Resp. Rej., ¶¶418-428.

[559] **RL-157**, *Parkerings*, *supra* note 545, ¶344.

[560] **RL-163**, *Gustav F W Hamester GmbH & Co KG v. Republic of Ghana*, ICSID Case No. ARB/07/24, Award, (18 June 2010), ¶¶ 335-337.

[561] Resp. PHB, ¶321.

3) A Necessary Balance between the Investor's Expectations and the State's Right to Regulate

588. In the Tribunal's opinion, contractual undertakings may indeed inform the existence of legitimate expectations, depending on the circumstances, including most notably the assurances contained in the contract, the other terms of the relevant agreement and the context in which the contract is executed. This said, absent other circumstances, the mere expectation that a contractual commitment will be respected and performed cannot suffice to establish a breach of the FET standard. The Tribunal agrees with Respondent that, should this be otherwise, "umbrella clauses would be redundant." As the tribunal in *Toto v Lebanon* acknowledged, contractual commitments may in appropriate circumstances give rise to legitimate expectations and entitle an investor to presume that the "overall legal framework will remain stable." Yet, for that to be the case, some manner of conduct by the State is required;[562] and, where a FET claim is grounded on contractual rights, a higher threshold must be met.[563]

589. The Tribunal notes the appeal of contrasting the conduct of a so-called "regular contractual partner" from conduct that could not have been committed in a purely contractual relationship (such as Claimants endeavour to do when they insist that Respondent's acts were that of a sovereign, not a commercial party).[564] However, as aptly noted by Schreuer, seemingly simple tests rarely offer conclusive responses: "the distinction between sovereign and commercial acts, which is accepted in the field of state immunity, is of unclear validity in the area of state responsibility. Also, even if the underlying relationship and the breach are clearly commercial, the motives of a government for a certain act may still be governmental."[565]

590. In the Tribunal's view, the typology of FET cases developed by the authors McLachlan, Shore and Weiniger provides an arguably useful (though in no way determinative) description of how tribunals seek to balance investors' desire for stability and States' right to amend their laws and regulations:

> In striking a balance between stability and flexibility in the regulatory regime, tribunals have typically required the presence of one of the following three elements in finding a breach of the treaty standard:
>
> (a) A specific assurance or promise of a competent organ attributable to the State upon which the investor reasonably relied in deciding to invest;
>
> (b) Regulations that are substantively arbitrary or discriminatory in their application to foreign investors; or

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[562] **CL-106**, *Toto Costruzioni Generali S.p.A. v Lebanon*, ICSID Case No. ARB/07/12, Award (7 June 2012), ¶¶159 and 161 [*Toto v Lebanon*]

[563] **CL-106**, *Toto v Lebanon*, *ibid*, ¶163

[564] See for instance the statements of the tribunal in *Consortium RFCC v Kingdom of Morocco*, ICSID Case No. ARB/00/6, Award (22 December 2009), ¶51 (**CL-122**).

[565] **CL-100**, Schreuer, *The ICSID Convention*, *supra* note 332, p 154.

(c) A total alteration of the entire regulatory framework for foreign investments in the particular field that has the effect of virtually eliminating the benefits that the investor reasonably anticipated upon making the investment.[566] [Emphasis added]

591. The second category of cases referred to above would seem to capture Claimants' allegations of violation of the FET standard pertaining to discrimination and violation of due process, addressed below at paragraphs 867 and following.

592. As to the first scenario, and as stated above at paragraph 566, Claimants recognise, at least implicitly, that they do not benefit from any explicit promise as to the stability of the regulatory regime. Rather, as appears from the excerpt above at paragraph 565, their legitimate expectation case revolves around the enforcement of the privatisation contracts or, at minimum, on the application of the key principles of the regulatory framework which they say were contemplated in those agreements. They describe their expectations in this regard as being that "the key principles of the regulatory framework applicable to ASTV, as set out in the Services Agreement, would not be radically overturned during its term."[567] Therefore, in the Tribunal's opinion, if made out, Claimants' FET case most likely falls within the third category of cases identified by McLachlan *et al*.

593. In this respect, the authors explain that "tribunals have found a breach of the standard on the ground that the cumulative effect of the State's regulatory changes has been to alter completely the regulatory framework in a manner that virtually eliminates the investor's reasonably expected benefits."[568] Indeed, in the three (3) cases they study, which were all commented on by the Parties here, the tribunals did not treat specific commitments by an organ of the State as a *sine qua non*. These tribunals rather emphasised the investor's reliance on the regulatory regime in place at the time of the investment, and focused on the total structural changes to the original regime and the extreme economic consequences of such changes on the investor.

594. First, in *El Paso v Argentina*, the tribunal expressed the view that a State may be found to have infringed the FET standard where it totally alters the legal framework applicable to an investment, and this, even in the absence of a stability clause or a similar specific commitment:

> In other words, fair and equitable treatment is a standard entailing reasonableness and proportionality. It ensures basically that the foreign investor is not unjustly treated, with due regard to all surrounding circumstances. FET is a means to guarantee justice to foreign investors.

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[566] Campbell McLachlan, Laurence Shore and Matthew Weiniger, *International Investment Arbitration – Substantive Principles*, 2nd ed (Oxford: Oxford University Press, 2017), ¶7.165 [McLachlan, Shore and Weiniger].

[567] Cl. PHB, ¶97d.

[568] McLachlan, Shore and Weiniger, *supra* note 566, ¶7.168.

> There can be no legitimate expectation for anyone that the legal framework will remain unchanged in the face of an extremely severe economic crisis. No reasonable investor can have such an expectation unless very specific commitments have been made towards it or unless the alteration of the legal framework is total.[569] [Footnote omitted]

595. It determined on this basis that the cumulative effect of the measures adopted by Argentina in the wake of the 2001 economic crisis amounted to a total alteration of the legal environment originally established to attract foreign investors. The tribunal then took into consideration the various means by which Argentina had represented to foreign investors that a devaluation of the Argentinian Peso would *not* affect their investments.[570]

596. Second, in *Micula v Romania*, the investors demonstrated that they had been induced to invest in a particular region of Romania by means of a programme of tax incentives, and that Romania had later completely stripped the programme of those incentives. The record also showed that Romanian officials had represented to the claimants that they would be compensated should the regime be repealed or fundamentally altered over a 10-year period.[571]

597. The tribunal reasoned that the intent of the State to commit itself, or not, bears little relevance to determining whether the investor holds legitimate expectations. Rather, the analysis turns on a factual assessment as to whether the State acted in such a way as to create such expectations.[572] It concluded, on the facts at hand, that Romania had violated the FET standard, given that the investor had relied on the State's assurance of support and that a *quid*

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[569] **RL-145**, *El Paso v Argentina*, *supra* note 544, ¶¶373-374. Resp. C-M, ¶¶401 and 402 and Resp. Rej., ¶355.

[570] **RL-145**, *El Paso v Argentina*, *ibid*, ¶517 [footnotes omitted]: "It cannot be denied that in the matter before this Tribunal the cumulative effect of the measures was a total alteration of the entire legal setup for foreign investments, and that all the different elements and guarantees just mentioned can be analysed as a special commitment of Argentina that such a total alteration would not take place. As stated by the tribunal in LG&E, when evaluating the same events, 'here, the Tribunal is of the opinion that Argentina went too far by completely dismantling the very legal framework constructed to attract investors.'"

[571] **CL-109**, *Ioan Micula, Viorel Micula and others v Romania,* ICSID Case No. ARB/05/20, Award (11 December 2013), ¶¶686-689 [*Micula v Romania*]. Claimants relies on this decision to support their position that implicit assurances may form legitimate expectations, Cl. Reply, ¶167, referring to paragraph 669 of the award.

[572] **CL-109**, *Micula v Romania*, *ibid*, ¶669. As regards a specific assurance of regulatory stability, the tribunal explained: "However, the fair and equitable treatment obligation is not an unqualified guarantee that regulations will never change. Investors must expect that the legislation will change from time to time, absent a stabilization clause or other specific assurances giving rise to a legitimate expectation of stabilization. The BIT's protection of the stability of the legal and business environment cannot be interpreted as the equivalent of a stabilization clause. In the Tribunal's view, the correct position is that the state may always change its legislation, being aware and thus taking into consideration that: (i) an investor's legitimate expectations must be protected; (ii) the state's conduct must be substantively proper (e.g., not arbitrary or discriminatory); and (iii) the state's conduct must be procedurally proper (e.g., in compliance with due process and fair administration). If a change in legislation fails to meet these requirements, while the legislation may be validly amended as a matter of domestic law, the state may incur international liability." (¶529).

pro quo had been required from the investor. In the tribunal's words, Romania "did not merely 'trim down' the incentives, as the Respondent contends […] [it] virtually eliminated rather than simply modified or amended" the relevant regime.[573] This sufficed to engage Romania's liability: "it cannot be fair and equitable for a State to offer advantages to investors with the purpose of attracting investment in an otherwise unattractive region, require these investors to maintain their investments in that region for twice the period they receive the incentives, and then maintain the formal shell of the regime but eviscerate it of all (or substantially all) content."[574]

598. Third, the tribunal in *Perenco v Ecuador*, a case that Claimants analogise with their own case here,[575] emphasised that the terms of a contract entered into by the State bear particular significance,[576] even where the contractual arrangement does not contain a stabilization clause.[577]

599. In *Perenco*, a State entity had entered into production sharing contracts with several foreign investors, including the claimant, for the exploration and exploitation of two (2) oil blocks. The tribunal noted that these contracts had been executed under a specific and duly considered legislative framework and that this framework had also been integrated in the agreements. In the tribunal's view, it was therefore reasonable for the investors to expect that the contracts would not be altered unilaterally by State action, except in accordance with the terms of the contracts and the State's law:[578]

> The Participation Contracts were anchored in a legislative framework duly considered and enacted by the Nation's Congress. That framework and its rationale set out certain key features of the new contractual regime which were then reflected in the contracts subsequently concluded with oil companies. Consequently, any contractor could reasonably expect that the contracts' structure would not be altered by Petroecuador unilaterally or undone by subsequent State action external to the contract except in accordance with their terms and the State's law. [Footnotes omitted]

600. The tribunal declined to find that the increase of the State's taxation of the revenues of the oil concessions in question to 50% breached the FET standard (given, *inter alia*, that such an increase was not proven to fundamentally alter the structure of the contracts and that there was no evidence that "it blunted further investment").[579] By contrast, the tribunal found that

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[573] **CL-109**, *Micula v Romania*, *ibid*, ¶682.

[574] **CL-109**, *Micula v Romania*, *ibid*, ¶687.

[575] Cl. Reply, ¶¶182-184; Cl. PHB, ¶¶142, 150, 152; Tr. Day 1, Claimants' Opening Statement, 10:17-12:17.

[576] **CL-111**, *Perenco v Ecuador*, *supra* note 550, ¶561.

[577] **CL-111**, *Perenco v Ecuador*, *ibid*, ¶562.

[578] **CL-111**, *Perenco v Ecuador*, *ibid*, ¶563.

[579] **CL-111**, *Perenco v Ecuador*, *ibid*, ¶¶599-602.

subsequent tax increase to 99%, coupled with other State measures, completely overturned the existing system and therefore violated the FET standard.[580]

601. The Tribunal considers it appropriate to refer to two (2) other cases relied on by Claimants, *Walter Bau v Thailand* and *TECO v Guatemala*, both of which would also fall in the third category of the aforementioned typology.

602. The UNCITRAL tribunal in *Walter Bau v Thailand* found the respondent State liable toward the investor based on an assessment of what it referred to as the "total factual matrix," rather than on any finding of an explicit statement or specific conduct by Thailand.[581] The latter had refused to approve toll hikes contemplated in a concession contract for the building of a toll road. This was, according to the tribunal, in contradiction with the common understanding of the parties that the claimant would earn a "reasonable rate of return" on its investment. The tribunal factored into its assessment: (i) the semi-public nature of the concession, (ii) the "inherent unlikeliness that any investor would contemplate entering into such a long-term arrangement without a legitimate expectation of reasonable return," (iii) tolls were the only mean to recoup the investment made and (iv) "there had been extensive consideration of the economic viability of the concession by many parties."[582] On this latter element, the Tribunal notes in its analysis of legitimate expectations that the parties to the agreement had addressed the issue of the return to be earned by the investor. More specifically, the parties to the agreement had conducted studies to ascertain what would constitute a reasonable rate of return and that they had entered into this contract with the belief that this return would vary between 15 and 21%. In the course of the negotiation of an amendment to the contract, the minister of Finance had even explicitly mentioned that the various alternatives envisioned would allow the concessionaire to "achieve a reasonable rate on his investment (14%)."[583] As discussed below at paragraphs 686 and following, however the circumstances of the present case differ significantly from those in *Walter Bau v Thailand*.

603. In *TECO v Guatemala*, the claimant alleged, as do Claimants in the present matter, that it benefited from assurances regarding the methodology for establishing utility tariffs.

604. TECO had acquired a formerly state-owned electricity company, EEGSA. Prior to the privatisation, Guatemala had adopted a new tariff regime through the General Electric Law. This legislation provided that tariffs were to be based on the VAD factor, designed to represent the average cost of capital of an efficient company asset base. The VAD factor was to be determined based on a consultant study submitted by the distributor of electricity and to be reviewed by the regulator, the CNEE, according to parameters adopted in State resolutions. The regulatory scheme also provided for the appointment of an Expert Commission should disagreement between the distributor and the regulator arise. Eleven years later, a dispute arose after CNEE employed a methodology requiring that the CNEE (and not the distributor)

[580] **CL-111**, *Perenco v Ecuador*, *ibid*, ¶627.

[581] **CL-120**, *Walter Bau v Thailand*, UNCITRAL, Award (1 July 2009) [*Walter Bau v Thailand*].

[582] **CL-120**, *Walter Bau v Thailand*, *ibid*, ¶¶12.3 and 12.4.

[583] **CL-120**, *Walter Bau v Thailand*, *ibid*, ¶¶12.3d)-f).

undertake the VAD factor study which resulted in lower tariffs. This new methodology required that the VAD factor study be undertaken by the CNEE, as opposed to the distributor.

605. In support of its FET claim, TECO relied on certain statements made by Guatemala in preparation for the privatisation as well as on the Memorandum of Sale prepared at the time by EEGSA's consultant:

> 614. Page 19 of the presentation states that "any material change in tariff methodology must be supported by a study conducted by an internationally recognized independent consultant." As for the Memorandum of Sale, it is more specific and states, in the relevant parts relating to the regulatory framework, that "VADs must be calculated by distributors by means of a study commissioned from an engineering firm, but the Commission may dictate that the studies be grouped by density. The Commission will review those studies and can make observations, but in the event of discrepancy, a Commission of three experts will be convened to resolve the differences."
>
> 615. Attached to the Memorandum of Sale was an English-language draft of the future law of electricity, providing in Article 75 that "the Commission [CNEE] shall review the studies performed and may make comments on the same. In case of differences made in writing, the Commission and the distributors shall agree on the appointment of an Expert Commission made of three members, one appointed by each party and the third by mutual agreement. The Expert Commission shall rule on the differences in a period of 60 days counted from its appointment."[584] [Emphasis omitted; Footnotes omitted]

The tribunal found that these were not specific assurances regarding the stability of the regime[585] and that, in any event, the amendments to the law did not alter the fundamental principles of the regulatory regime.[586] The tribunal also determined that the change in the methodology, *i.e.* that tariffs would be set according to the regulator's own study rather than the distributor's, was neither unfair, nor arbitrary.[587] It suggested however that, in the absence of a stabilisation clause, regulatory changes *may* breach the FET standard where such changes are either made in bad faith or with the intent of depriving the investor of the benefit of its investment.[588] The matter rather turned on whether Guatemala had applied domestic law in a

[584] **CL-110**, *TECO Guatemala Holdings LLC v The Republic of Guatemala*, ICSID Case No. ARB/10/17, Award (19 December 2013), ¶¶614 and 615 [*TECO v Guatemala*].

[585] **CL-110**, *TECO v Guatemala*, *ibid*, ¶618.

[586] **CL-110**, *TECO v Guatemala*, *ibid*, ¶619. According to the tribunal, the matter rather turned on whether Guatemala had applied domestic law in a fair and non-arbitrary manner, see ¶¶621 and 622.

[587] **CL-110**, *TECO v Guatemala*, *ibid*, ¶630.

[588] **CL-110**, *TECO v Guatemala*, *ibid*, ¶629: "At any rate, this argument is ill-grounded. As rightly pointed out by the Respondent, Guatemala never agreed or represented that the regulatory framework would remain unchanged. In absence of a stabilisation clause, it is perfectly acceptable that the State amends the relevant laws and regulations as appropriate. It is only if a change to the regulatory framework is made in bad faith or with the intent to deprive the investor of the benefits of its investment that it could entail the State's international responsibility."

fair and non-arbitrary manner.[589] In this respect, the Tribunal ultimately found that, although it was entitled to relied on its own study, it had violated due process by (i) not providing reasons for not using the distributor's study and (ii) that it did not abide to the principle that disagreement between the distributor and the regulator would be resolved having regarded to the conclusions of a neutral Expert Commission.[590]

4) The Claimants' Legitimate Expectations at the Time of the Privatisation

606. The Tribunal consider it appropriate to recall that the legitimate expectations of an investor are to be determined at the time the investment is made. This has been stated by several tribunals, for example in *Electrabel*, both in the Decision on Jurisdiction, Applicable Law and Liability and the Award:

> As regards the relevant point in time for the assessment of legitimate and reasonable expectations, it is common ground in "investment jurisprudence" and between the Parties that <u>the assessment must refer to the time at which the investment is made</u> […][591] [Emphasis added]
>
> *Legitimate Expectations*: As regards Electrabel's submissions on legitimate expectations under the ECT's FET standard, the Tribunal finds no evidence that Hungary represented to Electrabel, <u>at the times of its investments</u> in Dunamenti, that it would ever act differently from the way that it did act towards Dunamenti or Electrabel.[592] [Emphasis added]

607. This is acknowledged by Claimants themselves,[593] citing *Lemire*:

> The FET standard is thus closely tied to the notion of legitimate expectations - actions or omissions by [the State] are contrary to the FET standard if they frustrate legitimate and reasonable expectations

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[589] **CL-110**, *TECO v Guatemala*, *ibid*, ¶¶621 and 622: "621. It is clear, in the eyes of the Arbitral Tribunal, that any investor has the expectation that the relevant applicable legal framework will not be disregarded or applied in an arbitrary manner. However, that kind of expectation is irrelevant to the assessment of whether a State should be held liable for the arbitrary conduct of one of its organs. What matters is whether the State's conduct has objectively been arbitrary, not what the investor expected years before the facts. A willful disregard of the law or an arbitrary application of the same by the regulator constitutes a breach of the minimum standard, with no need to resort to the doctrine of legitimate expectations.
622. There is therefore no need to dwell any further on the Parties' arguments on representations and legitimate expectations. In particular, there is no need for the Tribunal to deal with the Parties' arguments as to whether the Claimant is entitled to rely on the alleged expectations of the entity that invested in EEGSA in 1998."

[590] **CL-110**, *TECO v Guatemala*, *ibid*, ¶¶664, 665, 670 and 710.

[591] **CL-107**, *Electrabel* (Decision on Jurisdiction), *supra* note 452, ¶7.76.

[592] **RL-124**, *Electrabel* (Award), *supra* note 544, ¶155.

[593] Cl. Mem., ¶28.

on which the investor relied at the time when he made the investment.[594] [Alteration in original]

608. The same position had been adopted earlier in *Duke Energy v Ecuador*:

> To be protected, the investor's expectations must be legitimate and reasonable at the time when the investor makes the investment. The assessment of the reasonableness or legitimacy must take into account all circumstances, including not only the facts surrounding the investment, but also the political, socioeconomic, cultural and historical conditions prevailing in the host State. In addition, such expectations must arise from the conditions that the State offered the investor and the latter must have relied upon them when deciding to invest.[595] [Footnotes omitted]

609. The Tribunal turns now to an assessment of the facts of the present case, with particular attention to the role of Respondent's organs and any statements or conduct attributable to the State concerning the stability of the water tariff regime and the profits to be earned by Claimants further to ASTV's privatisation.

610. The Tribunal first considers the purpose and objectives of ASTV's privatisation and the manner in which those objectives were presented to potential foreign investors (a), as well as the broader context within which the privatisation took place (b), before engaging in an analysis of the relevant agreements (c) and their terms (d). Lastly, the Tribunal will address Respondent's argument as to the alleged illegality of the Services Agreement (e).

a) The Purpose and Objectives of the Privatisation

611. The bidding documentation confirms unequivocally that the primary purpose of ASTV's privatisation was to obtain the hands-on managerial expertise and financial clout of a foreign operator with a view to bringing ASTV into compliance with Estonian and European regulatory standards. This notably appears from the Information Memorandum, which states:

> The principal objective of the City of Tallinn from the Transaction is to attract a Strategic Investor for the management and financing of the Company in order to achieve the quality and service standards set by National and European Union regulations.[596]

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[594] **CL-1**, *Joseph Charles Lemire v Ukraine*, ICSID Case No. ARB/06/18, Decision on Jurisdiction and Liability (21 January 2010), ¶264.

[595] **RL-159**, Duke Energy v Ecuador, ¶¶ 339-340. See also **RL-158**, Enron Creditors Recovery Corporation (formerly Enron Corporation) and Ponderosa Assets, L.P. v Argentine Republic, ICSID Case No. ARB/01/3, Award (22 May 2007), ¶262.

[596] **C-10**, ASTV Information Memorandum (3 July 2000), pp 158 and 165.

612. The bidding process accordingly aimed at identifying, not a passive financial investor, but a "Strategic Investor," a partner committed to directing ASTV's technical, operational and financial development over the long term:

> The City wishes to attract an Investor who is fully committed to the development of the Company, and has the necessary technical, operational and financial capability to meet the established levels of service, as well as relevant international experience in the provision of water and wastewater services.[597]

613. The Strategic Investor would bear responsibility for determining and implementing the means and methods to meet the company's required levels of services, and its performance would be measured by reference to these service levels.[598]

614. The bidding criteria, reported above at paragraph 142, effectively excluded any domestic operator from the bidding process.

615. The bidding documentation further identified "stable and transparent tariff regulation" among the principal objectives of the privatisation, and expressly acknowledged the relationship between the water tariffs charged by ASTV to consumers and the foreign investment needed to improve and maintain ASTV's service levels.[599] The Explanatory Memorandum made this clear, expressly recognising that these tariffs must allow the Strategic Investor to earn "justified profitability" on its investment:

> One of the most important objectives of the City is to ensure the stability of water tariffs in the future. The production of high-quality drinking water and the treatment of wastewater in Tallinn require large expenses due to the peculiarity of nature. One of the most important reasons is the poor quality of the raw water – 90% of the water used in Tallinn comes from Lake Ülemiste and only 10% from groundwater. The water of Lake Ülemiste is muddy and contains a lot of seaweed. The quality of water is also affected by human activities in the vicinity of rivers and canals belonging to a water intake of 2,000 square kilometres. Large expenses are to be incurred in order to achieve a high quality in the water discharged from the treatment plant. In addition to the purification of surface water, it is also necessary to install treatment equipment on several groundwater wells. The treatment of wastewater under the requirements of the agreements concerning protection of the Finnish Gulf (HELCOM) is also expensive and requires substantial investments in the wastewater treatment plant in the near future – 313 million EEK within the next 3 years. […]
>
> Currently, Tallinn City approves the tariff on the basis of an application of a water undertaking on a yearly basis. <u>Such regulation does not ensure certainty about the development of tariffs for the City or the</u>

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[597] **C-10**, ASTV Information Memorandum (3 July 2000), p 223.

[598] **C-10**, ASTV Information Memorandum (3 July 2000), p 231.

[599] **C-9**, Minutes of the meeting of the City of Tallinn committee for preparing and implementing the tender (20 April 2000) and Explanatory Memorandum (5 March 2000), p 135.

investor. The last change in tariffs was in January 1998; since then, the actual tariff (adjusted with inflation) has continuously fallen – and the company fails to perform all obligations assumed by the loan agreement with EBRD, e.g. the obligation to increase tariffs with inflation and to keep the debt service coverage ratio at the level of at least 1.5. Neither does the applicable tariff ensure compliance with the requirements for the tariff level arising from the Public Water Supply and Sewerage Act (PWSSA). According to the PWSSA, the price of the service must ensure: (i) coverage of the production expenses, (ii) compliance with the quality and safety requirements, (iii) compliance with the environmental protection requirements, and (iv) justified profitability. […]

> Therefore, it is necessary to establish a longer-term, transparent tariff mechanism that allows for compliance with the requirements established by the laws and contracts and ensures the financing of investments, while making AS Tallinna Vesi increase efficiency. The tariff level is directly related to the required service level and the resultant investment needs, and the tariff must also allow for achieving justified profitability for the investor.[600] [Emphasis added]

616. It is in light of these considerations that the City's advisor, Suprema, suggested the formula for setting water tariffs that would later be included in the Services Agreement.[601] Bearing in mind the financial and other commitment required from the investor and the long-term, strategic nature of the investment, Suprema also warned the City of Tallinn that the investor's "main two expectations" – a stable operating environment and the ability to earn "reasonable profitability" – would have to be respected. Suprema posited that the interests of investor and the City's objectives would largely coincide in this respect:

> For the success of the privatisation, it is also important to turn attention to the expectation of the investor. Privatisation cannot be successfully conducted without taking into consideration the expectation of the investors. The more assured the investor is of the stability of the operating environment of the company and the more precisely the different aspects of co-operation between the City and investor are defined, the larger is the interest of the Investor which in turn is reflected in the higher offered price.
>
> In the case of AS Tallinna Vesi, the investment horizon is long-term (at least 15-20 years), as investments are of a long-term nature. The investor undertakes to achieve the objectives set by the City and expects to receive reasonable profitability in return. Through the ownership of the share, the profitability comprises of paid dividends and the development of goodwill.

[600] **C-9**, Minutes of the meeting of the City of Tallinn committee for preparing and implementing the tender (20 April 2000) and Explanatory Memorandum (5 March 2000), pp 139-141.

[601] **C-9**, Minutes of the meeting of the City of Tallinn committee for preparing and implementing the tender (20 April 2000) and Explanatory Memorandum (5 March 2000), p 143.

For the achievement of the main two expectations, the investors assume certainty in the following aspects:

- Control over management and the ability to have a say in developing the strategy of the company in order to secure the achievement of the objectives set by the City.
- Ability to make investment decisions according to the earlier agreed parameters.
- Clear and stable tariff regulation.
- Ability to decide over the profit distribution of AS Tallinna Vesi.

The above objectives largely coincide with the objectives of the City (efficient management of the company, investments to improve the service quality and stable tariff regulation). The regulation of the relationship between the city and investor in the aforementioned areas is discussed in Annexes 1 and 2.[602] [Emphasis added]

617. The Tribunal thus finds that ASTV's privatisation was conceived and represented to the bidders as a long-term project demanding significant financial, strategic, managerial and operational input from a foreign investor, whose investment would be recouped by means of water tariffs to be set at levels that would allow the investor to earn "justified" or "reasonable" profits over the anticipated term of the investment. The privatisation documentation did not provide any further information on this point and, as the Explanatory Memorandum itself warned that:

> Currently, Tallinn City approves the tariff on the basis of an application of a water undertaking on a yearly basis. Such regulation does not ensure certainty about the development of tariffs for the City or the investor.[603]
> [Emphasis added]

618. The Tribunal also finds that these contextual factors cannot in and of themselves substantiate Claimants' alleged legitimate expectations. Although they weighed heavily in the decision to proceed with the investment, the terms of the privatisation agreements themselves bear greater emphasis and are indeed determinative in delineating what Claimants could, and could not reasonably expect since they crystallise the common intention of the parties at the time of the privatisation.

[602] **C-9**, Minutes of the meeting of the City of Tallinn committee for preparing and implementing the tender (20 April 2000) and Explanatory Memorandum (5 March 2000), pp 146-148.

[603] **C-9**, Minutes of the meeting of the City of Tallinn committee for preparing and implementing the tender (20 April 2000) and Explanatory Memorandum (5 March 2000), p 141.

b) *The Broader Context of ASTV's Privatisation*

619. It is uncontested that ASTV's privatisation was an initiative of the City of Tallinn. Claimants have nonetheless stressed what they refer to as the national and international implications of the privatisation, due to the alleged difficulties of ASTV under the 1994 EBRD Loan (i), the role of the Central Government in the extension of the term of ASTV's license (ii) and the involvement of the EBRD through the 2000 and 2002 EBRD Loans (iii).[604] After considering these, the Tribunal will set out its findings in point (iv).

(i) <u>ASTV's Performance under the 1994 EBRD Loan</u>

620. Claimants highlight the role of the Central Government as State guarantor of the 1994 EBRD Loan and the various exchanges with the EBRD regarding compliance with the terms of this loan.[605] They argue that ASTV's poor performance could have led to the calling of the State Guarantee, which would have created an obstacle to ASTV's privatisation. By way of illustration, in a letter to the City's mayor dated 24 August 1999, copied to the Estonian Finance Ministry, the EBRD warned the City of the serious consequences of its planned decrease in water tariffs, and requested that it abandon the plan. The EBRD stated that it was "seriously concerned, not only by the breach of covenants [of the 1994 EBRD Loan] but also by the adverse effect that a reduction in tariffs would have on any future privatisation or sale of shares in Tallinn Water Limited."[606]

621. There is little doubt that ASTV was not in full compliance with the terms of the 1994 EBRD Loan prior to the privatisation. As a matter of fact, ASTV's failure to raise its tariffs in the period prior to privatisation was represented to potential investors as being non-compliant with the 1994 EBRD Loan.[607] Yet, Mr Põder, who acted as a Deputy Secretary General of the Ministry of Finance at the time and who was later employed by the EBRD in 2000, testified in this arbitration that the concern pertaining to ASTV's compliance, in particular the City's insistence on decreasing water tariffs for purely political reasons, was resolved further to the 1999 election. In fact, the City of Tallinn's decision to decrease ASTV's tariffs was revoked in November 1999, some months before the issuance of the Tender Notice in June 2000.[608] Furthermore, according to Mr Põder, the EBRD's concerns were all resolved by the time the 1994 EBRD Loan was refinanced in 2000.[609]

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[604] Cl. Mem., ¶¶39-41, 53, 54 and 111a; Cl. Reply, ¶¶20-23, 41, 43 and 60a; Cl. PHB, ¶¶66-69, 72 and 73.

[605] See *supra* at paragraphs 84-90.

[606] **C-282**, Letter from EBRD to Mr Edgar Savisaar (24 August 1999).

[607] **C-9** Minutes of the meeting of the City of Tallinn committee for preparing and implementing the tender (20 April 2000) and Explanatory Memorandum (5 March 2000), p 141; **C-10**, ASTV Information Memorandum (3 July 2000), p 195.

[608] **RL-223**, Regulation No. 100 of the City of Tallinn (24 November 1999); **C-12**, Notice of Tender (26 June 2000).

[609] Tr. Day 4 Mr Põder 185:21-187:2; Põder 1st WS, ¶2; Põder 2nd WS, ¶2.

622. The Tribunal further notes, as pointed out by Respondent,[610] that UUTBV itself remarked at the time of its investment in ASTV that the EBRD had "no complaints" about the latter's performance.[611]

(ii) The Extension of the Term of ASTV's License

623. In order to demonstrate the involvement of the Central Government in the privatisation, Claimants also highlight the Government's role in the required extension of the term of ASTV's license. As discussed above,[612] in aid of the privatisation, in view of the long-term nature of the investment and the expectations of the sort of long-term investor required, the City of Tallinn sought a derogation from the applicable national regulation so as to extend the duration of ASTV's license from five (5) to twenty (20) years.

624. In the course of this process, which took place over the spring of 2000, the Ministry of Finance and the ECA, as well as the Prime Minister himself, gained knowledge of ASTV's privatisation (if they had not previously been aware of the circumstances) and became at least tangentially involved. The City of Tallinn informed the Minister of Finance of the long-term nature of the investment required and alluded to the expectations of the "entrepreneurs" from whom it hoped to secure such an investment:

> In the current situation it is not rational or reasoned to appoint a water undertaking in the City of Tallinn for a period of 5 (five) years. This results from the fact that development of water business (reconstruction of the existing network for the purpose of improving water quality, construction of new networks to new areas) requires the development of long-term investment programmes from the water undertaking and the implementation thereof. <u>The payback period for networks and equipment is significantly longer than a 5-year period</u>. Resulting from the abovementioned a frequent change in water undertakings would not have a positive impact of [sic] the development of the water business as a whole in the City of Tallinn. […]
>
> <u>In order to ensure the fact that entrepreneurs would have economic interest for providing the services of water supply and wastewater discharge and that in the future the obligations set for the water undertaking to be established by the Development Plan would actually be carried out, the term of the exclusive right to be granted to the water undertakings should be set as the time period equivalent to the terms of the validity of four permits for special use of water (also the "TKT"), i.e. 20 (twenty) years</u>.[613] [Emphasis added]

625. This being said, there is no question that the relevant license could only be held by the water undertaking, *i.e.* ASTV, not the investor in the undertaking. And although the Ministry of

[610] Resp. Rej., ¶37.

[611] **R-323**, Letter of Mr Tim Lowe to Mr Rain Tamm (31 March 2000).

[612] See *supra* paragraphs 152 and following.

[613] **C-286**, Letter from Jüri Mõis to Siim Kallas (16 May 2000).

Finance took into consideration the capital-intensive nature of the sector in extending ASTV's license term, there is no evidence that it also took into consideration the specific interests of ASTV's future investor.[614] Nor is there any evidence that the Central Government was provided with a copy of the Services Agreement or that it considered either the particular return expected by the investor or the share price.[615]

(iii) The EBRD's Role in the Privatisation: the 2000 and 2002 EBRD Loans

626. In Claimants' view, further evidence of the national and international implications of the privatisation can be gleaned from the 2000 and 2002 EBRD Loans.[616]

627. The 2000 EBRD Loan was conditional upon the execution of agreements with the investor "acceptable to the Bank providing for a basis on which [ASTV] will, in the opinion of the Bank, be able to function as a profitable commercial enterprise and fulfil its obligation under this Agreement, including, a service agreement and a share purchase agreement."[617] Mr Põder testified that had there been concern with the privatisation agreements, the EBRD's board would have been consulted.[618]

628. As for the 2002 EBRD Loan, its terms required compliance with the Services Agreement[619] and provided the EBRD with the right to review any amendments to the Services Agreement or to the Business Plan appended to the Shareholders' Agreement.[620] The EBRD also appeared content with the regulatory mechanism referenced in the 2002 EBRD Loan, by lauding the "strong environmental impact [of the 2002 EBRD Loan] and […] the improved regulatory mechanism it promoted through the loan covenants."[621] On this point, Mr Põder testified that, during the approval process, the general tariff mechanism was discussed at the EBRD with reference to an agreement for the first five (5) years.[622] Claimants also note that the EBRD welcomed the proposed financing "particularly for its strong environmental impact."[623]

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[614] **C-14**, Response from the Ministry of Finance (20 June 2000).

[615] At the Hearing, Mr Põder, who was Deputy Secretary General of the Ministry of Finance at the relevant time, testified that he had no recollection that the government was provided with this information, Tr. Day 4 Mr Põder 214:23-215:17.

[616] Cl. PHB, ¶¶86-93.

[617] **C-17**, 2000 Loan Agreement between ASTV and the EBRD (31 October 2000), s. 3.02(a). Claimants also rely on what appears to be a response to certain correspondence that mentions that the EBRD has accepted the structure of the transaction. This document does not however indicate either the sender or the addressee (**C-287**, Responses to the 22 May 2000 Fax (undated).

[618] Tr. Day 4 Mr Põder 196:11-197:3.

[619] **C-23**, 2002 Loan Agreement between ASTV and EBRD (8 November 2002), s. 5.01.

[620] **C-23**, 2002 Loan Agreement between ASTV and EBRD (8 November 2002), s. 5.01.

[621] **C-431**, EBRD Board Minutes (4 December 2001).

[622] Tr. Day 4 Mr Põder 215:18-216:18.

[623] Cl. PHB, ¶21.

(iv) Findings of the Tribunal regarding the Broader Context of ASTV's Privatisation

629. The evidence concerning the interest and involvement of the Estonian Government and the EBRD in ASTV's privatisation confirms that the privatisation indeed resonated at both the national and international levels. In line with Claimants' submissions, the Tribunal considers that this may have provided to potential foreign investors, including UUTBV, some comfort as to the seriousness and legitimacy of the City's endeavours. It may even have informed UUTBV's views and conduct at the time of the privatisation (and the entry of the 2002 EBRD Loan). However, these aspects of the privatisation, such as they are, cannot by themselves be said to amount to any sort of assurance by Estonia, explicit or implied, capable of creating legitimate expectations as a matter of international law. Indeed, in the overall context of the privatisation, especially in the dealings between the relevant authorities and potential investors, the involvement of the national and international institutions in question was relatively minimal and, on the facts at hand, does not assist in substantiating the legitimate expectations alleged by Claimants.

c) The Nature of the Privatisation Agreements and the Capacity in which the City of Tallinn Intervened in these Acts

630. In assessing the nature of the representations made by the City through the privatisation agreements, and whether or how they may have given rise to legitimate expectations on the part of Claimants, the Tribunal will first consider the capacity in which the City of Tallinn intervened in ASTV's privatisation. After summarising the positions of the parties on this point (i), the Tribunal will consider the Estonian law expert evidence filed by the Parties (ii) and then state its findings (iii).

(i) The Positions of the Parties

631. Claimants submit that the City of Tallinn negotiated and executed the Services Agreement and approved the 2001 Business Plan in its capacity as a State authority.[624]

632. Their argument focuses on the (undisputed) characterisation of the tariff part of the Services Agreement as a public law agreement pursuant to Estonian law. Hence, they say, the negotiation and execution of the Services Agreement must be considered as an exercise of public power and, to be consistent, the same must hold true for its five (5) amendments. Claimants further argue that the 2001 Business Plan forms part of this public law relationship since the Services Agreement refers to it for the purpose of determining water tariffs.[625]

633. Respondent argues that the privatisation agreements are purely commercial acts of the City of Tallinn, save for the tariff component of the Services Agreement.[626]

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[624] Cl. PHB, ¶183.

[625] Cl. PHB, ¶¶184 and 185.

[626] Resp. PHB, ¶¶64-71.

634. Concerning the Services Agreement, Respondent relies on its Clause 34(3), which explicitly states that the Services Agreement is to be considered as a private and commercial contract: "(3) The City irrevocably and unconditionally acknowledges that the execution, delivery and performance of this Agreement constitute private and commercial (and not public) acts of the City."[627] According to Estonia, this clause reflects the common and subjective understanding of the parties at the time of the execution of the Services Agreement and undermines any relevance of the public law nature of the tariff provisions of the document.[628] Estonia submits that UUTBV's subjective understanding of the objectives and purpose of the Services Agreement and the Shareholders' Agreement are also evidenced by its comments in the course of the negotiation of the agreements, during which UUTBV took care to emphasise among other things the different purposes of the Services Agreement and the Shareholders' Agreement by notably suggesting that the Shareholders' Agreement would deal with management issues.[629] In addition, Respondent submits that the inclusion of a dispute resolution clause at Art. 37 of the Services Agreement confirms its commercial and private nature, and that it cannot be enforced against Estonia through an ICSID arbitration.[630]

635. Concerning the *Shareholders' Agreement*, Respondent reiterates that the City did not intervene therein in the exercise of its regulatory function and refers to the various statements in the Agreement to the effect that it in no way hinders the exercise of the City's governmental authority.[631] By way of example, Art. 5.1 of said agreement provides that:

> Unless the Shareholders shall otherwise agree, […] the City of Tallinn shall not use the powers available to it as a shareholder of the Company (<u>without anyhow limiting the rights and obligations of the City of Tallinn as a local government</u>) to prevent […] the conduct the Company's business […] [632] [Emphasis added]

(ii) <u>The Estonian Law Experts Evidence on the Nature of the Privatisation Agreements</u>

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[627] **C-22**, Services Agreement (including schedules) (12 January 2001), Clause 34(3), p 516.

[628] Resp. PHB, ¶71.

[629] See Resp. Rej., ¶¶103-105, referring to **R-325**, Draft Services Agreement, attachment of the letter of International Water to LHV (16 October 2000), p 30, where UUTBV provided the following mark-up regarding the termination right of the City: "the relationships between the City [of Tallinn] and the Investor should not have any affect [sic] on [the Services Agreement]. […] The sanctions with respect to non-compliance with the terms and conditions of the Shareholders' Agreement would normally be established in the Shareholders' Agreement." and **R-325**, Draft Services Agreement, attachment of the letter of International Water to LHV (16 October 2000), p 33, where UUTBV comments as follows on certain restriction of ASTV's corporate operations (such as disposal of its assets): "this paragraph (and most notably sub-paragraph (iv)) should not be included in this Agreement as they restrict the normal operations of the Company to the extent not justifiable by the nature of the Services and this Agreement. These are issues of the Company's management that are regulated in the Shareholder's Agreement. The purposes and objectives of the two agreements should not be confused."

[630] Resp. PHB, ¶¶72-75.

[631] **C-20**, Shareholders' Agreement (12 January 2001), ss. 5.1, 5.5.8 and 5.5.9.

[632] **C-20**, Shareholders' Agreement (12 January 2001), s. 5.1.

636. The Parties' Estonian law experts – Mr Rask, Respondent' expert; and Mr Pikamäe, Claimants' expert – agree that the tariff part of the Services Agreement constitutes a public law act, entered into by the City of Tallinn in its regulatory capacity.

637. But for that, the respective characterisation of the various privatisation agreements by the Parties' experts differ insofar as Mr Rask insists on the distinction between the different roles assumed by the City of Tallinn (as a government and public regulator on the one hand, and as a commercial party to a sale and a shareholder on the other hand), whereas Mr Pikamäe approaches the privatisation agreements as interconnected parts of a unified transaction that, in his opinion, concerns the performance of the City's administrative function. We summarise below their respective opinions.

- *The Services Agreement*

638. According to Mr Rask, only the tariff component of the Services Agreement (Annex E) and related provisions directly pertaining to public law powers (Mr Rask refers to the assignment by the City to ASTV of the obligation to provide public water and sewerage services) constitute an administrative act.[633] Mr Rask considers the remainder of the Services Agreement as a private, civil law contract.

639. According to Mr Pikamäe, the Services Agreement, as a whole, is an administrative act issued by way of agreement. According to Claimants' expert, this agreement comprises "essentially the permission, i.e. right and obligation granted by the City of Tallinn to ASTV to provide the services of supplying water in the specified area […]."[634]

640. The District Court of Tallinn's decision aligns with Mr Rask's opinion[635] and the reasons of both the Circuit Court[636] and the Supreme Court seem to support this position.[637] In the Tribunal's view, the key point is that the Parties' experts and the Estonian courts all agree that the tariff component of the Services Agreement is of a public, administrative law nature. The differences between the experts on the other elements of the Agreement have less bearing.

- *The Shareholders Agreement (including the 2001 Business Plan)*

641. Mr Rask opines that the Shareholders' Agreement is a civil law contract because: (1) its purpose is to regulate the decision-making as to ASTV's strategic business activities and (2) it sets out the rights and obligations of the City of Tallinn in its capacity as a shareholder of ASTV.[638]

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[633] Rask 1st ER, ¶96; Rask 2nd ER, ¶¶4 and 11.

[634] Pikamäe 1st ER, ¶¶222 and 223, referring to Clause 3 of the Services Agreement (**C-22**).

[635] **RL-55**, Tallinn District Court's case No. 3-11-1355 (31 May 2012), p 7.

[636] **C-432**, Tallinn Circuit Court Decision of 26 January 2017, ¶¶17 and 18.

[637] Supreme Court Decision (12 December 2017), ¶17.

[638] Rask 1st ER, ¶104.

642. Mr Rask acknowledges that the 2001 Business Plan addresses the determination of water tariffs. He nonetheless considers the document to be a civil instrument as it lacks any independent tariff-setting mechanism and because the City did not mention the 2001 Business Plan as a basis for the determination of the water tariffs, whereas it did refer to the applicable legislation and the 1999 PWSSA in adopting tariffs.[639] He further takes the view that the 2001 Business Plan contradicts the tariff-setting mechanism of the Services Agreement insofar as the Services Agreement provides that tariffs must be determined over a 5-year period while the 2001 Business Plan contains projections covering the entire duration of ASTV's license.[640]

643. During the Hearing, when shown the reference in the Services Agreement to the 2001 Business Plan as a criterion for determining justified profitability,[641] Mr Rask conceded that the Business Plan may form part of the public law relationship.[642] He went on to opine that because the criteria to establish justified profitability had to be adopted by the Council of the City of Tallinn, which was not the case, the Services Agreement in its entirety was illegal[643] (this question is addressed below at paragraphs 717 and following).

644. <u>Mr Pikamäe</u> disagrees and considers that the 2001 Business Plan forms part of the administrative relationship arising out of the Services Agreement. As mentioned, he considers the privatisation agreements to be interrelated. Mr Pikamäe relies in particular on the reference in Schedule E of the Services Agreement to ASTV's tariff proposals being based on a Business Plan[644] as well as on various references in the privatisation agreements and in the Information Memorandum in support of his opinion that the 2001 Business Plan was clearly intended to complement the Services Agreement with regards to the setting of tariffs. In the course of his cross-examination at the Hearing, he nonetheless acknowledged that he does not consider the Shareholders' Agreement *per se*, that is, in isolation from the other privatisation agreements, to be an administrative agreement.[645]

- *The Closing Memorandum and the Memorandum of Understanding*

645. <u>Mr Rask</u> considers that neither of these agreements are public contracts.

646. Mr Pikamäe considers the Closing Memorandum and the Memorandum of Understanding attached thereto (or at least the provisions relating to the 2001 Business Plan) to form part of the administrative relationship arising out of the Services Agreement and the privatisation agreements as a whole, based on the same reasoning developed for the 2001 Business Plan.

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[639] Rask 1st ER, ¶¶107 and 108.

[640] Rask 2nd ER, ¶26.

[641] **C-22**, Services Agreement (including schedules) (12 January 2001), Appendix E, p 616.

[642] Tr. Day 6 Mr Rask 140:15-142:2.

[643] Tr. Day 6 Mr Rask 143:11-144:24.

[644] Pikamäe 1st ER, ¶¶234-242.

[645] Tr. Day 6 Mr Pikamäe 91:10-22.

Similarly, he acknowledges that the Closing Memorandum on its own does not directly pertain to the performance of a public function.[646]

- *The Contract for the Sale and Subscription of Shares*

647. According to Mr Rask, share sales contracts are typically considered as civil law contracts, even where a public authority is one of the signatories.[647]

648. Mr Pikamäe, for his part, asserts that this agreement also forms part of the contractual arrangement setting out the terms of the privatisation on the basis that the conclusion of the Services Agreement was a condition precedent to the entry force of the Contract for Sale and Subscription.[648] Findings of the Tribunal on the Nature of the Privatisation Agreements and the City's Status

649. In view of the consensus on the public law nature of the tariff component of the Services Agreement, with which the Tribunal agrees, it is clear that the Services Agreement cannot be said to consist of a purely commercial agreement of a private law nature, creating a purely private commercial relationship between the parties. At least part – the Tribunal would say, an essential part – of the Services Agreement concerns the exercise of an important public function. In entering into the Services Agreement the City cannot be considered a "normal contractual partner." On the contrary, the negotiation and execution of the Services Agreement by the City directly implicated its sovereign prerogative, and at least in respect of this essential element of ASTV's privatisation the Tribunal finds that City of Tallinn acted in a public, regulatory capacity. The Tribunal has no doubt that the Service Agreement has been entered into by the City of Tallinn as a public law entity and ASTV.

650. This has been even acknowledged in the Shareholders Agreement's definitions:

> "Service Agreement" means the written service agreement [….] entered into between the Company and the City of Tallinn on or before the date of this Agreement to regulate and specify the Company's obligations towards the City of Tallinn as a legal person in public law, with respect to the Company's activities.[649] [Emphasis added]

651. The same is not true for the Shareholders' Agreement, which has been entered into by the City of Tallinn as a shareholder, and recognises in numerous articles that the contractual commitments entered into do not infringe on the city of Tallinn regulatory power, of which a few examples can be given here:

> Article 5.1 Principal Covenants
>
> […] Unless the Shareholders shall otherwise agree, the Investor shall use all the power available to it to cause the company to the City of Tallinn shall not use the powers available to it as a shareholder of the

[646] Pikamäe ER, ¶¶244-247.

[647] Rask 1st ER, ¶103.

[648] Pikamäe 1st ER, ¶¶234-242.

[649] **C-20**, Shareholders' Agreement (12 January 2001), s. 1.

> Company (without anyhow limiting the rights and obligations of the City of Tallinn as a local government) to prevent and the Company shall conduct the Company's business […]
>
> Article 5.2 Negative Covenants Related to the Company
>
> Unless the Shareholders shall otherwise agree and as long the City of Tallinn is a shareholder of the Company, the Shareholders acting in their capacity as shareholders of the Company Company (without anyhow limiting the rights and obligations of the City of Tallinn as a local government) shall not allow the Company to and the Company shall not […];
>
> Article 5.5 Covenants of the City of Tallinn
>
> 5.5.1. The City of Tallinn shall use its reasonable endeavours within the limits set out by the relevant applicable legal acts to fulfil its obligations […].
>
> […]
>
> Article 5.5.9. The covenants of the City of Tallinn specified in Sections 5.5.1-5.5.8 (inclusive) shall not Company anyhow limit the rights and obligations of the City of Tallinn as a local government.

652. Yet, it is readily apparent from the privatisation agreements themselves, even if they are of a different legal nature, that they are interrelated and intended to form a unified whole. The Services Agreement refers to both the Shareholders' Agreement[650] and the Share Sale and Subscription Agreement,[651] and the execution of these latter instruments was a condition precedent to the entry into force of the Services Agreement.[652] The Shareholders' Agreement and the other privatisation contracts were necessary components of the legal relationship to be established between the investor and the City of Tallinn. This arrangement was deliberately conceived by the City of Tallinn and its advisors and represented to prospective investors in the Explanatory Memorandum and the Information Memorandum.[653] Nothing in the evidence adduced or submissions made in the arbitration reasonably assails this assessment.

653. Having found that the privatisation agreements form integral parts of a single transaction, the Tribunal does not consider it necessary or particularly fruitful to assess the legal nature of each agreement, on its own, in isolation from the other components of the privatisation. Rather, to

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[650] **C-22**, Services Agreement (including schedules) (12 January 2001), Definitions section, s.v. "Shareholders' Agreement," Clauses 17 and 21.

[651] **C-22**, Services Agreement (including schedules) (12 January 2001), Definitions section, s.v. "Share Sale and Subscription Agreement," Clauses 7(4)(e)(v).

[652] **C-22**, Services Agreement (including schedules) (12 January 2001), Clause 2(1)(a).

[653] **C-9**, Minutes of the meeting of the City of Tallinn committee for preparing and implementing the tender (20 April 2000) and Explanatory Memorandum (5 March 2000), pp 149 and 154; **C-10**, Information Memorandum, pp 165 and 229.

address Claimants' claim of legitimate expectations, what is called for is an examination of the actual terms of the privatisation as manifested in the agreements.

d) The Terms of the Privatisation Agreements and the Status of the 2001 Business Plan

654. Two elements bear particular relevance for the purpose of assessing Claimants' claim of legitimate expectations as of the time of the privatisation: the mechanism for setting water tariffs (i), and the potential for a change of regulator and change in the law (ii). The Tribunal's overall determinations on the terms of the privatisation agreements are set out in sub-section (iii) below.

(i) The Mechanism for Determining Water Tariffs

- *Parties' positions*

655. It is not disputed that the provisions of the Services Agreement require that tariffs be re-set for every five-year operating period (i.e., after 2005 and after 2010).654 As discussed above, Claimants have clarified that they do not construe the Services Agreement as determining the water tariffs for the entire license period.[655]

656. The crux of the Parties' disagreement concerns the method for setting tariffs agreed at the time of the privatisation and, more specifically, the relevance if any of the 2001 Business Plan.

657. It is Claimants' case that UUTBV specifically negotiated a definition of justified profitability in the Services Agreement which included a reference to the 2001 Business Plan, and that this definition informed their legitimate expectations.[656] In their Skeleton Argument, they describe these expectations as follows:

> The Business Plan submitted with UUTBV's bid projected K factors of zero for years 6 to 15. Given the background to the privatisation, the heavily negotiated approach to justified profitability, and the terms of the Services Agreement, <u>ASTV and UUTBV's legitimate expectations at the time of the privatisation were that the K factors for the second and third Operating Periods (years 6 to 15) would be set by reference to this Business Plan</u>, and therefore any departure from zero for the K factors would be informed by departures from that Business Plan. For example, and as explained at Reply/59:

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[654] This was recognised by Claimants' Estonian law expert, Mr Pikamäe (Tr. Day 6 Mr Pikamäe 45:16-21) and by Mr Meaney, Claimants' economic expert (Tr. Day 7 Mr Meaney 25:18-21). Mr Pikamäe also recognised that a detailed business plan would have to be presented to the regulator.

[655] Claimants explained in their post-hearing submission that instead of claiming a guaranteed return, they "had a legitimate expectation that the contracts entered into on privatisation would be respected, and that when the K factors were being set for the second and third Operating Periods, they would be set by reference to the tariff path in the Business Plan, with any departure from that justified by variations from that Business Plan." (Cl. PHB, ¶117).

[656] Cl. PHB, ¶¶101-106; Cl. Mem., ¶¶80-86; Cl. Reply, ¶¶55-62.

> 1) If the City of Tallinn was requiring substantial and costly further service level improvements over and above those set by the privatisation, that might justify a positive K coefficient; and
>
> 2) Conversely, if ASTV was proving substantially more profitable than envisaged in the Business Plan, then a negative K coefficient may be justified.[657] [Emphasis in original omitted; Emphasis added]

658. Respondent replies that the Services Agreement intentionally did not fix (as the City of Tallinn did not wish to fix it) the justified profitability to be earned by ASTV over the entire mandate period.[658] Relatedly, Respondent submits that UUTBV knew, when it submitted its bid, that the 2001 Business Plan would not form part of the City's evaluation of its bid,[659] and therefore they could not have expected the City of Tallinn to implement the profitability projections included Business Plan.[660]

- *The facts*

659. The negotiating history of the privatisation agreements shows that the City had no intention that the Services Agreement would set in stone the income or profitability to be earned by ASTV over the license period. The City's advisors voiced this position expressly and clearly during the November 2000 Meeting:

> The Advisors were unwilling to consider any definition of "Justified Profitability" that specified a number (or range of numbers) or made explicit reference to the Investor's Business Plan. They specifically noted that they do not wish to create a "fixed income instrument" and that they wish to maintain incentives for the Investor.[661]

660. This is corroborated by the testimony of Mr Falko Sellner, a former employee of SevernTrent who participated in the drafting of the privatisation agreements.[662] Mr Sellner explains that the City rejected the first internal drafts of the agreement providing for a "guaranteed compensation scheme."[663] This is not really in dispute: as noted several times, Claimants disclaim any entitlement to a fixed income stream or a risk-free investment.

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[657] Claimants' Skeleton Argument, ¶41. See also Cl. Mem., ¶111c; Cl. Reply, ¶¶59-61, 63.

[658] Resp. Rej., ¶¶89-94; Resp. Rej., ¶¶56-75; Resp. PHB, ¶¶11-51.

[659] Resp. Rej., ¶¶83-85.

[660] Resp. Rej., ¶¶108-112.

[661] **C-79**, Notes of Meeting between UUTBV, Suprema, Luiga & Mugu, Allen & Overy and SevernTrent (17 November 2000), pp 1459 and 1460.

[662] Sellner WS, ¶¶3 and 8.

[663] Sellner WS, ¶21.

661. What is at issue is the legal relationship between the 2001 Business Plan appended to the Shareholders' Agreement, and the Services Agreement, and the implication if any for determining tariffs beyond the five-year Initial Period.[664]

662. The bidding documentation clearly shows that the City of Tallinn did not consider that the business plan would be a separate criterion in its evaluation of bids received from prospective investors.[665] As appears from the Information Memorandum, the City requested that bidders bid specifically on (i) the K-coefficients for the 2001-2005 period, and (ii) the price of the shares to be issued to UUTBV.[666] The City further required that the business plan to be submitted with the bids cover only the 2001-2005 period.[667]

663. This would explain why the Information Memorandum suggests that tariffs beyond 2005 would be determined based on a business plan to be submitted later on, focusing on the period in question, and not the one included in the initial bid:

> A price review will take place in the fifth year of operation which will determine the K coefficient of the tariffs for the subsequent five years. <u>The Company will submit its business plan for the period in sufficient detail to enable the Regulator to fulfill his duties</u>.[668] [Emphasis added]

664. According to Mr Sellner, the City required a business plan from the bidders in order to substantiate each bidder's planning, and to verify how the bidder supported the tariffs for the first five (5) years of the mandate. The business plan was not, in his view, intended to be referred to for the determination of tariffs beyond 2005.[669] Respondent thus argues that it is fallacious for Claimants to connect UUTBV's offer to the tariff increases beyond 2005 provided for in the 2001 Business Plan.[670]

665. Claimants, for their part, contend that the City of Tallinn effectively represented to prospective investors that a tariff increase of up to 75% would not necessarily be considered unreasonable.[671] They refer to a 27 October 2000 letter from the Privatisation Committee which, in response to requests for clarification, informed the qualified bidders that there would be a maximum escalation of K-coefficients for the first five (5) years after the closing of the privatisation transaction:

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[664] There does not appear to be any debate that the tariffs for the Initial Period were to be calculated pursuant to the K-coefficients included in the successful bid.

[665] **C-16**, Tallinn City Council Committee on Privatisation of ASTV Meeting Minutes (23 November 2000).

[666] **C-10**, ASTV Information Memorandum (3 July 2000), p 228; Sellner WS, ¶25.

[667] **C-10**, ASTV Information Memorandum (3 July 2000), p 241; **C-69**, Letter from Suprema to UUTBV (20 October 2000).

[668] **C-10**, ASTV Information Memorandum (3 July 2000), p 241.

[669] Sellner WS, ¶¶15, 23-27.

[670] See Resp. PHB, ¶¶47 and 48.

[671] Cl. Mem., ¶89.

> The Privatisation Committee has resolved at the meeting on October 23, 2000 that the cumulative escalation of the K-coefficients (i.e. real change in tariffs) over the 5-year period after Closing must not exceed 75%. Any offer containing K-coefficients leading to higher escalation of tariffs, shall be deemed unreasonable and disqualified.[672]

666. The evidence does not disclose any other specific indication of what the City would have deemed to be an unreasonable level of profit.

667. It is noted that the draft privatisation agreements evolved throughout the parties' negotiations. In particular for present purposes, it is noted that further to the November 2000 Meeting, and thus, after the issuance of the Information Memorandum, the City of Tallinn agreed to include the "vision presented in the business plan" among the criteria for establishing justified profitability after 2005.[673]

668. This development was given effect in Schedule E to the Services Agreement, on which Claimants place great emphasis:[674]

> <u>The Parties proposing Justified Profitability shall select 5 suitable market comparables and establish an appropriate level of Justified Profitability and further taking into account</u>
>
> (i) generally accepted commercial principles for water and wastewater utilities
>
> (ii) the specific economic situation in Tallinn and Estonia and
>
> (iii) <u>the Business Plan.</u>[675] [Emphasis added]

669. Claimants construe the phrase "Business Plan" as meaning specifically the 2001 Business Plan submitted with UUTBV's bid.[676] However, as pointed out by Respondent, the Services Agreement does not define the phrase "business plan" and the use of capital letters throughout this agreement appears inconsistent.[677] Respondent further argues that the consideration of

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[672] **C-72**, Letter from Suprema to UUTBV (27 October 2000).

[673] **C-16**, Tallinn City Council Committee on Privatisation of ASTV Meeting Minutes (23 November 2000), pp 283-284. It did not include, after the words "the business plan," the phrase "of the Bidder submitted at the time of the Bid" as had been suggested by UUTBV, **C-80**, Letter from UUTBV to Suprema (18 November 2000), p 1462. Respondent claims that the reference to the "*vision"* offered by the business plan, when considered in context, cannot be a reference to the implied profitability of the business plan, Resp. Rej., ¶74 and Resp. PHB, ¶¶40 and 41.

[674] Cl. Mem., ¶111b; Cl. Reply, ¶¶60b, 60c, 60d.

[675] **C-22**, Services Agreement (including schedules) (12 January 2001), p 618.

[676] Claimants infer this from the use of capital letters, Tr. Day 1, Claimants' Opening Statement, 42:10-46:23.

[677] Respondent refers to Schedule D, Part III, Section B, which refer to both "business plan" and "Business Plan" in the same paragraph, **C-22**, Services Agreement (including schedules) (12 January 2001), p 615: "Failure constitutes non completion and commissioning of Investment plan improvements in accordance

any business plan covering a particular operating period would only be subsidiary to the comparison with the selected market comparables and the other factors enumerated in Schedule E.[678]

670. The 2000 November Meeting also led Suprema, one of the City's advisors, to recommend that the business plan submitted by the winning bidder be appended to the Shareholders' Agreement, and that the signatories of the Shareholders' Agreement should undertake to carry out that business plan.[679] This recommendation was eventually implemented in the Shareholders' Agreement by means of the parties' agreed commitment to make reasonable efforts to ensure the fulfilment of the 2001 Business Plan.[680]

671. The Letter of Understanding similarly records the parties' comprehension of the purpose of the 2001 Business Plan attached to the Shareholders' Agreement:

> Whereas, in connection with its bid for the acquisition of the majority shareholding in AS Tallinna Vesi (the "Company") the Investor has submitted a business plan ("Business Plan") to the City;
>
> Whereas, the City has reviewed the Business Plan and has approved it and accepted it;
>
> Whereas, the City has asked the Investor to clarify certain issues addressed in the Business Plan and related to management of the Company and has received an explanation from the Investor that the City deems satisfactory. Now therefore, the Parties have executed this Letter with the purpose to describe their mutual understanding about the interpretation of the Business Plan. […]
>
> 1.4 It is the intention of the Parties to co-operate in good faith and to make their best efforts in order to ensure implementation of the Business Plan (as it may be amended from time to time) and to guarantee the financial and technical strength of the Company [ASTV] […]
>
> 1.5 The Parties understand and agree that the success of [ASTV] and the implementation of the Business Plan are grounded on the good faith co-operation of the Parties and on the performance of the mutual obligations and undertakings that have been described in the documents related to the contemplated transaction.
>
> 1.6 The Investor [UUTBV] has submitted its bid for the shares of [ASTV] with the understanding and assumption that as a shareholder

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with Business Plan. The business plan may be amended and agreed during the Initial Period in line with operational improvements initiated by the Company and agreed with the City."

[678] Resp. PHB, ¶20.

[679] **C-81**, Email from Priit Koit to Tim Lowe (21 November 2000), Attachment: "Memorandum for International Water / United Utilities regarding incorporation of changes to the Transaction Documents and the Service Agreement" (20 November 2000), p 1464.

[680] **C-20**, Shareholders' Agreement (12 January 2001), p 368, s. 5.5.8.

> of [ASTV] the City of Tallinn will act in the best interests of [ASTV], will co-operate with [UUTBV] in the implementation of the Business Plan and will abstain from any action that may imperil such implementation […]
>
> 2.5 The City hereby confirms that it has carefully reviewed the Business Plan and its annexes, that the Business Plan (including its annexes) as presented is acceptable to the City […] The City further confirms that to the best of the City's knowledge, the assumptions, conclusions and understandings on which the Investor has based the Business Plan (and including its annexes) and that have been expressly described in the Business Plan are correct, reasonable and acceptable to the City. [Emphasis added]

672. As stated in the excerpt immediately above, before signing the Letter, the City of Tallinn "carefully reviewed" the 2001 Business Plan, which embraced the entire license period, and found it to be "acceptable to the City." The City approved it after the Privatisation Committee had determined, on 6 December 2000, that UUTBV's bid was the best of the bids received.[681] On 12 December 2000, Suprema requested UUTBV particulars on the 2001 Business Plan and mentioned that SevernTrent had already examined it from a "technical perspective."[682] On 18 December 2000, UUTBV responded to Suprema's requests[683] and, three (3) days later, the Tallinn City Government passed a resolution declaring UUTBV's bid to be the best.[684]

673. Respondent underlines that the Letter of Understanding only addresses management matters, as opposed to commercial matters, and does not relate to "justified profitability."[685] Respondent also relies on Clause 2.1 of the Closing Memorandum, which provides that the Articles of Association and the applicable law take precedence over the 2001 Business Plan.[686]

674. For their part, Claimants place special reliance on both the "front-loaded" investment structure of UUTBV's bid and the implied return of 14.2% projected by the financial model appended to the 2001 Business Plan (the "**Financial Model**").[687]

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[681] **C-86**, Draft Resolution of the City of Tallinn (6 December 2000).

[682] **C-87**, Letter from Pritt Koit to Tim Lowe (12 December 2000).

[683] **C-89**, Letter from Tim Lowe to Pritt Koit (18 December 2000).

[684] **C-48**, Resolution of the City of Tallinn regarding the Issue and Sale of Shares of ASTV (21 December 2000).

[685] The most closely related matter to the tariffs commented in the Letter of Understanding is the definition of "Reasonable Costs" (see s. 7.3.3 of the 2001 Business Plan, **C-20**, Shareholders' Agreement (12 January 2001)).

[686] **C-49**, Closing Memorandum (24 January 2001), Appendix A, Clause 2.1.

[687] **C-20**, Shareholders' Agreement (12 January 2001), Appendix 1. The Financial Model's projections were derived from the K-coefficients for the first five (5) years and the assumption that ASTV's tariff would remain unchanged in real terms for the remainder of the mandate. It also included projected distributions to ASTV's shareholders.

675. First, UUTBV claims that its bid was conceived specifically to address the City's stated desire to avoid drastic tariff increases during the initial years after privatisation, as confirmed by Mr Sellner during the Hearing.[688] In fact, UUTBV's bid provided for zero tariff increases until year 4, even though the required capital investment could not wait and so was "front-loaded" in the first years of the mandate.[689] By contrast, the 2001-2005 K-coefficients put forward by the other qualified bidder, CLIG 4 would have seen significant tariffs increase immediately upon privatisation.[690]

676. Second, UUTBV's 2001 Business Plan itself indicates that ASTV's profitability would be considered over the entire mandate period, as opposed to shorter periods of time, and that the determination of tariffs for the two (2) last Operating Periods (beyond 2005) were integral to the profitability analysis and projections, which fundamentally shaped Claimants' expectations.[691]

677. For example, although it covers in detail only the years 2001-2005, the Shareholders' Agreement states that the 2001 Business Plan establishes the basis on which subsequent Operating Periods, and the business plans covering those periods, will be defined:

> This Business Plan covers in detail the period 2001-2005 inclusive, and provides the commercial, financial, operational and technical basis upon which the period from 2006 onwards will be defined. This Business Plan will therefore be used as the basis for the drafting of future Company Business Plans.[692]

678. As well, the 2001 Business Plan explicitly states the investor's expectation that justified profitability for the second and third Operating Periods will be determined in accordance with its Appendix 4:

> We note that Schedule E of the Services Agreement provides for the selection of 5 suitable market comparables and establishment of an appropriate level of Justified Profitability by further taking into account:
>
> • generally accepted commercial principles for water and wastewater utilities

[688] Tr. Day 4 Mr Sellner 19:3-12: "Look, I tell you what I recall, okay? I don't want to speculate here. The City of Tallinn didn't want any increases, at least not in the beginning. Now, there wasn't really a system in place that could predict the tariffs beyond the first five years. So at the time of the transaction, there wasn't a tariff development system there. So what the City really wanted beyond this five years in terms of tariff policy would be a compromise between 'I want you to invest into or connect et cetera' and an appropriate tariff against it."

[689] Cl. Mem., ¶¶92 and 95b. The projected capital investments are laid out at Appendix 3 of the Business Plan, **C-20**, Shareholders' Agreement (12 January 2001), pp 461-463.

[690] **C-48**, Resolution of the City of Tallinn regarding the Issue and Sale of Shares of ASTV (21 December 2000).

[691] Cl. Mem., ¶94.

[692] **C-20**, Shareholders' Agreement (12 January 2001), s. 1.1 of the 2001 Business Plan, p 383.

• the specific economic situation in Tallinn and Estonia, and

• the Business Plan.

This assessment can also include the performance of the Company in the immediately preceding year of operation. IWUU envisages the mechanism for setting the Justifiable Profit will be in accordance with the calculation exhibit in Appendix 4 of this Business Plan.[693]

679. Moreover, the 2001 Business Plan reiterated that UUTBV's offer was linked to the specific increases in tariffs set out in its financial model:

> IWUU's offer is linked to specific increases in tariffs defined in the financial model included in this Business Plan and the formula linking the offered price per share and the tariff increases is included in the financial model. IWUU is prepared to reallocate the tariff increases to better suit the objectives of the City if it would be felt by the City to beneficial.[694]

680. Finally, Claimants refer to the bid of the only other qualified bidder, CLIG 4. As did UUTBV, CLIG 4 also included with its bid a business plan laying out financial projections covering the entire mandate period and expressed the reasonable expectation that justified profitability would be considered over this whole period.[695]

681. By way of reply, Respondent submits that Claimants could not have expected that the City of Tallinn would implement the projections included in the 2001 Business Plan.[696] It notes that Section of 7 of the 2001 Business Plan, reproduced above at paragraph 678, merely states that the investor "envisages that the mechanism for setting the Justifiable Profitability will be in accordance with the calculation exhibit in Appendix 4 of the Business Plan" [emphasis added].[697] Furthermore, Appendix 4, which lays out the method for calculating tariffs and "justified profits," does not refer to the Financial Model. The "Justifiable Profit" section of Appendix 4 rather expands on the selection of the comparables for establishing justified profitability, as contemplated by Schedule E of the Services Agreement.[698]

682. In any event, Respondent argues that it would not have been possible to set the post-2005 tariffs on the basis of the 2001 Business Plan since Schedule E of the Services Agreement refers to a future business plan pertaining to "the period to be regulated."[699] Relying on a pre-

[693] **C-20**, Shareholders' Agreement (12 January 2001), s. 7.3.1 of the Business Plan, p 446; see also s. A.4.3 ("Justifiable Profit"), pp 465 and 466, which defines the methodology to set out tariffs.

[694] **C-20**, Shareholders' Agreement (12 January 2001), s. 7.4 of the Business Plan, p 447.

[695] Cl. Reply, ¶60e, referring to **C-386**, CLIG 4 Business Plan submitted with its bid for ASTV (1 December 2000), pp 6420 and 6421.

[696] Resp. PHB, ¶¶44-46.

[697] **C-20**, Shareholders' Agreement (12 January 2001), s. 7 of the 2001 Business Plan, p 446.

[698] **C-20**, Shareholders' Agreement (12 January 2001), Appendix 4 of the 2001 Business Plan, pp 462-466.

[699] **C-22**, Services Agreement (including schedules) (12 January 2001), p 617.

set level profitability would further be impossible since some data could not be forecast, such as ASTV's sales, production costs and investments and sources of funding over the entire mandate period, which could not have been known in 2001.[700] In addition, the 2001 Business Plan did not contain the required level of detail for the years after 2005.[701]

683. Finally, Respondent argues that the 14.2% profitability implied by the 2001 Business Plan cannot in any case be considered justifiable.[702] First, Schedule E of the Services Agreement provided that justified profitability would be determined primarily on the basis of a comparative analysis of five (5) contemporaneous market proxies, which could not have been conducted in 2001.[703] Second, the 14.2% profitability benchmark is not stated expressly in the 2001 Business Plan; it is the product of an analysis by Mr Meaney, who admitted that this calculation required that he exercise certain judgment the basis of which is not specified in the 2001 Business Plan.[704]

- *The Tribunal's findings on the mechanism for determining water tariffs*

684. The Tribunal agrees with Claimants that the parties to the Services Agreement considered the meaning of justifiable profitability during their negotiation. This was motivated by the investor's concern regarding the open-ended nature of the 1999 PWSSA and its desire to curtail uncertainty in that respect. What is at issue, however, is whether these negotiations resulted in a commitment by the City, the only State entity involved, regarding the tariff-setting mechanism and, more generally, ASTV's profitability.

685. Notwithstanding that the Services Agreement does not define the phrase "Business Plan," the Tribunal accepts that Schedule E likely refers to the 2001 Business Plan, though it considers the scope and significance of this reference to be far narrower than Claimants contend. In the Tribunal's opinion, reference to the 2001 Business Plan in this context merely provides particulars on the application of the mechanism already set out in the Services Agreement.

686. Indeed, the reference to the 2001 Business Plan at Schedule E cannot extend to the Financial Model, or to the investor's anticipated returns. On a plain reading of Schedule E, the mention of the 2001 Business Plan primarily relates to the sub-section of the 2001 Business Plan on "Justified Profitability." This section as well as the appendix to which it refers do not mention the Financial Model. They rather define the expected return with reference to the selected proxies, as also foreshadowed by Schedule E of the Services Agreement:

> Comparison will be made with Estonian companies in business areas such as waste disposal, electricity production, and other utility type

[700] Respondent refers to the testimonies of Dr Hern (Tr. Day 7 Dr Hern 154:21-155:13) and Mr Sellner (Tr. Day 4 Mr Sellner 81:16-82:14), Resp. PHB, ¶34.

[701] See **C-20**, Shareholders' Agreement (12 January 2001), p 383, which states that the 2001 Business Plan covers in detail the 2001-2005 period.

[702] Resp. PHB, ¶¶25-30.

[703] Respondent relies on Mr Meaney's testimony (Tr. Day 6 Mr Meaney 252:18-253:5), Resp. PHB, ¶27.

[704] Tr. Day 7 Mr Meaney 6:17-23, 7:18-21, 8:19-9:1, 7:12-17, 8:6-8.

businesses. The minimum return to the Company will always be in line with these proxies.[705] [Emphasis added]

687. Even if it could be said that Schedule E referred to the entirety of the 2001 Business Plan, which the Tribunal does not accept, the Tribunal would still find that this reference is of limited importance considering that Schedule E ascribes greater weight to several other elements factors for the purpose of fixing the K-coefficients (and thus the water tariffs), including an analysis with 5 "suitable market comparables." This is consistent with the evidence of both Mr Pikamäe, who testified that all of the specific factors listed in Schedule E were intended to be subsidiary to the analysis of the selected comparables, as well as Mr Gallienne, who agreed that the five (5) comparables was the starting point of the analysis.[706]

688. As a consequence, the reference to the 2001 Business Plan at Schedule E cannot substantiate a legitimate expectation that a departure from zero (0) for the K-coefficient would be informed by the 2001 Business Plan[707] or, more generally, that the investor could legitimately expect to earn any return implied therein. The situation thus significantly differs from that in *Walter Bau v Thailand*, commented above at paragraph 602, where the parties, including State entities, explicitly considered and addressed the level of expected return.

689. The undertaking of the City to use reasonable efforts to implement the 2001 Business Plan, as recorded in the Letter of Understanding, does not affect this finding. The Letter of Understanding merely consists of a best-effort undertaking in this regard, which can hardly be assimilated to a specific commitment towards the investor concerning the determination of tariffs. The general nature of this undertaking cannot displace, or supplement, the terms of the Services Agreement pertaining to the mechanism for setting tariffs or, more precisely, the meaning of justified profitability.

(ii) The Stability of the Regulatory Framework

690. The second element pertinent to the analysis of Claimants' expectations consists in the various clauses of the privatisation agreements regarding changes in the law and the identity of the regulator.

- *Positions of the Parties and relevant facts*

691. Respondent submits that, in the Service Agreements, ASTV expressly accepted that the regulatory framework might change over the license period, and that ASTV undertook to comply with such changes.[708]

[705] **C-20**, Shareholders' Agreement (12 January 2001), Appendix 4 of the Business Plan, p 465.

[706] Tr. Day 6 Mr Pikamäe 68:6-13; Tr. Day 2 Mr Gallienne 203:3-10.

[707] See the description by Claimants of their expectations reproduced above at paragraph 657.

[708] Resp. PHB, ¶¶52-63; Resp. Rej., ¶¶95 and 96; Resp. C-M, ¶¶104-110.

692. First, the definition of ASTV's mandate refers to the "right to charge Tariff pursuant to the Statutory Requirements,"[709] which are defined as comprising changes to the applicable law and regulations over time:

> [A]ll applicable laws, regulations and legal requirements and Directives <u>having the force of law from time to time</u> during the Mandate Period and the requirements of all Required Consents […][710] [Emphasis added]

693. Second, Clause 7, which specifically governs the setting of tariffs, also refers to the "Statutory Requirements":

> The Tariffs which the Company may charge to Clients shall be determined in accordance with the provisions of this Agreement and Statutory Requirements and as provided in this Clause 7.[711]

694. The same clause further provides that the tariff shall reflect the K-coefficient "to the extent consistent with the Tariff Criteria,"[712] which are similarly defined as "the criteria for determining the Rates of Tariffs as set out in Part I of Schedule E as the same may be amended or supplemented from time to time in accordance with the Statutory Requirements"[713]. Similarly, Schedule E: Part 1 refers to the setting of tariff "in accordance with the PWSSA,"[714] which is also defined as including its amendments.[715]

695. Third, Respondent emphasises that Clause 10(1)(a) of the Services Agreement provides that the Statutory Requirements prevail over the terms of the agreement in case of conflict:

> Notwithstanding any other provision of this Agreement, the Company shall at its own cost carry out its obligations under this Agreement and shall comply at all times with all Statutory Requirements and Required Consents (including those introduced after the date of this Agreement).[716]

696. Fourth, ASTV has expressly undertaken to comply with the "Statutory Requirements."[717]

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[709] **C-22**, Services Agreement (including schedules) (12 January 2001), Clause 1, s.v. "Mandate."

[710] **C-22**, Services Agreement (including schedules) (12 January 2001), Clause 1, s.v. "Statutory Requirements."

[711] **C-22**, Services Agreement (including schedules) (12 January 2001), Clause 7(1)(a).

[712] **C-22**, Services Agreement (including schedules) (12 January 2001), Clause 7(4)(b), p 489.

[713] **C-22**, Services Agreement (including schedules) (12 January 2001), Clause 1, s.v. "Tariff Criteria," p 482.

[714] **C-22**, Services Agreement (including schedules) (12 January 2001), Schedule E: Part I, p 616.

[715] **C-22**, Services Agreement (including schedules) (12 January 2001), Clause 1, s.v. "PWSSA," p 480.

[716] **C-22**, Services Agreement (including schedules) (12 January 2001), Clause 10(1)(a).

[717] **C-22**, Services Agreement (including schedules) (12 January 2001), Clause 10(1)(b).

697. Mr Rask, Respondent's Estonian law expert, opines that under Estonian law these provisions make clear that ASTV recognised and agreed that it would be bound by changes to the regulatory framework, including changes to the 1999 PWSSA.[718]

698. Respondent also submits that Clause 5(4)a) of the Services Agreement anticipated a change of regulator:

> It is acknowledged by the parties that under Statutory Requirements to be enacted in the future, <u>certain of the functions of the Mandate Monitoring Unit may be transferred to an independent water utilities regulator (the "Regulator") pursuant to a regulatory framework to be established in accordance with Statutory Requirements</u>. To the extent that such functions are so transferred, the Mandate Monitoring Unit shall cease to exercise such functions.[719] [Emphasis added]

699. As noted above at paragraph 180, the Services Agreement defines the Regulator as including an entity to be appointed pursuant to the framework for the establishment of the MMU, the purpose of which purpose was to monitor ASTV's compliance with the Levels of Services.[720]

700. Respondent draws support, in a similar way, from the undertaking by ASTV to comply with any orders and directives issued by "any Competent Authority" pursuant to Clause 10(1)(b) of the Services Agreement, whereas the definition of "Competent Authority" was open-ended:[721]

> "Competent Authority" includes any court of competent jurisdiction and any local, national or supranational agency, inspectorate, department, local city, minister, ministry, official or public or statutory person (whether autonomous or not) acting within their competence and authority in or of the Government and includes (without limitation) the Regulator, the Tallinn Environmental Agency and the Tallinn Health Protection Authority […].[722]

701. Mr Sellner, a member of the team advising the City of Tallinn on the privatisation, offered relevant evidence on this point. He confirmed that the identity of the regulator, as well as the regulatory regime remained unknown throughout the privatisation process: "there was no regulator, there was no regulatory regime."[723] Questioned on the discussion of the same subject between the City, its advisors and the bidders, he explained that, notwithstanding the

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[718] Rask 1st ER, ¶¶128-130.

[719] **C-22**, Services Agreement (including schedules) (12 January 2001), Clause 5(4)(a), p 487.

[720] **C-22**, Services Agreement (including schedules) (12 January 2001), Clause 1, s.v. "Regulator," p 481: "Regulator" means the independent water utilities regulator appointed pursuant to the regulatory framework referred to in Clause 5(3)."

[721] **C-22**, Services Agreement (including schedules) (12 January 2001), Clause 10(1)(b), p 493.

[722] **C-22**, Services Agreement (including schedules) (12 January 2001), s.v. "Competent Authority," p 476.

[723] Tr. Day 4 Mr Sellner 52:3-5. See also Tr. Day 4 Mr Sellner 12:12 and 19:5-7.

lack of written record on this point, it was obvious that the City of Tallinn could not bind any future regulator by way of the privatisation agreements.[724]

702. According to Mr Sellner, it also was also clear to every stakeholder that the City of Tallinn, also an owner of ASTV, was not a regulator in the usual sense. The expectation was thus that the regulatory functions assumed by the City at the time would be transferred to an independent State authority, referred to as the "Regulator" in the draft agreements. Until this transfer, the City's advisors had suggested that the MMU assume ASTV's regulatory matters, including tariffs.[725] Mr Sellner explained that, whenever bidders raised the issue of tariff setting for the years after 2005, they were told that there could be "no guarantees, especially given that the MMU was yet to be established, and even that would in turn be replaced by a new regulator further in the future, whom the City of Tallinn could not bind by the contracts signed upon the privatisation."[726]

703. For their part, Claimants argue that references in the Services Agreement to "Statutory Requirements" and the like cannot displace the parties' intentions and expectations that the tariffs were to be set according to parameters determined in the Services Agreement:

> The Services Agreement was the solution adopted by the City of Tallinn, to provide sufficient clarity of the regulatory and tariff regime that would apply to provide bidders with the confidence to bid in the knowledge they would be able to obtain a return over the period of the Services Agreement. It should be borne in mind that while each of the bidders could comment on and propose changes to the Services Agreement, it was ultimately the City of Tallinn, as regulator, that determined what was in the final version offered to all of the Qualified Bidders.[727]

704. Therefore, changes in the applicable legal framework could not have been, and were not, intended or expected to annihilate completely the tariff framework established by the Services Agreement on the basis of which the privatisation proceeded.[728] This understanding would be consistent with and further demonstrated by the fact that the privatisation agreements do not

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[724] Tr. Day 4 Mr Sellner 52:11-25: "Q. […] The question was: was there any discussion that the City of Tallinn could not bind any future regulator by the contracts signed at the time of privatisation? A. There was discussion, of course, yes, because there was no regulatory regime. Q. Do you recall seeing any document where this was recorded? A. Where what was recorded? Q. That the City of Tallinn could not bind any future regulatory regime? A. Well, that goes without saying. How could it possibly be done by a regime that we don't know how it will be?" [Emphasis added]

[725] Sellner WS, ¶¶14 and 15. He further explained that an MMU does not generally replace the regulator, since regulatory functions lie solely with sovereign entities. Rather, the MMU was seen as an advisor to the actual regulator, the City of Tallinn.

[726] Sellner WS, ¶24.

[727] Cl. PHB, ¶75.

[728] Cl. Reply, ¶¶236-252.

set out a general applicable tariff regime, but apply specifically and solely to the privatised ASTV.[729]

705. Regarding the possibility of a change of regulator, Claimants do not dispute that the Services Agreement foreshadowed the appointment of a new regulator.[730] In their submission, however, such a change was not intended to divorce the determination of tariffs from the monitoring of the quality of ASTV's services, the task to be entrusted to the MMU. This can be inferred for example from Clause 5(4)(d) of the Services Agreement, which states that:

> [I]n addition to exercising the functions of the Mandate Monitoring Unit, the Regulator may also be the person responsible under the Statutory Requirements for the setting of Tariffs and the provisions of Clause 7(4) and Clause 9 shall apply accordingly.[731] [Emphasis added]

706. In this respect, it is also to be noted that, pursuant to Clause 7(4), the City undertook that it, the "Regulator" or any other person responsible for the setting of tariffs shall determine these tariffs according to Clause 7 of the Services Agreement, which lays out the method for determining tariffs. It is also indicated in this Article 7(4) that the Rates can be modified as a consequence of a change of law.

707. In the same vein, Mr Gallienne testified that he was aware that a change of regulator could occur, but understood that any new regulator would "regulate [ASTV]'s contract."[732]

- *Findings of the Tribunal regarding the stability of the regulatory framework*

708. The Tribunal agrees with the interpretation offered by Respondent. The Services Agreement terms plainly disclosed to Claimants that the regulatory framework was not static and, what is more, that change was indeed likely. There is no stabilisation clause here; the relevant provisions could even be said to comprise anti-stabilisation clauses.

709. These elements must also be considered against the legal environment prevailing in 2001. At that time, the PWSSA was a newly enacted law within a newly independent State and the evidence establishes that this yielded uncertainty (which, as commented in the previous section, provoked discussion among other things on the meaning of justified profitability). Moreover, the City of Tallinn, the sole State entity involved in the privatisation and which made any representations whatsoever to the bidders, did not have authority under Estonian law to guarantee the maintenance of the 1999 PWSSA or the stability of any element of the Estonian legal order. In the light as well of Mr Sellner's evidence, it simply cannot be sustained that an

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[729] Cl. Reply, ¶194.

[730] Tr. Day 1, Claimants' Opening Statement, 38:5-6.

[731] Cl. Reply, ¶¶247-252, referring to **C-22**, Services Agreement (including schedules) (12 January 2001), Clause 5(4)(d).

[732] Gallienne 2nd WS, ¶25; Tr. Day 2 Mr Gallienne 210:17-212:4.

investor as sophisticated as UUTBV[733] could have formed the expectation that the regulatory regime prevailing at the time of the investment would apply throughout the Mandate Period.

710. This is so irrespective of the specificity of the tariff regime that the parties to the privatisation agreements may have set out to craft. The City of Tallinn and the investors may have negotiated an interpretation of "justified profitability" and a mechanism for setting tariffs under the 1999 PWSSA. They could not, however, and it could not have been reasonably understood, that in doing so they would bind the Central Government and the Estonian Parliament to a legislative or regulatory freeze or to a commitment to respect that mechanism notwithstanding legislative change. The current matter is not analogous to *Perenco v Ecuador*, commented above at paragraphs 598-600, insofar that, here, the privatisation agreements were not "anchored in a legislative framework duly considered and enacted by the [Estonian Parliament]."[734]

e) Conclusions of the Tribunal on Claimants' Legitimate Expectations at the time of the Privatisation

711. In the light of the foregoing, the Tribunal is not satisfied that, in entering into the privatisation agreements, Claimants formed legitimate expectations protected under the Treaty.

712. That the privatisation was aimed at attracting a foreign investor and its expertise, that the investment was understood to be a long-term project, and that the investor structured its bid in a "front-loaded" manner may all be so. These do not, however, substantiate either the legitimacy of the Claimants' expectations under international law or the far-reaching obligations of Respondent that Claimants allege and seek to vindicate here.

713. As mentioned above, the commitment on which the investors claim to have relied in making their investment must be assessed by reference among other things to the terms of the relevant contracts. Context is certainly significant. However, the privatisation agreements at issue here themselves belie Claimants' claims.

714. As noted above, the Tribunal does not find that the privatisation agreements or other manifestations of the will of the City contained or constituted a commitment to any type of implied return or specific level of profitability.

715. Moreover, not only do the privatisation agreements lack any stabilisation clause, but their terms plainly exclude any expectation of legal or regulatory stability, or any specific commitment to shield the privatisation from future legal or regulatory change – which is perhaps not surprising given the lack of involvement in the privatisation by the Central Government, the State entity with jurisdiction to adopt and amend the PWSSA.

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[733] Ancillary, the Tribunal notes that the Information Memorandum advised the prospective bidders to seek their own legal advice regarding the legal statement made there which included general explanation on the PWSSA and the applicable regulations, **C-10**, ASTV Information Memorandum (3 July 2000), p 158.

[734] See **CL-111,** *Perenco v Ecuador*, *supra* note 550, ¶563.

716. In the circumstances, Claimants could not legitimately expect that what they refer to as the "key principles" of the privatisation agreements would be maintained throughout the Mandate Period.

f) The Legality of the Services Agreement and the 2002 and 2007 Amendments

717. Estonia claims that the Services Agreement, the 2002 Amendment as well as the 2007 Amendment were unlawful. Although it is not strictly necessary to do so, the Tribunal will briefly address these issues for the sake of completeness.

718. Mr Rask, Respondent's legal expert, posits that the Services Agreement and its amendments were formally unlawful because they were entered into by the Tallinn City *Government* rather than the City *Council.*[735] According to him, the City Council wrongly delegated the establishment of a mechanism for setting ASTV's tariffs to the Tallinn City Government in adopting the 22 December 1999 Resolution and then contravened to the 1999 PWSSA, which required that such a mechanism be established by the Council itself.[736]

719. Mr Rask also opines that the Services Agreement, the 2002 and the 2007 Amendments were *substantially* unlawful for they would not prescribe the determination of tariffs based on costs. This unlawfulness would be heightened for the 2002 and 2007 Amendments, since they would both fix tariffs over an improperly long period.[737]

720. Mr Rask goes on to explain that, as a matter of Estonian law, an administrative act (or administrative contract) will be deemed retroactively void where its illegality was obvious (or if declared as such by a court or the parties to the agreement). In the case at hand, he concludes that it is "debatable" whether the Services Agreement was *null ab initio*, and defers to the Estonian courts on this point. Yet, the 2002 and 2007 Amendments' unlawfulness would be obvious, thereby warranting a finding of retrospective nullity.[738]

721. With regards to the *formal* unlawfulness, both the Tallinn District Court and the Supreme Court of Estonia have ruled that it is inappropriate for Estonia to raise the formal unlawfulness of the Services Agreement. The Tallinn Circuit Court found that the Services Agreement (and its amendments) could be performed until 31 October 2010 (*i.e.* up to the entry into force of the AMB) and that Estonia may not "retrospectively raise" the question.[739] The Supreme Court of Estonia reached a similar conclusion but added that, upon the entry into force of the 2010

[735] Rask 2nd ER, ¶¶46-70.

[736] **RL-67**, Regulation of the Tallinn City Council No. 47 "Procedure for regulating the price of the water supply and sewerage service of Tallinn public waterworks and sewerage" (22 December 1999). This resolution merely restates the relevant provisions of the 1999 PWSSA.

[737] Rask 1st ER, ¶¶141-144; Rask 2nd ER, ¶¶71-82 and ¶111.

[738] Rask 1st ER, ¶¶18, 157 and 158.

[739] **C-432**, Tallinn Circuit Court Decision of 26 January 2017, ¶19.

PWSSA, the Services Agreement was no longer capable of performance because this new legislation had modified the principles for calculating justified profitability.[740]

722. In the light of these findings, the Tribunal does not consider it necessary to address Mr Rask's somewhat qualified suggestion concerning the formal unlawfulness of the Services Agreement and its 2002 and 2007 Amendments.

723. With regards to the *substantive* unlawfulness, the Circuit Court and the Supreme Court both stated interpreted the 1999 PWSSA as precluding the fixing of tariffs over an extensive period of time, but both refrained from making any finding as to the illegality of the agreements at hand and the obvious character of such illegality.[741]

724. In the Tribunal's opinion, Respondent has failed to establish that the 2002 and 2007 Amendments, as well as the Services Agreement, must be found null due to their alleged substantive unlawfulness. Such unlawfulness, if any, could hardly have been considered as obvious considering that industry practice may diverge, as discussed below at paragraphs 849 and following, and the absence of legislative guidance, let alone any obvious limitation under applicable Estonian law at the time.

5) The Impact of Post-Privatisation Events on Claimants' Legitimate Expectations

725. The Parties have also made detailed submissions commented on certain post-privatisation events that, in their view, either confirmed or undermined any legitimate expectations that Claimants might have held. The Tribunal addresses these briefly below, notwithstanding that their bearing is limited in view of the finding of absence of legitimate expectations at the time of the privatisation.

a) The Payment of Management Fees and Dividends to UUTBV, and the Restructuring of ASTV

726. As to the payment of management fees and dividends to UUTBV, Respondent argues that UUTBV recouped 83% of its investment over the first years of the privatisation, in particular by means of ongoing management fees charged to ASTV and the payment of dividends and the restructuring of ASTV's capital, referred above at paragraphs 193-195.[742]

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[740] Decision of the Supreme Court of Estonia of 12 December 2017, ¶24. It is noted that the Supreme Court then refers to the exclusion of the privatisation value as a basis for calculating justified profitability under the 2010 PWSSA: "Unlike the Circuit Court, the Chamber still admits that the new version of the PWSSA created a legal situation, in which it was not any more possible to follow the Services Agreement not only due to the change in the regulator's competence, but also due to the issue with the size of tariffs. The PWSSA's new version specifies the term justified profitability by prescribing the 'justified profitability on the capital invested by the water undertaking' to serve as a basis for the tariffs. In the Chamber's view, the amendment has made it impossible to take the privatisation value as a basis for calculating the justified profitability."

[741] Decision of the Supreme Court of Estonia of 12 December 2017, ¶23; **C-432**, Tallinn Circuit Court Decision of 26 January 2017, ¶21.

[742] Respondent's Skeleton Argument, ¶27; Resp. C-M, ¶¶132 and 133; Resp. Rej., ¶¶125-131.

727. Regarding the management fees, Respondent obliquely criticises UUTBV for having entered into a Technical Services Agreement with ASTV, pursuant to which ASTV agreed to pay UUTBV management fees in return for certain management services.[743] It is noted that Dr Hern, Respondent's economic expert, did not consider this element of Estonia's claims in view of what he considered a lack of relevant data.[744]

728. For their part, Claimants explain that UUTBV always envisaged the possibility that as part of the privatisation it might be necessary to bring into ASTV certain of its experts to stabilise and improve ASTV's operations and efficiency.[745] The 2001 Business Plan provided that ASTV would enter into two (2) agreements, one with an affiliate of United Utilities International and one with an affiliate of International Water, and detailed the fees to be paid pursuant to these agreements.[746] On 12 December 2000, Suprema requested particulars on these aspects of the Business Plan[747] and on 18 December 2000, UUTBV agreed to merge the two (2) agreements and provided the requested information on the fees to be charged.[748] These letters were later annexed to the Closing Memorandum.[749]

729. Respondent also claims that, by November 2001, UUTBV had recovered the total sum of EUR 36.5 million from its EUR 44 million investment by way of two (2) transactions: (i) the payment of dividends by ASTV for a total amount of EUR 11.6 million in 2001, which resulted in a EUR 5.9 million dividend to UUTBV[750] and which was made from an investment reserve accumulated by ASTV prior to the privatisation[751] and (ii) a reduction of ASTV's share capital of ASTV by 80%,[752] from EUR 71.3 million to EUR 12.8 million, corresponding to a EUR 30.6 million payout for UUTBV.[753]

730. Claimants do not appear to have engaged with Respondent as to the payment of dividends. As to the restructuration of ASTV's capital, Claimants submit that, as with the management fees, the 2001 Business Plan specifically envisaged this restructuring in order to optimise ASTV's capital structure and align it with those of other water undertakings. They nonetheless

[743] Resp. Rej., ¶¶122 and 123; **C-113**, Prospectus for ASTV 2005 IPO (2005), p 1885; **R-326**, Calculation of UUTBV's management fees.

[744] Resp. C-M, ¶131 and ¶132; Resp. Rej., ¶¶121-124, referring to the Explanatory Memorandum, **C-9**, Minutes of the meeting of the City of Tallinn committee for preparing and implementing the tender (20 April 2000), p 149 and to ASTV IPO Prospectus (**C-113**, pp 1973 and 1974) for the amounts of fees earned by UUTBV.

[745] Cl. Reply, ¶72, referring to **C-70**, Letter from UUTBV to Suprema (23 October 2000), p 1433.

[746] **C-20**, Shareholders' Agreement (12 January 2001), pp 404-405 and 459.

[747] **C-87**, Letter from Pritt Koit to Tim Lowe (12 December 2000).

[748] **C-89**, Letter from Tim Lowe to Pritt (18 December 2000).

[749] **C-49**, Closing Memorandum.

[750] **C-90**, ASTV Annual Report 2000, pp 1522.10 and 1522.32.

[751] Resp. C-M, ¶133.

[752] **R-178**, Minutes of the extraordinary general meeting of ASTV (1 November 2001).

[753] Resp. C-M, ¶¶132-135; Resp. Rej., ¶¶125-131.

acknowledge that, pursuant to the 2001 Business Plan, the modification of ASTV's capital was to be achieved only at the end of the first Operating Period.[754]

731. The Tribunal finds that the transactions criticized by the Respondent were, for the most part, planned before the execution of the privatisation agreements. As a result, they have no bearing on any alleged expectations of the Claimants.

b) The 2002 Amendment to the Services Agreement

732. As noted above at paragraph 196 the Services Agreement was amended in 2002 to address two (2) matters:[755] a review of the K-coefficients for the years of 2003 to 2005, and the determination of the K-coefficients for the years of 2006 to 2010; and the establishment of the MMU.

733. The Tribunal is satisfied that the 2002 Amendment was entered into at the request of the City of Tallinn, which, in the context of the rising cost of living in Estonia generally, was concerned by the impact on the City's residents of the agreed tariff increases for the 2001-2005 period laid out in the 2001 Business Plan. The City asked, and ASTV agreed, that these increases instead be spread out over a longer period, specifically, until 2010.[756]

734. The Tribunal is further satisfied that, as submitted by Claimants,[757] the common intention of the parties was not to increase the profitability of ASTV.[758]

c) The Replacement of the 2000 EBRD Loan by the 2002 EBRD Loan

735. As stated above at paragraphs 203-206 and 626-628, the 2002 EBRD Loan replaced the 2000 EBRD Loan, which was never drawn.[759] The new facility sought to finance the NEP and other investments required under the Services Agreement, to refinance the 1994 EBRD Loan, to finance the costs of the 2000 EBRD Loan as well as to restructure ASTV's balance sheet through share capital reduction. In the context of this transaction, ASTV pledged all of its material assets, present and future, and UUTBV pledged its shares.

736. Claimants submit that the 2002 EBRD Loan was beneficial to the Central Government[760] since it led to the release of the State Guarantee, as contemplated by the Information

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[754] Cl. Reply, ¶¶81 and 82, referring to **C-20**, Shareholders' Agreement (12 January 2001), pp 452-453.

[755] **C-30**, 2002 Amendment.

[756] **C-98**, Letter from City of Tallinn to ASTV and letter from ASTV to City of Tallinn of same date (10 April 2002). The new Financial Model attached to the 2002 Amendment also indicated that any changes to tariffs for the period beyond 2010 (2011-2015) would be restricted to changes to the CPI (i.e. the K-coefficient was assumed to be 0), **C-30**, 2002 Amendment (30 September 2002), p 776.

[757] Cl. Reply, ¶122.

[758] "This would slow down the growth in tariffs and spread them over a longer period," **C-98**, Letter from City of Tallinn to ASTV and letter from ASTV to City of Tallinn of same date (10 April 2002), p 1547.

[759] **C-23**, 2002 Loan Agreement between ASTV and EBRD (8 November 2002).

[760] **C-23**, 2002 Loan Agreement between ASTV and EBRD (8 November 2002), s. 5.03.

Memorandum[761] (and thereby reinforced their legitimate expectations).[762] Regarding the pledging of ASTV's assets, they underline that the 2000 EBRD Loan, which terms had been penned before UUTBV's bid, also provided for the entry into a share and retention agreement as a condition precedent for the disbursements of the funds[763] and that the 2001 Business Plan had planned a rebalancing of the capital structure of ASTV by notably increasing debt funding.[764]

737. Respondent submits for its part that the 2002 EBRD Loan led ASTV to assume a riskier facility and became necessary as a result of ASTV's share capital reduction.[765] Considering that UUTBV initiated the change in ASTV's capital structure and that it had promised to carry out the works over the 2001-2005 period, it would have been more proper, says Estonia, for UUTBV to assume the risk associated with these actions.[766]

738. As regards ASTV's capital restructuring and the 2001 dividend payment, the Tribunal has already stated its opinion that the capital reduction achieved through the 2002 EBRD Loan could not have undermined Claimants' legitimate expectations, if such expectations had been established, considering that it had been included in the 2001 Business Plan.

739. As for the impact of the 2002 EBRD Loan on the Central Government, the Tribunal merely notes that these developments are elements of context but, on the facts at hands, they bear minimal relevance for the establishing of any legitimate expectations alleged by Claimants.

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[761] Cl. Reply, ¶79, referring to **C-10**, ASTV Information Memorandum (3 July 2000), p 219.

[762] They rely on s. 5.1 of the Loan, pursuant to which ASTV undertook to carry out the works according to the Services Agreement and the "Shareholder Agreement Business Plan" (**C-23**, 2002 Loan Agreement between ASTV and EBRD (8 November 2002), s. 5.01) as well as on the letter of support issued by the City on 5 September 2002. In this letter, which was a condition precedent to the Loan disbursement, the City represented that the privatisation agreements, including the Services Agreement, constitute "valid and binding obligation of the City" (Cl. Reply, ¶108; **C-305**, City Support Letter (5 September 2002)). Prior to the issuance of the letters, the City's external advisors had also confirmed the validity of the Services Agreement (**C-302**, Legal opinion from Paul Varul to the City of Tallinn (3 July 2002)).

[763] Cl. Reply, ¶79; **C-17**, 2000 Loan Agreement between ASTV and the EBRD (31 October 2000), s. 3.02, p 295.

[764] Cl. Reply, ¶¶81 and 82; **C-20**, Shareholders' Agreement (12 January 2001), s. 8.2.2, p 77.

[765] Resp. Rej., ¶¶136-139. It acknowledges that both Loans required the pledging of ASTV's assets but stresses that ASTV's exposure was significantly less under the 2000 EUR 15.5 million Loan than the 2002 EUR 80 million facility. Respondent further disagrees that this financing strategy was anticipated at privatisation: according to the Explanatory Memorandum, the drawing of additional loans would be for the fulfilment of ASTV's investment plans. Resp. Rej., ¶137, referring to **C-9**, Minutes of the meeting of the City of Tallinn committee for preparing and implementing the tender (20 April 2000) and Explanatory Memorandum (5 March 2000), p 148.

[766] Resp. C-M, ¶142.

d) The Involvement of the EBRD as an Indirect Equity Investor from 2003 to 2010

740. As referred to above at paragraphs 207 and 208, the EBRD purchased a 25% stake in ASTV in 2003 and exited its investment in 2010.[767]

741. Claimants argue that the involvement of the EBRD constituted a further assurance as to both the legitimacy of the privatisation agreements and the fact that ASTV would follow the 2001 Business Plan.[768]

742. On this point, the Tribunal reiterates its comments regarding the impact of the involvement of the EBRD in ASTV's privatisation above and at paragraph 629. The involvement of the EBRD forms part of the relevant context and may have reinforced to some degree Claimants' understanding of the legitimacy of the privatisation agreements. It does not constitute a separate assurance giving rise to legally cognisable legitimate expectations.

e) The 2005 IPO

743. Claimants assert that the 2005 IPO reaffirmed the legitimacy of their expectations as to the privatisation agreements,[769] notably because the IPO, an initiative of the mayor of Tallinn, triggered considerable local attention. ASTV's representatives would have, in turn made presentations to international investors, with representatives of the City in attendance, on the quality of the contractual arrangements and the stability of the tariff mechanism.[770]

744. Respondent argues that the Prospectus actually demonstrates that Claimants anticipated regulatory changes for it contained disclosures of risks associated with the tariff regime and the regulatory framework[771] and implied that the 2011-2015 tariffs were not guaranteed.[772]

745. By way of rebuttal, Claimants call for a contextual reading of the Prospectus' disclosure of risks by considering the special nature of this type of legal document. To the contrary, the IPO constituted another instance where the tariff methodology of the Services Agreement was restated, thereby reinforcing their expectations as to the legitimacy of this regime.[773] They

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[767] **C-251**, Snapshot of ASTV website showing financial reports (2015).

[768] Claimants' Skeleton Argument, ¶47.

[769] Cl. Mem., ¶¶127-130; Cl. Reply, ¶273c.

[770] Gallienne 1st WS, ¶¶59-63. Claimants further submit that the stability of the contractual arrangement was reflected in analysts' reports that portrayed ASTV as a low-risk investment thanks to the tariff arrangement prevailing until 2015 (**C-116**, Carnegie report on ASTV IPO, "A Pure Water Play" (4 May 2005); **C-130**, Hansabank/Swedbank report on ASTV (6 November 2005).

[771] Resp. Rej., ¶¶149-159; Resp. C-M, ¶¶154-158.

[772] Resp. PHB, ¶112, where Respondent explains that the Prospectus not making any mention of the 2001 Business Plan. Similarly, although the Prospectus mentions that the setting of the K coefficients until 2010 provides ASTV with "a stable platform for conducting its operations until 2010," the Prospectus does not make any equivalent statement with respect to 2011-2015 tariffs, **C-113**, Prospectus for ASTV 2005 IPO (2005), pp 1944 and 1945.

[773] Claimants' Skeleton Argument, ¶48.

recognise that the Prospectus did not represent that the 2011-2015 tariffs were fixed. Yet, they claim, the Prospectus made clear that, should the City of Tallinn impose levels of services more onerous than contemplated, the associated increase in costs would be offset by a corresponding increase in the K-coefficients.[774]

746. In the Tribunal's opinion, the caveats contained in the Prospectus confirm that it was clearly understood that a change in the identity of ASTV's regulator was foreseen and that its tariffs were not entirely immune to intervention by the City acting in its regulatory capacity.

f) The 2007 Amendment

747. As mentioned above at paragraphs 221-224, in executing the 2007 Amendment, the City of Tallinn and ASTV agreed to set the K-coefficients at zero (0) for the 2011-2020 period, that is, extending beyond the term of ASTV's license in 2015.[775] This amendment has given rise to several points of contention between the Parties, including the Respondent's claim of illegality addressed above at paragraphs 717-724, the purpose of the 2007 Amendment and whether this instrument can ground any legitimate expectation. The Tribunal will review these two (2) last elements below.

(i) <u>The Purpose of the 2007 Amendment</u>

748. Claimants argue that, as with the 2002 Amendment, the 2007 Amendment was entered into at the request of the City of Tallinn, in connection with the repayment of the NEP. The parties to the Services Agreement would have agreed on K-coefficients for the period 2010-2020 to offset the financial risks associated with the extension of the repayment of the NEP and the risk of slippage in the repayment schedule.[776] As with the 2002 Amendment, the 2007 Amendment would have been intended to maintain the value under the original agreement.[777]

749. According to Respondent, Claimants' real motive in setting the K-coefficients until 2020 was to mitigate the risks arising out of a potential change of regulator, which they believed would impose a negative K-coefficient on ASTV.[778] Respondent submits that the 2007 Amendment was executed in the wake of widespread discussion of impending regulatory changes and was

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[774] **C-113**, Prospectus for ASTV 2005 IPO (2005), pp 1881 and 1923; evidence of Mr Gallienne, Tr. Day 3 Mr Gallienne 43-51. In the course of his re-direct, Mr Gallienne was brought to several excerpts of the Prospectus concerning the Services Agreement and other privatisation agreements and where the tariff mechanism contained therein, including the 15-year license period and the purpose of the K-coefficient. Mr Gallienne explained that his understanding was that increases in costs for achieving levels of services were to be offset by increase in the K-coefficient.

[775] **C-32**, 2007 Amendment.

[776] Cl. PHB, ¶¶196-198 and ¶¶201-203.

[777] **C-129**, Letter from City of Tallinn to ASTV (26 September 2007); **C-123**, Memo from ASTV to City of Tallinn (18 December 2006); Gallienne 1st WS, ¶¶80 and 84; Gallienne 2nd WS, ¶74.

[778] Estonia also refutes that the 2007 Amendment had for purpose to offset the financial costs arising out of the deferral of payments by the City of Tallinn because such costs were offset by 11% interest on the City's deferred payments, Resp. PHB, ¶159. However, Respondent does not appear to directly engage with Claimants' argument that the 2007 Amendment sought to offset the financial risks (as opposed to costs) carrying with the deferral of payment of the NEP.

specifically designed to address ASTV's concern that starting in 2010 its tariffs would be impacted by a negative K-coefficient.[779] Respondent then places particular reliance on a September 2006 strategy note authored by Roch Cheroux, who was ASTV's CEO at the time and who conducted the negotiations leading to the 2007 Amendment.[780] In this note, Mr Cheroux stated:

> Fixing the k coefficient at a positive or 0 value is the first objective because, considering the level of profitability of the company, <u>it's most probable that the 2010 price review will end up with a negative k coefficient</u>.[781] [Emphasis added]

750. Mr Gallienne, who held various positions at for ASTV from April 2002 to October 2014,[782] testified at length on these issues. His testimony supports Claimants' position regarding the rationale for the 2007 Amendment and the fixing of tariffs beyond the License Period.[783] ASTV's express and overriding objective was then to reassure the market about the stability of ASTV[784] and the 2007 Amendment would have thus further reinforced Claimants' confidence in the stability in the tariff mechanism.[785]

751. At the Hearing, Mr Gallienne referred to this setting of the K-coefficient as a "baseline agreement," which could be departed from by the regulator in certain circumstances and could not provide investment certainty.[786] He conceded that the financial models elaborated for the purposes of the 2007 Amendment did consider the consequences of a negative K-

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[779] Resp. PHB, ¶¶147-157; 168-170.

[780] Plenderleith 1st WS, ¶8; Gallienne 1st WS, ¶78.

[781] **C-327**, Email from Roch Cheroux to Ian Plenderleith and David Hetherington, Attachments: "Network Extension Financing Negotiation" and ASTV's three solutions for 2007 Amendment (21 September 2006), p 5067.

[782] Gallienne 1st WS, ¶8.

[783] According to him, the City of Tallinn approached ASTV in September 2006 with a request to spread out the repayment of the NEP works due to the increase in the construction costs. The City nonetheless wished to maintain the original schedule for the works in order to comply with the EU Urban Waste Water Treatment Directive, Gallienne 1st WS, ¶79. Moreover, The City would not even have anticipated being able to complete repayments by 2015, Gallienne 2nd WS, ¶60; see also, **C-329**, Email from Roch Cheroux to Bob Gallienne and other Attachments: "Explanation on amending the Project Agreements" and "Proposal to City" (22 December 2006).

[784] Gallienne 2nd WS, ¶84, referring to **C-329**, Email from Roch Cheroux to Bob Gallienne and other Attachments: "Explanation on amending the Project Agreements" and "Proposal to City" (22 December 2006).

[785] Gallienne 2nd WS, ¶66. Mr Gallienne further refers to investment analyst reports that would confirm same, Gallienne 1st WS, ¶¶86-88, referring to **C-136**, Unicredit report on ASTV (18 March 20080, **C-137**, Baltic Business Analysts report on ASTV (27 March 2008), **C-138**, EVLI Equity Research report on ASTV (17 July 2008) and, **C-146**, Hansabank/Swedbank report on ASTV (16 February 2009).

[786] Tr. Day 3 Mr Gallienne 20:20-23 and 67:9-68:14.

coefficient[787] and that avoiding negative K-coefficients in every year from 2011 would translate into a gain of "tens of millions."[788]

752. As for ASTV's knowledge of the forthcoming change of regulator, Respondent highlights that Mr Gallienne confirmed during the Hearing that ASTV became aware of the Chancellor of Justice's report of 2005, regarding the potential abuse of dominance in the water industry, at the time of its publication.[789] He also acknowledged that ASTV was aware of the criticism directed at ASTV's tariffs at the time.[790] It is of note, however that, at this juncture, the reforms of the Ministry of Environment focused on the failure of some municipalities to set water tariffs at a sufficiently high level to cover needed works and that the endeavours which eventually led to the creation of the AMB had not begun yet.

753. The Tribunal is content that the 2007 Amendment had not for primary purpose to mitigate the risk of a change of regulator. This does, however, affect the Tribunal's finding made above that Claimants could not have expected that their regulatory regime, including the identity of the regulator, would remain unchanged.

(ii) <u>The Impact of the Alleged Illegality of the 2007 Amendment</u>

754. As addressed above, Respondent alleges that the 2007 Amendments was unlawful in an obvious manner.[791] As a result, the 2007 Amendment could not ground any of Claimants' alleged legitimate expectations as a matter of international law. They refer to *Mamidoil v Albania*, in which the tribunal held that the investor could not claim any rights relating to the continuation of activities considered illegal under domestic law.[792]

755. By way of rebuttal, Claimants submit that Respondent is barred altogether from relying on the alleged illegality of the 2002 and 2007 Amendments pursuant to the doctrine of *estoppel*,[793] which applies here due to Estonia's involvement in these instruments.

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[787] Tr. Day 3 Mr Gallienne 79:7-24.

[788] Tr. Day 3 Mr Gallienne 2:10-33:3.

[789] Tr. Day 2 Mr Gallienne 232:25-234:20.

[790] Tr. Day 2 Mr Gallienne 237:24-238:5.

[791] Resp. Rej., ¶393.

[792] Resp. Rej., ¶¶393 and 394; **RL-237**, *Mamidoil Jetoil Greek Petroleum Products Societe Anonyme S.A. v. Republic of Albania*, ICSID Case No. ARB/11/24, Award (30 March 2015), ¶716: "Therefore, the Tribunal finds that the construction and the operation of the tank farm did not comply with Albanian law and were illegal. In the circumstances, Claimant is not entitled to rely on the perpetuation of its activities in illegal circumstances and cannot claim a violation of legitimate expectations with respect to the illegal operation of the tank farm. This finding is consistent with the Tribunal's earlier view that it has jurisdiction to hear the claims, given that Respondent had shown its willingness to consider a legalization once the respective applications were made. Absent such legalization, however, Claimant could not legitimately expect that it could continue its activities in Albania despite their illegality."

[793] Cl. Reply, ¶¶267-277.

756. Respondent challenges the application of this doctrine and, alternatively, submits that it cannot be construed as preventing the host State from exercising its regulatory power.[794] According to Respondent, Estonia has not created any reliance since it was not involved in either the creation or the approval of the 2002 and 2007 Amendments. Should estoppel nonetheless apply, it would only defeat its case as to the illegality of the 2002 and 2007 Amendments, but would not prevent Estonia from exercising its regulatory powers in respect of the amendments.[795]

757. Considering the Tribunal's findings regarding the alleged illegality of the 2007 Amendment, it is not necessary to assess whether the doctrine of estoppel finds application. That being said, and as suggested by Respondent, this issue is distinct from the question of Estonia's use of its regulatory powers.

758. It is also unnecessary to consider whether Claimants can derive any legitimate expectations from the 2007 Amendment notwithstanding that it was entered into after the investment. Indeed, since Claimants have failed to demonstrate that they had gained any legitimate expectations at the time of privatisation, the impact of the 2007 Amendment on these alleged expectations does not bear relevance. Furthermore, one can hardly conceive that the 2007 Amendment could, alone, suffice to substantiate legitimate expectations since terms of the Services Agreement that disclosed a potential change in the law and of the regulator were not amended by this instrument.

g) The 2009 Amendment and the Foregoing of a 2% K-coefficient

759. Claimants contend that the execution of the 2009 Amendment provides further confirmation of their expectation arising from the privatisation agreements. This final amendment to the Services Agreement did not affect the determination of water tariffs. It too was entered into at the request of the City,[796] specifically to *decrease* (as opposed to extend over time) the City's payments to ASTV for the NEP so as to reflect the significant decrease in construction costs in Estonia.[797]

760. In October 2009, ASTV further agreed to decrease the 2010 K-coefficient from +2 to 0 (i.e., to forego the previously agreed tariff increase for 2010),[798] specifically to take account of the impact of the ongoing recession in Estonia.[799]

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[794] Resp. Rej. ¶¶396-416.

[795] Resp. Rej., ¶416.

[796] Gallienne 2nd WS, ¶77.

[797] Gallienne 1st WS, ¶¶89 and 90.

[798] **C-153**, Letter from ASTV to City of Tallinn (28 September 2009).

[799] Plenderleith 2nd WS, ¶26. Mr Gallienne testified to the same effect, Gallienne 1st WS, ¶95 and Gallienne 2nd WS, ¶77.

h) *Conclusion regarding Claimants' Legitimate Expectations Supposedly based on Post-Privatisation Events*

761. In sum, the Tribunal finds that Claimants have failed to demonstrate that they could held any legitimate expectations based on post-privatisation events protected under the Treaty.

6) Claim of Breach of the FET Independently of the Existence of Legitimate Expectations

762. The Tribunal turns here to Claimants' claims of a breach of the FET standard that, they submit, go beyond and are separate from their legitimate expectations claim.

763. Claimants advance that Respondent breached the FET standard through a process that started in 2009. The crux of their claim lies in the rejection of the 2011 Tariff Application by the ECA on 2 May 2011 and the adoption by the ECA of the ECA Prescription on 10 October 2011 by which ASTV was ordered to re-apply for tariffs 29% lower than its 2010 tariffs. Both of these decisions were taken by the ECA on the basis of the recently- enacted 2010 PWSSA (introduced by the AMB) and its Methodology.

764. The Tribunal will first address Respondent's legal argument regarding the application of the police powers doctrine and the impact, if any, of the good faith or bad faith of Respondent's organs. It will next review the factual evidence regarding the purpose of the AMB and its the adoption, and the basis of the 2011 Tariff Application and its rejection by the ECA. The Tribunal will then assess the expert evidence regarding the legal status of the Services Agreement upon the entry into force of the AMB and regarding the adoption of the Methodology.

a) *The Relevance of the Doctrine of Police Powers and of the Good Faith of Respondent*

765. Respondent alleges that the adoption of the AMB was a *bona fide* exercise of its regulatory powers consistent with the police powers doctrine: Estonia acted in good faith and the impugned measures consist of non-discriminatory regulatory acts.[800] Respondent acknowledges that tribunals have typically applied the police powers doctrine in the context of expropriation claims but contends that the doctrine applies equally in FET cases.[801]

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[800] Resp. C-M, ¶¶400-406.

[801] Respondent relies on *Spyridon Roussalis v Romania*, where the tribunal found that the updating of food and safety regulations upon Romania's accession to the EU and the application of the new regulations to the investment at issue did not breach any legitimate expectations of the claimant. The claimant had argued that the revocation of a permit was unjustifiable and discriminatory and that Romania had failed to protect its legitimate expectations by conducting several inspections and imposing severe penalties for failure to comply with the updated regulations (it being unchallenged that the operator was not in compliance with those regulations). The tribunal found that Romania did not violate international law because the impugned actions were taken pursuant to regulations which reflected "a clear and legitimate public purpose" and explained: In the Tribunal's view, "Claimant may not have expected that the State would refrain from adopting regulations in the public interest, nor may Claimant have expected that the Romanian authorities would refrain from implementing those regulations," **RL-151**, *Spyridon Roussalis v Romania*, ICSID Case No. ARB/06/1, Award (7 December 2011), ¶691.

766. Claimants submit that the doctrine does not apply as separate, affirmative defence to FET claims. They refer to *Suez v Argentina* in which the tribunal found that it is unnecessary and inappropriate to apply the police powers doctrine to a FET claim because the police powers analysis is effectively subsumed in the FET analysis. That is, a breach of the FET standard necessarily entails a finding that the State has exceeded its reasonable right to regulate.[802] Claimants also point out that it is well-established that a breach of the FET standard does not require evidence of bad faith on the part of the State[803] and submit that, should it be established that the AMB was specifically targeted at ASTV, Respondent's burden to demonstrate that its conduct was fair and equitable would be heightened.[804]

767. The Tribunal tends to agree with Claimants – and with the approach adopted by the tribunal in Suez v Argentina. The essence of the FET standard is to assess and balance, in the circumstances and on the facts of a given case, the State's right to regulate (which entails the right to interfere to some degree with investors' rights) and the legitimate expectations of foreign investors. A finding of a violation of the FET standard necessarily entails a determination that the State exceeded its reasonable right to regulate, and to interfere with investors' rights. There is no need for a separate, "duplicative" assessment of the State's right to regulate under the police powers doctrine. Additionally, because bad faith is not essential, the absence of clear targeting of the investment in question would not necessarily preclude a violation of the FET standard. Evidence of bad faith may nonetheless indicate elements of arbitrariness in the State conduct, which should also be weighed in the analysis.

b) The Purpose of the AMB and its Adoption

768. Claimants allege that the AMB provisions concerning profitability in the Estonian water sector targeted ASTV with the objective of curtailing its profits. They do not dispute that the AMB may have embraced other objectives, including addressing what the Parties have referred to as the

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[802] Cl. Reply, ¶¶219-226, referring to **CL-104**, *Suez, Sociedad General de Aguas de Barcelona, S.A. and Interagua Servicios Integrales de Agua, S.A. v Argentine Republic*, ICSID Case No. ARB/03/17, Decision on Liability (30 July 2010), ¶148: "The police powers doctrine is a recognition that States have a reasonable right to regulate foreign investments in their territories even if such regulation affects investor property rights. In effect, the doctrine seeks to strike a balance between a State's right to regulate and the property rights of foreign investors in their territory. However, the application of the police powers doctrine as an explicit, affirmative defense to treaty claims other than for expropriation is inappropriate, because in judging those claims and applying such principles as full protection and security and fair and equitable treatment, both of which are considered in subsequent sections of this Decision, a tribunal must take account of a State's reasonable right to regulate. Thus, if a tribunal finds that a State has violated treaty standards of fair and equitable treatment and full protection and security, it must of necessity have determined that such State has exceeded its reasonable right to regulate. Consequently, for that same tribunal to make a subsequent inquiry as to whether that same State has exceeded its legitimate police powers would require that tribunal to engage in an inquiry it has already made. In short, a decision on the application of the police powers doctrine in such circumstance would be duplicative and therefore inappropriate."

[803] **RL-161**, *Técnicas Medioambientales Tecmed, S.A. v United Mexican States,* ICSID Case No. ARB(AF)/00/2, Award (29 May 2003), ¶153.

[804] Cl. PHB, ¶356. This submission is in response to one of the questions of the Tribunal put to the Parties to address in their post-hearing briefs, Letter of the Tribunal to the Parties of 24 January 2017.

"**Low Tariff Problem**," that is, the deliberate pricing of water and sewerage services below levels required to finance the necessary infrastructure works.[805]

769. According to Respondent, the AMB sought to depoliticise the determination of water tariffs and to ensure the application of fair and sustainable tariffs by introducing a central, independent regulator.[806] It notes that, in dismissing ASTV's complaint, the European Commission found that the AMB was motivated by public interest, and underlines that prior to the enactment of the AMB, various State entities and stakeholders had suggested such a transfer of authority. More specifically, it notes that, in its pre-closure letter, the European Commission stated:

> It is within a Member State's discretion to decide to change a legal regime seeking to attain justified legitimate objectives. As argued by the Estonian authorities, there was a need to change the existing regulatory regime of the water sector in Estonia in order to prevent situations of conflicts of interest (where the price setting authority is at the same time a shareholder at the undertaking) and to ensure a fair price for consumers. For that, an independent control mechanism had to be established. Moreover, the new regime ensures increased transparency and better regulation for setting tariffs for water services. Hence one could consider that the objective of the change in the regulatory regime in the water sector is justified on the grounds of public interest.
>
> […]
>
> It is true that the legał and contractual framework of the privatisation of the Company provides for certain guarantees for investors and creates certain legal expectations. However, the principle of legal expectations does not mean that restrictions on persons' rights or a cessation of benefits are impermissible as such. As it was mentioned earlier, it is at the Member State's discretion to change a legal regime if it considers that this is a proportionate way to achieve a legitimate objective.[807] [Emphasis omitted; Footnotes omitted]

770. The following review of the evidence is divided into three (3) sections: the 2005-2009 reform proposals (i), the development of the AMB (ii) and the introduction of the AMB (iii).

(i) 2005-2009 Regulatory Proposals

771. Respondent refers to the work and statements of various actors, beginning in 2005, concerning the reform of water tariff regulation. These, it says, ultimately led to proposals for the creation of a national regulator. More specifically, Respondent mentions the three (3) reform proposals referred above at paragraphs 211 and following:

[805] Cl. PHB, ¶¶286-296.

[806] Resp. PHB, ¶¶204-218 and 283-286; Resp. Rej., ¶190.

[807] **C-219**, Pre-closure letter issued by European Commission in response to ASTV's Complaint (26 September 2011), p 3584.

- The reform proposal of the Ministry of Environment;
- The reform proposal of the Chancellor of Justice;
- The reform proposal of the State Audit Office.

772. Unlike the Chancellor of Justice's proposal, which they contend was directly targeted at ASTV (their position in this regard forms part of their due process claim), Claimants contend that the Ministry of Environment and the State Audit Office initiatives aimed at redressing the Low Tariff Problem specifically, which was no longer an issue with ASTV after its privatisation. According to Claimants, the AMB as adopted contained provisions directed at ASTV unrelated to and which did not originate from the Ministry of Environment's or State Audit Office's proposals.[808]

773. Ms Kroon acknowledged during the Hearing that the focal point of the Ministry of Environment proposed reform was indeed the Low Tariff Problem, and that the State Audit Office was concerned with the same issue.[809] That being said, she also explained that the Ministry of Environment, in developing a control mechanism for tariffs, had also considered the issue of having tariffs set at a *fair* level, as appears from a 2009 draft authored by the Ministry of Environment.[810]

774. Similarly, Respondent notes that, in his 2009 Q4 report to UUTBV, Mr Plenderleith recognised that the Ministry of Environment's draft bill, just as the AMB, sought to transfer authority over water tariffs from the City to the ECA and stated that ASTV intended to work closely with the relevant institutions to influence the outcome.[811]

775. The Tribunal is satisfied that the evidence does indeed show that the Ministry of Environment intended to propose the transfer of authority over water tariffs from municipalities to a national authority, and that this fact was known to Claimants. In any event, the extent to which the Ministry of Environment and the State Audit Office may have been concerned with ASTV's tariffs does not bear significantly on the issue to be determined since, as discussed below, it is clear that the provisions of the AMB that predominantly affected ASTV were not of their initiative.

(ii) <u>The Motivation behind the AMB and the Alleged Lack of Investigation and Analysis by its Sponsors</u>

776. Claimants contend that Mr Vaher and Mr Reinsalu, the two (2) members of the Estonian Parliament who formally sponsored the AMB, acted irresponsibly by introducing the AMB in order to force a decrease in ASTV's tariffs without having duly investigated and analysed the

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[808] Cl. PHB, ¶¶287-289.

[809] Tr. Day 5 Ms. Kroon 72:11-74:15 and 77:13-25.

[810] Tr. Day 5 Ms. Kroon 76:2-77:25 and 82:10-84:5; see **RL-89**, Ministry of Environment's Draft Act Amending the PWSSA (2009), p 55 (last paragraph of the 5th section).

[811] **C-350**, ASTV 2009 Q4 update dated 2009, p 5284.

matter.[812] This, Claimants say, forms part of what they refer to as a concerted campaign against ASTV that began in 2009.[813]

777. Firstly, Claimants contend that Messrs. Vaher and Reinsalu wrongly focused on ASTV's profit margin,[814] and they attribute the EOKL's various pronouncements in this regard to Mr Vaher and Mr Reinsalu, both of whom were members of EOKL's board during the relevant period.[815]

778. According to Claimants, ASTV's profit margin is not a proper proxy for assessing their compliance with the 1999 PWSSA, as confirmed by the fact that none of the economic experts who testified in this arbitration has relied on this metric. Claimants contend that the EOKL's and Messrs. Vaher's and Reinsalu's statements were further misleading since they were restricted to yearly profit margins or tariff increases in certain years which did not reflect the overall economic framework of the privatisation.[816]

779. In response, Estonia reminds the Tribunal that other stakeholders had made statements critical of ASTV, and that the EOKL itself had taken a position on the issue,[817] before Mr Vaher joined the EOKL board in 2009.[818] According to Mr Vaher, the EOKL would have started to look into Tallinn's water tariff in 2008.[819] It published a first article critical of ASTV on 1 August 2008 and, in a January 2009 press release it expressly called for the reduction of ASTV's tariffs.[820] Other public statements by the EOKL followed in May 2009, September 2009 and October 2009.[821] Mr Vaher also disputes that he and Mr Reinsalu had any decisive influence over the

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812 Cl. PHB, ¶¶302-305, ¶¶310-316.

813 Cl. Mem., ¶152; Cl. PHB, ¶217.

814 Cl. PHB, ¶¶302-305.

815 Cl. PHB, ¶¶298-301.

816 Cl. PHB, ¶¶303 and 304.

817 Resp. PHB, ¶¶183-187; **R-156**, Article by Martin Mutov "Tallinn Vesi gilds its shareholders" published in the online version of Postimees (24 May 2006); **R-113**, Article "SDE: the city government has let Tallinna Vesi to walk them over" (26 September 2007); **R-238**, Article by the EOKL "The mechanism of price increase in the City of Tallinn is inappropriate" published on Estonian Homeowners' Association website (1 August 2008); **R-114**, Article "People's Union of Estonia: the city must change the treaty with AS Tallinna Vesi" (1 August 2008); **R-120**, Article by the EOKL "Homeowners Association's roundtable for water price regulation: the transfer of monopolies under the control of the Competition Authority" (26 January 2009); **R-112**, Article "Robber barons in Tallinn water business: more than half the water price goes to business profit" (2 April 2009); **R-195**, "The Capital: Privatization of ASTV was fumbling," Õhtuleht (17 August 2009); **C-349**, Article from Äripäev, "Competition Authority, please come and help!" (27 October 2009).

818 Mr Vaher testified that he first joined the board of the EOKL in April 2009, Vaher 2nd WS, ¶¶6 and 7.

819 Vaher 1st WS, ¶21.

820 **C-143**, MTÜ Eesti Omanike Keskliit press release, "330 million profit from 400 [thousand] people" (23 January 2009). See also **R-120**, Article by the EOKL "Homeowners Association's roundtable for water price regulation: the transfer of monopolies under the control of the Competition Authority" (26 January 2009).

821 **C-145**, Press article, "Owners' Union is planning to take the dispute over water tariff to the court" (15 May 2009); **C-152**, Press article, "Homeowners' Association: Tallinna Vesi should reduce its tariffs by at least 20%" (28 September 2009) and **C-155**, Press article, "State is willing to take monopolies in hand" (13 October 2009).

EOKL considering that the EOKL board comprises fifteen (15) members who decide by majority and that it is supervised by a 25-member council.[822]

780. Second, Claimants also claim that the fact that Messrs. Vaher and Reinsalu decided to introduce the AMB in April 2009 demonstrates that they acted on an ill-informed basis.[823]

781. Mr Vaher in fact confirmed that he and Mr Reinsalu took the decision to introduce the AMB before the release of the ECA Analysis of ASTV's tariffs in November 2009. According to Mr Vaher, he and Mr Reinsalu nonetheless gathered information from multiple sources, including the ECA, the Chancellor of Justice, the EOKL and the media.[824]

782. Claimants submit that none of these sources could have actually informed their decision to go forward with the introduction of the AMB. Reference to the works of the Chancellor of Justice would be irrelevant considering that the latter first took interest in ASTV in June 2009.[825] Nor could Messrs. Reinsalu and Vaher's purported consultation with the EOKL be germane due to their involvement in the organisation. Similarly, any reference to the media would be misplaced because most of the media coverage in fact resulted from the EOKL's activity.[826]

783. As far as the contacts between the ECA and Messrs. Vaher and Reinsalu are concerned, it is established that they met in June 2009 and that Mr Ots shared with them the ECA's preliminary findings regarding ASTV's tariffs. This included the ECA's estimate that ASTV's profitability was 19.6%, the figure that Mr Vaher and Mr Reinsalu would later include in the AMB Letter that was in turn appended to the AMB draft as introduced in Parliament in October 2009.[827] The Tribunal notes that, according to Claimants, it was inappropriate for Mr Ots to share this preliminary information with Messrs. Vaher and Reinsalu, including because the ECA ultimately concluded that ASTV's profitability was of 18.1% and that its so-called investigation was deficient and lacked due process.[828]

784. Third, Mr Vaher confirms that he and Mr Reinsalu did not consult with either ASTV or the City of Tallinn.[829] Mr Vaher testified that he became aware of the existence of the Services

[822] Vaher 2nd WS, ¶9.

[823] Cl. PHB, ¶305.

[824] Tr. Day 5 Mr Vaher 24:10-14.

[825] Teder WS, ¶6; **R-130**, Letter of the Harju County Governor to the Chancellor of Justice (17 June 2009).

[826] Cl. PHB, ¶¶313 and 314.

[827] Cl. PHB, ¶¶307-309; Vaher 1st WS, ¶36; **C-39**, AMB Letter, p 908: "Poor protection of consumers' rights and not following the competition law has in more conspicuous cases led to a situation in which for example the productivity of the assets invested of the leading water undertaking of Tallinn is 19.6%. Taking as the basis the general European practice regarding the justified rate of profit of the water undertaking (7-8%), if the draft bill applies the price of water for the end consumer of Tallinna Vesi alone should reduce by ca 24% next year."

[828] Cl. PHB, ¶¶307-309.

[829] Tr. Day 5 Mr Vaher 24:7-22. Claimants also refer Mr Vaher's testimony where he explained that he inferred from the fact that the City of Tallinn's passivity that it was "more interest in dividends" than other cities based, Cl. PHB, ¶315, referring to Tr. Day 5 Mr Vaher 53:3-15.

Agreement through the media and that he had no knowledge of its 15-year term or its tariff mechanism.[830] He explained that, considering that the AMB's primary objective lay in the centralisation of authority over the regulation of tariffs (as opposed to the principles for determining tariffs), it was simply not necessary to consider the impact of the AMB's on the arrangements in force.[831]

785. Simply put, the Tribunal does not consider it necessary to engage in an analysis of or in any way to rule on the conduct and motives of the AMB's sponsors for the purpose of deciding Claimant's claim for breach of their legitimate expectations. It is obvious from the evidence that Messrs. Vaher and Reinsalu and the EOKL dedicated significant effort to attracting the public's and the Central Government's attention to what they considered to be ASTV's excessive tariffs and profitability; and that this effort was successful and likely played a role in the initiation and drafting of the AMB. However, this alleged "targeting" of ASTV by the persons in question, even if it were found to be such, cannot in itself be considered wrongful, still less as constituting internationally wrongful conduct of the Estonian State. The proper focus is rather the precise basis on which the Estonian authorities ordered the decrease of ASTV's tariffs.

(iii) The Introduction of the AMB in October 2009

786. As discussed above at paragraphs 257 and following, the draft AMB was introduced in the Estonian Parliament on 15 October 2009.

787. Claimants posit that the purpose of AMB, from its introduction to its adoption and entry into force, was to lower ASTV's tariffs. They rely on the fact that the AMB Letter accompanying and explaining the draft bill expressly refers to ASTV and the need to lower its tariff by 24%. They also rely on the absence of any mention in the bill of the politicisation of water tariffs, the alleged purpose of the AMB;[832] and indeed none of the provisions of the October 2009 AMB expressly address the Low Tariff Problem.[833] Claimants similarly note that, when the Ministry of Environment notified the authors of the AMB of the Ministry's own draft bill in October 2009, it stated that the most important difference between the two (2) drafts was the section of the draft AMB imposing a cap on justified profitability.[834]

788. Respondent challenges this interpretation by arguing first that the AMB sought to address the nation-wide problem of the failure by municipal water regulators to implement the 1999

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[830] Tr. Day 5 Mr Vaher 7:13-23, 8:5-7 and 24:19-22.

[831] Tr. Day 5 Mr Vaher 57:17-58:9.

[832] See footnote 827 above. ASTV was also the only water undertaking mentioned in the second AMB explanatory letter presented for its first reading in March 2010, **R-196**, Explanatory memorandum to the amended text of the AMB submitted for the first reading (5 March 2010), p 9.

[833] **C-417**, Documents related to the drafting of the Anti-Monopoly Bill (6 October 6, 2009 – 12 November 2009), pp 7704-7706.

[834] **C-417**, Documents related to the drafting of the Anti-Monopoly Bill (6 October 2009 – 12 November 2009), p 7782.

PWSSA properly.[835] According to Mr Vaher, the AMB sought both to protect consumers and to redress the failure of local authorities to set proper tariffs. Mr Vaher further emphasised that the fundamental purpose of the AMB was to ensure compliance with the principles already in existence, not to introduce new principles, governing the actual setting of tariffs.[836]

789. Respondent also asserts, based on Mr Vaher's evidence that the purpose of the AMB was not to interfere with the contractual arrangements between the City of Tallinn and ASTV.[837] It is noted that Mr Vaher nonetheless conceded that ASTV was in his view the prime example of a water utility charging excessive tariffs.[838]

790. As above, the Tribunal does not consider that the early history and evolution of the draft AMB discloses conduct by the State that can be considered wrongful in itself. That history does, however, confirm that at least one focus of the draft AMB at the time was the profitability of ASTV.

(iv) The Parliamentary Works after the Introduction of the Draft AMB, and the Introduction of the Phrase "*of the capital invested by the water undertaking*"

791. The evidence pertaining to the elaboration of the AMB with arguably the most direct potential bearing on Claimants' claims are the exchanges between the ECA and the sponsors of the AMB.

792. Claimants focus particularly on the inclusion in the bill, between its introduction in October 2009 and its adoption by Parliament, of the key phrase "of the capital invested by the water undertaking" to qualify the concept of "justified profitability."[839] According to Claimants, the AMB Explanatory Letter having committed to a 24% decrease in ASTV's tariffs, the draft bill was amended specifically to achieve this purpose.[840]

793. On the face of the proposal to amend the draft, this modification was aimed at clarifying that non-refundable aid would not be included in the asset base to be used for calculating justified profitability.[841] According to Mr Vaher, "the exact method for the calculation of the regulated asset base for the purpose of determining 'justified profitability' was neither the reason for this amendment nor was this ever discussed in connection with the ECA's proposal."[842] But this does not seem to be the case.

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835 Resp. Rej., ¶190.

836 Vaher 1st WS, ¶34.

837 Tr. Day 5 Mr Vaher 57-58.

838 Tr. Day 5 Mr Vaher 30:20-34:22.

839 **RL-87**, AMB, s. 2(8), amending s. 14 (2)5) of the 1999 PWSSA.

840 Cl. PHB, ¶355.

841 **R-124**, Amendment proposals to the AMB by the ECA (22 March 2010).

842 Vaher 1st WS, ¶44; Vaher 2nd WS, ¶13.

794. Claimants argue forcefully that this amendment was targeted directly at ASTV. They refer to an email from Mr Ots to Messrs. Vaher and Reinsalu of April 2010, in which Mr Ots commented on the introduction of this new wording:

> The way to solve the problem that was raised yesterday (how to avoid a monopoly pumping up the value of its assets) is by supporting the proposals made by the Competition Authority (which are included in our official letter):
>
> PWSSA §14 (2) (5): justified profitability of the capital invested by the water undertaking.
>
> PWSSA §141 (3) The justified profitability rate forecasted by the water undertaking may not exceed 10 per cent of the capital invested by the water undertaking, on the basis of the weighted average cost of capital.
>
> Our correction is marked in red. These corrections are underlining that the calculation of profitability is made by applying the capital invested by the undertaking, i.e. the company, eliminating the possibility of applying the capital invested by the shareholders *via* stock exchange, instead.[843]
> [Red font in the original; underlining added]

795. Mr Ots confirmed at the Hearing that by "the company" he was in fact referring specifically to ASTV in this exchange.[844]

796. Claimants draw further support from the fact that, in its March 2010 comments on the November 2009 ECA Analysis, ASTV very clearly stated that the ECA mistakenly failed to make any allowance for the capital invested during the privatisation.[845] Moreover, they say, the ECA set out to align the conclusions of the Analysis with the stated goal of the AMB's sponsors – to achieve a 24% reduction of ASTV's tariffs – by itself concluding that ASTV should reduce its tariff by an even greater amount of 25%.[846]

797. Both Mr Ots and Mr Vaher testified at the Hearing that the inclusion of the phrase "of the capital invested *by the water undertaking*" had as its objective to exclude from the determination of justified profitability any non-refundable aid granted by the European Union.

798. Yet, when questioned on the impact that this change would have on ASTV, Mr Vaher conceded that ASTV was in fact the only Estonian water undertaking listed on a stock exchange:

> THE PRESIDENT: I am asking you a different question, which is whether you knew or you were aware that that change of wording would affect ASTV, the effect of this law would be to have an impact on ASTV?

[843] **C-419**, Consultations relating to draft AMB (5 March 2010 – 2 August 2010), p 7915.

[844] Tr. Day 4 Mr Ots 97-100.

[845] **C-165**, Letter from ASTV to the ECA (1 February 2010), p 2815.

[846] Cl. PHB, ¶355.

> A. As I said also that this wording would clarify the main principle of justified profitability which was already in the law, so the answer is that if there would be any confusion of justified profitability, then this wording
> would clarify in a much better fashion any confusion about the justified profitability in the future, and in that sense you can say that it would affect any utility which the ECA would then scrutinise or start controlling.
> THE PRESIDENT: I understand that, thank you. Did you consider that ASTV had been pumping up the value of its assets at the time?
> A. No, we didn't.
> THE PRESIDENT: Were ASTV's shares listed on the stock exchange?
> A. Yes.
> THE PRESIDENT: Were other Estonian water undertakings listed on the stock exchange at the time?
> A. No.[847]

799. Respondent argues that the new wording would not have changed Claimants' position because the 1999 PWSSA already excluded the use of the privatisation value for the calculation of the RAB: since the 1999 PWSSA refers to justified profitability of the "water undertaking," and not of its shareholders', the share price paid by the buyer is irrelevant to the calculation in any event.[848]

800. Claimants reply that Respondent's position is disingenuous in the extreme given that, in the course of preparing for the European Commission proceedings, Estonia's representatives themselves implied that the two (2) texts had different meanings.[849]

801. In the light of this evidence, the Tribunal is persuaded that the phrase "capital invested *by the water undertaking*" sought to exclude privatisation value from the calculation of tariffs. Although this might not have been the sole purpose of this amendment to the draft AMB, the evidence nonetheless indicates that this was an important reason for the amendment, and was directed specifically at ASTV. As to Respondent's argument that such modification did not alter the state of Estonian law, the Tribunal rejects that proposition and agrees in this respect with the Estonian Supreme Court.[850]

802. That being said, the Tribunal does not find that this legislative change is indicative of a breach of the FET standard. This modification to the PWSSA falls within the scope of the changes that an investor should have foreseen, especially when considering the clauses of the Services Agreement disclosing potential change in the law. It cannot either be sustained that the fact that some aspects of the AMB were directed to ASTV means that its adoption necessarily

[847] Tr. Day 5 Mr Vaher 56:18-57:15.

[848] Resp. C-M, ¶¶218 and 219; Resp. Rej., ¶203; Resp. PHB, ¶¶213 and 214. See also Messrs. Ots and Vaher's testimony at the Hearing, Tr. Day 4 Mr Ots, 97-100 and Tr. Day 5 Mr Vaher 48-50.

[849] Cl. PHB, ¶360, referring to **C-419**, Consultations relating to draft AMB (5 March 2010 – 2 August 2010), p 8000 and **C-428**, Letter of the Permanent Representation of Estonia to the EU etc. (24 August 2012), p 8182.

[850] **C-432**, Tallinn Circuit Court Decision of 26 January 2017, ¶¶22 and 26.

amounts to a breach to international law. In this respect, even if not directly pertinent to the FET standard, the Tribunal is mindful that at least one international tribunal has concluded that the curtailing of perceived luxury profits constitutes a proper policy motivation.[851] What is more, it is fair to understand, upon review of the evidence, a concern with ASTV in particular was legitimate considering its especially significant position among water utilities in Estonia.

c) The Basis of the 2011 Application and Its Rejection

803. On 2 May 2011, the ECA dismissed the 2011 Application. Respondent acknowledges that the principal ground for the ECA's decision was the assimilation of ASTV's RAB to the privatisation value.[852] Nor is it disputed that in reaching this decision the ECA did not consider the privatisation agreements.[853]

804. Respondent submits that the ECA's decision was correct because ASTV's 2011 Application lacked a clear legal basis (i) and was economically flawed (ii). It is Respondent's case that, because Claimants' claim rests entirely on the 2011 Application, should the Tribunal find that the ECA was justified in rejecting the Application, Claimants' case falls.[854]

(i) The Alleged Lack of Clear Legal Basis of the 2011 Tariff Application

805. Respondent first alleges that the 2011 Tariff Application lacks a clear legal basis as it is impossible to ascertain from the Application whether ASTV asks the ECA to enforce the K-coefficients set in the 2007 Amendment (at a zero value), to conduct a price review pursuant to Schedule E, Part I of the Services Agreement, and/or to apply the so-called Ofwat methodology laid out in the "Tariff Application 2011-2015" section of the Application.

806. Estonia acknowledges that the 2011 Tariff Application refers several times to the Services Agreement, but it submits that these are intended only to refer to ASTV's past performance, as illustrated by the fact that the "Tariff Application 2011-2015" section does not engage in an application of the privatisation agreements.[855]

807. Claimants counter that Respondent misconstrues the 2011 Tariff Application. The Application not only refers to the Services Agreement but specifies that it is "made on the basis of the Services Agreement" and clearly seeks to preserve the tariff structure of the Services Agreement as amended. They explain that the economic analysis enclosed with the

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[851] **RL-154**, *AES v Hungary*, *supra* note 487, ¶10.3.34

[852] Resp. Rej., ¶206; Resp. C-M, ¶231, Ots 1st WS, ¶¶107-110.

[853] In its letter informing ASTV of the rejection of the 2011 Tariff Application, the ECA stated that it was not possible to consider the agreements executed with the City of Tallinn, **R-173**, Letter from the ECA to ASTV (28 February 2011), p 43 of the pdf.

[854] Resp. PHB, ¶¶233-247.

[855] **C-187**, Letter from ASTV to ECA, enclosure: 2011 Tariff Application (9 November 2010), pp 3060-3063, 3092-3093, 3094-3106.

Application was intended only as a "cross-check" of the consequences of applying that tariff structure.[856]

808. The Tribunal considers that the 2011 Tariff Application and related evidence shows that ASTV clearly specified to the ECA that it considered itself entitled to submit tariffs for 2011 and the following four years pursuant to its existing contractual arrangement with the City of Tallinn:

> Under the terms and conditions of our Services Agreement with the City of Tallinn signed in 2001 ASTV has a contractual right to a tariff change from 1 January 2011. In order to ensure compliance with this Services Agreement, we are making our tariff application for 2011 and the following four years.[857]

809. The body of the 2011 Tariff Application indeed contains significant references to the Services Agreement, including statements to the effect that ASTV applies for lower tariffs than those that could be enforced under the Services Agreement. A close reading of the evidence, however, suggests that ASTV used the Services Agreement as a point of reference not only with regards to its tariffs but as well, if not principally, its Levels of Services:

> This tariff application is made on the basis of the Services Agreement supplemented by any improvements that the company has delivered over the period since privatisation. A selection of the key performance indicators taken from the Services Agreement and custom and practice are detailed in the table below. This tariff application is based upon the continued consistent achievement of these standards throughout the five year period with no detriment to our customers.[858]

810. With regards to the financial calculation of tariffs, ASTV explains that the Tariff Application relies on a "building block" model inspired by the Ofwat methodology:

> **This financial and economic tariff application is made by using many of the factors contained in the building block approach that is used by Ofwat, the regulator for water and sewerage services in England and Wales.** We feel this methodology is the most appropriate as it is the oldest regulatory model for the water sector in the world which has been continually refined and improved over the last 20 years, and is recognised as the world leading water regulatory regime. Moreover this regime which regulates privatised water companies, similar to ASTV, is clearly recognised as by [sic] the Competition Authority (CA) as exemplifying best practice as it has been continually referenced by the CA in their comments and analysis of ASTV.[859] [Emphasis in original]

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[856] Cl. PHB, ¶¶374-377.

[857] **C-187**, Letter from ASTV to the ECA, enclosure: 2011 Tariff Application (9 November 2010), p 3060.

[858] **C-187**, Letter from ASTV to the ECA, enclosure: 2011 Tariff Application (9 November 2010), p 3095.

[859] **C-187**, Letter from ASTV to the ECA, enclosure: 2011 Tariff Application (9 November 2010), p 3095.

811. Although the 2011 Tariff Application does clearly refer to the methodology set out in the Services Agreement,[860] it nonetheless seems that for the purpose of establishing its 2011-2015 tariffs ASTV chose to rely principally, not on the Services Agreement, but on the Ofwat principles.

(ii) The Alleged Economic Flaws of the 2011 Tariff Application

812. Independently of the foregoing, Respondent submits that the ECA was correct in rejecting the 2011 Tariff Application for the following reasons:[861]

813. First, the 2011 Tariff Application equated ASTV's RAB with the privatisation value, which was prohibited under the 2010 PWSSA.

814. Second, the Application was premised on a miscalculation of ASTV's RAB by double-counting the amount invested in ASTV at the time of the privatisation. In fact Mr Meaney admitted that the Application mistakenly overstated ASTV's RAB by EUR 80 million on this basis;[862] for his part Dr Hern considers the error to be equivalent to EUR 98 million.[863]

815. Third, the 2011 Tariff Application sough an increase for a period of five (5) consecutive years, which was inconsistent with the 1999 PWSSA, the 2010 PWSSA and the Methodology.

816. Fourth, the 2011 Tariff Application suffered from other deficiencies, such as the inclusions of pollution charges paid by ASTV for breaches to the environmental regulation and the cost of bad debts, as also noted by the Supreme Court of Estonia.[864]

817. These arguments will be assessed when reviewing the economic expert evidence filed by the Parties. Before doing so the Tribunal will address the important question of the impact of the entry into force of the 2010 PWSSA on the privatisation agreements.

d) The Legal Impact of the Entry into Force of the AMB/2010 PWSSA on the Lawfulness and Enforceability of the Tariff part of the Services Agreement

818. The entry into force of the 2010 PWSSA, which was introduced into Estonian law by the adoption of the AMB, raises, first, the issue of the status of the Services Agreement under Estonian law, and second, the question whether the ECA correctly exercised its discretion in adopting the Methodology.

(i) The Status of the Services Agreement after the Entry into Force of the AMB

[860] **C-187**, Letter from ASTV to the ECA, enclosure: 2011 Tariff Application (9 November 2010), p 3094.

[861] Resp. PHB, ¶¶242-247.

[862] Meaney 2nd ER, ¶4.19 (footnote 77).

[863] Hern 2nd ER, ¶217.

[864] Respondent notes that, in its decision, the District Court of Tallinn underscored the lack of explanation by ASTV in these regards, **C-432**, Tallinn Circuit Court decision (26 January 2017), ¶27.

819. Respondent argues that the ECA was not bound by the Services Agreement.[865] Claimants disagree. They allege that with the entry into force of the AMB the ECA succeeded to the City of Tallinn as a party to the Services Agreement; alternatively, the Services Agreement was binding on the ECA as a public law contract entered into *in lieu* of an administrative act.[866]

- *Did the ECA succeed to the City of Tallinn as a Party to the Services Agreement?*

820. Mr Rask, Respondent's expert on Estonian law, opines that the ECA could not have succeeded to the City of Tallinn because the two (2) authorities played different roles: the responsibility of the City was to *set* water tariffs; the responsibility of the ECA was to *approve* (or not) these tariffs.[867] Mr Rask also submits that legal succession only operates where the law clearly provides for it, which the AMB does not. He states that the AMB prescribes neither the legal succession of the ECA, nor any obligation for the ECA to abide by earlier agreements or relationships.[868] He further notes that the Supreme Court of Estonia has held that the civil law rule of legal succession does not operate in case of transfer of administrative functions, such as between the City and the ECA, which among other things means that it is inappropriate to rely on civil law principles to address the AMB's silence in respect of succession.[869]

821. According to Mr Pikamäe, the question of legal succession and the transfer of responsibility for the Services Agreement from the City to the ECA depends on whether the new authority is in fact assigned functions within the competence of the previous authority – the absence of statutory provisions explicitly providing for succession is not determinative.[870] In Mr Pikamäe's opinion, the ECA succeeded to the City of Tallinn as a party to the Services Agreement given that, by virtue of the AMB, it assumed the responsibilities of the City, and thus replaced the City, for all matters concerning the setting of ASTV's water tariffs and related supervision.[871] He acknowledges that under the 1999 PWSSA, and as explicitly agreed in Section E and clause 7 of the Services Agreement, the City "sets" ASTV's tariffs, whereas under the AMB and the 2010 PWSSA the ECA "approves" or refuses to approve tariffs proposed by ASTV. According to Mr Pikamäe, the simple fact is that with the entry into force of the AMB all authority with respect to the level and supervision of ASTV's tariffs under the Services Agreement was transferred from the City to the ECA. Mr Pikamäe acknowledges that no Estonian decision confirms this approach.[872]

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[865] Resp. C-M, ¶221.

[866] Cl. Reply, ¶382a, referring to **R-196**, Explanatory memorandum to the amended text of the AMB submitted for the first reading (5 March 2010).

[867] Rask 1st ER, ¶¶147-151.

[868] Rask 1st ER, ¶¶147-149. He specifically refers to Art. 16(6) of the AMB, **RL-87**, AMB.

[869] Rask 1st ER, ¶150, referring to **RL-69**, Supreme Court's judgement in administrative case No. 3-3-1-5-11 (21 September 2011).

[870] Pikamäe 1st ER, ¶¶73 and 74.

[871] This would include Clauses 7, 8(1)(b)(iii), 2 and 9 as well as Schedule E of the Services Agreement, **C-22**, Services Agreement (including schedules) (12 January 2001); Pikamäe 1st ER, ¶6.22.

[872] Pikamäe 1st ER, ¶¶227-230.

822. The absence of legal succession as between the City of Tallinn and the ECA was confirmed by the 12 October 2015 decision of the Tallinn Administrative Court.[873] On appeal, the Supreme Court maintained this conclusion and explained that the ECA could not have legally succeeded to the City of Tallinn because the 2010 PWSSA did not grant the ECA the power to enter into such an agreement and because the new law changed the duties of the regulator:

> In order for the CA to be the legal successor of the City of Tallinn with regard to the performance of the tariffs part of the services agreement, the CA should have the right, under the currently applicable law, to enter into a contract of similar content. The Chamber is of the opinion that the PWSSA does not grant such rights, the duties of the regulator have significantly changed compared to the earlier version of the PWSSA. If the earlier version of the PWSSA § 14 (2) prescribed for the establishing of the tariff regulation procedure to fall within the competence of the local government council and the establishing of water tariffs to fall within the competence of the city- or rural municipality government, then the PWSSA § 14 (9) effective since 1.11.2010 grants the CA only the competence to develop the recommended principles for calculating the water tariffs and § 141 (1) grants the competence to determine the water tariff to the water undertaking itself, and leaves the CA as the regulator only with the competence to approve the tariffs (PWSSA § 142 (1)). If earlier the local government authority had the competence to determine in a legally binding manner the tariff regulation procedure and the other local government authority had the competence to unilaterally establish the water tariffs, then in the new legal situation, the CA's guidelines for calculating the water tariffs are solely of recommendatory nature, and usually the CA does not determine the price itself, but can only approve or not approve the price applied for by the water undertaking. The situation is not changed by the CA's right to establish temporary water tariffs in exceptional circumstances (PWSSA § 16 (9)), because the services agreement regulates a general case. Moreover, the agreement also contained numerous other provisions besides the tariffs, incl. for instance the city compensating for certain costs to the water undertaking, which clearly cannot be deemed as something transferred to the CA. Neither does it constitute the situation specified in the APA § 9 (3).[874]

823. The Tribunal is not minded to disagree with the Supreme Court, and does not consider that it has any basis to do so in any event. The Tribunal in fact views the matter similarly. Considering all of the evidence, authorities and legal opinions before it – especially as concerns the transformation of the role and responsibility of the regulator under the new law and the consequent change in the relationship between regulator and regulated undertakings – the Tribunal agrees with Respondent that the ECA did not legally succeed to the City of Tallinn as a party to the Services Agreement.

[873] **RL-167**, Tallinn Administrative Court Decision of 12 October 2015.

[874] Supreme Court Decision (12 December 2017), ¶20.1.

- *Was the ECA bound by the tariff part of the Services Agreement on the basis that it was a public law contract entered into* in lieu *of an administrative act?*

824. Claimants submit, on the basis of Mr Pikamäe's expert evidence, that even if the ECA did not legally succeed to the City of Tallinn, the ECA was nonetheless obliged to respect the Services Agreement on the basis that it is a public law contract entered into by the City *in lieu* of an administrative act pursuant to Art. 98 of the Estonian *Administrative Procedure Act* ("**APA**") and, as such, binding on all administrative authorities and courts pursuant to Art. 60(2) APA.[875]

825. Mr Rask, on the other hand, considers that the Services Agreement cannot be considered as a valid public contract given that it was entered into by the Tallinn City government without the Tallinn City Council having formally adopted the Agreement's tariff-setting mechanism beforehand, as required by the 1999 PWSSA.

826. Mr Rask further opines that, even if the Services Agreement fell within the ambit of Art. 98 APA as suggested by Mr Pikamäe, it would still not be governed by public law. As a matter of Estonian law, he says, public law contracts are governed by civil law in all respects save as regards their lawfulness.[876] The binding effect of public law contracts are not governed by Art. 60(2) APA but by Art. 8 of the Law of Obligations Act ("**LOA**"), which lays down the principle of privity of contract in civil law.[877] He also suggests that Mr Pikamäe errs by extending the binding effect of administrative act to the courts: in fact, both a public law contract and an administrative act may be annulled by an administrative court, though not by a civil court.[878] Lastly, Mr Rask opines that the price formation agreement contained in the Services Agreement related agreements could not bind third parties for their failure to comply with publicity requirements.[879]

827. In its December 2017 decision, the Supreme Court agreed with ASTV that the Services Agreement constituted a public law contract that had been entered into *in lieu* of an administrative act. It specified that the Services Agreement possessed the characteristics of a preliminary administrative act aimed at regulating an individual case.[880] However, it dismissed ASTV's Art. 60(2) APA argument and refused to consider the Services Agreement as "mandatory for everyone":

> In addition to the above, the complainant has stated that even if the ECA cannot be regarded as the legal successor of the City of Tallinn with regard to the performance of the Services Agreement, the Services Agreement is still binding on the ECA, because the resolution contained in an administrative act is mandatory for everyone (APA § 60 (2)). <u>The Chamber disagrees with that position. As stated in the</u>

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[875] Resp. Reply, ¶382b; Pikamäe 1st ER, ¶231, ¶¶56-65

[876] Pikamäe 1st ER, ¶33, referring to **RL-54**, Estonian Administrative Procedure Act (6 June 2001), s.105(1).

[877] Rask 2nd ER, ¶36.

[878] Rask 2nd ER, ¶37.

[879] Rask 2nd ER, ¶¶41 and 42.

[880] Supreme Court Decision (12 December 2017), ¶¶17, 17.3 and 18.

clause 17.3 of this decision, the tariffs part of the Services Agreement basically has the characteristics of a preliminary administrative act. This sets the terms and conditions only on the Tallinn City Government's decisions to establish prices for particular years. The tariff criteria stipulated in the contract have no effect beyond those decisions.[881] [Emphasis added]

828. The Tribunal is not persuaded otherwise, and considers it appropriate to defer to the Supreme Court of Estonia courts on this point of Estonian administrative law. Having considered the Parties' submissions, the Tribunal is satisfied that the Services Agreement could not have bound the ECA as regulator.

- *The Legality and Enforceability of the Services Agreement after the Entry into Force of the 2010 PWSSA*

829. The Parties concede that, upon the transfer of responsibility over tariffs from the City to the ECA, the status of the Services Agreement under Estonian law became unclear.[882]

830. The Tallinn District Court has found that the Services Agreement could be performed at least until the entry into force of the 2010 PWSSA.[883] The District Court found that ASTV could not demand performance of the Services Agreement from the ECA and that, by rejecting the 2011 Tariff Application, the ECA effectively terminated the Services Agreement.[884]

831. Respondent argues that, if interpreted literally, the 2007 Amendment would also have been null and void because Art. 14 PWSSA forbids the fixing of a tariff over a 13-year period without reviewing the undertaking's costs.[885] It relies on Mr Rask's opinion that, although it was "debatable" whether the nullity of Services Agreement was "obvious," the nullity of the 2007 Amendment (and of the 2002 Amendment) "appears […] closer to being obvious."[886] Mr Rask in turn relies partly on the opinion of Dr Hern, according to whom setting tariffs over a 13-year period is unprecedented.[887]

832. Claimants submit that the Tallinn District Court erred in finding that the ECA was not bound to comply with the terms of the Services Agreement. First, they note that the District Court did not assess the compliance of the tariff part of the Services Agreement with the 2010 PWSSA, but rather engaged in a comparison between the mechanisms required by the Services

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[881] Supreme Court Decision (12 December 2017), ¶21.

[882] Resp. PHB, ¶355; Cl. PHB, ¶¶393a and 416.

[883] **C-432**, Tallinn Circuit Court decision of 26 January 2017, ¶19.

[884] **C-432**, Tallinn Circuit Court decision of 26 January 2017, ¶20.

[885] Resp. PHB, ¶¶355 and 357-359; Resp. Rej., ¶¶171-174 and 363-368.

[886] Rask 1st ER, ¶18.

[887] Rask 2nd ER, ¶¶92-94 and 97.

Agreement and by the Methodology.[888] According to Claimants, the ECA should have attached greater significance to the methodology used by the City of Tallinn:

> However, the reason why the ECA should have attached greater significance to the methodology used by the City of Tallinn with respect to ASTV was that it was enshrined in a fixed term contract, entered into as a result of a model, EBRD-sponsored privatisation, in reliance on which UUTBV was encouraged to invest substantial sums and expertise into ASTV. It is not appropriate, and is a breach of the BIT, for Estonia, through its courts, to conclude that in order to be consistent with regulation in other sectors that contract – and the sums invested by UUTBV – should simply be ignored. There are a number of other options the ECA could have adopted to implement its methodology while respecting the ASTV's contract until the end of its term […].[889]

833. Claimants further submit that the District Court was wrong to conclude that the Services Agreement need not be taken into account by the ECA on the ground that it was incompatible with the Methodology, because the ECA's discretion to develop the Methodology cannot override its obligation to consider the Services Agreement.[890]

834. Second, according to Claimants, the District Court failed to apply the principle of Estonian law that a public law agreement remains valid and binding, even if it is unlawful, in the absence of nullity and knowledge of unlawfulness.[891] Claimants point out that the District Court did not identify a precise basis on which the Services Agreement could be considered void and that any finding of nullity would be contradictory to the Court's statement that, pursuant to the APA, "voidness of an administrative act (or a public law contract entered into instead) […] cannot emerge at a later stage."[892] Furthermore, the District Court was mistaken in holding that the ECA had terminated the contract through the rejection of the 2011 Tariff Application.[893]

835. On appeal, the Supreme Court reached a similar conclusion to that of the District Court in holding that the Services Agreement was no longer capable of performance under the 2010 PWSSA. As discussed above, the Supreme Court found that this result arises from both the change in the nature of the regulator's duties and the changes regarding the calculation of tariffs introduced by the 2010 PWSSA.[894]

836. The Tribunal considers the reasoning and conclusions of the Supreme Court persuasive, and does not find it necessary to comment further on this issue. In view of this decision, Claimants'

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[888] **C-432**, Tallinn Circuit Court decision of 26 January 2017, ¶¶26 and 27.

[889] Cl. PHB, ¶422.

[890] Cl. PHB, ¶446.

[891] Cl. PHB, ¶¶432 and 433.

[892] **C-432**, Tallinn Circuit Court decision of 26 January 2017, ¶19.

[893] Cl. PHB, ¶445.

[894] Supreme Court Decision (12 December 2017), ¶24. The Tribunal notes that the Supreme Court also found that the adoption of the 2010 PWSSA did not breach the legitimate expectations of ASTV under Estonian constitutional law (¶25).

argument regarding the enforceability of the Services Agreement bears less relevance and rather goes to the obligations of the ECA's in establishing the Methodology, which are discussed below.

(ii) The Obligations of the ECA regarding the Adoption of a Tariff Methodology under Estonian Law

837. According to Respondent, the ECA had no choice but to dismiss the 2011 Tariff Application because it contravened the law to the extent that the tariffs proposed by ASTV were not "cost-based." In other words, the ECA did not have the discretion to apply the Services Agreement's methodology.[895] Rather, the ECA had the authority to determine and apply the methodology of its choice as long as that methodology complied with the existing regulatory framework.[896]

838. Claimants argue that the language of the 2010 PWSSA afforded sufficient discretion to the ECA to consider the tariff methodology set out in the Services Agreement because the 2010 PWSSA neither defines the phrase "capital invested," nor prescribes a specific methodology for setting tariffs.[897]

839. Furthermore, as explained above, Claimants argue that the Services Agreement remained enforceable after the entry into force of the 2010 PWSSA and that the ECA was bound to apply the Services Agreement's methodology.[898] Alternatively, the ECA should have at least considered the Services Agreement and given due regard to the established practice of the former regulator.[899] They rely on Art. 3 and 4 of the APA, which notably provide that an administrative authority must consider the legitimate interests at play.[900]

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[895] Resp. Rej., ¶¶208-212, referring to Rask 1st ER, ¶¶185 and 186.

[896] Resp. PHB, ¶¶219-222.

[897] Cl. Reply, ¶¶118 and 119, referring to Pikamäe 1st ER, ¶¶20 and 21. Note that Mr Pikamäe refers to the minutes of meeting in the course of the parliamentary works stating that the inclusion of the words "of the capital invested" were intended to clarify the wording of the act which is otherwise vague: "Explanation: Depreciation of non-current assets financed by grant aid, and the justified profitability calculated thereon should not be included in the price of the service. To the best of the knowledge of the Competition Authority, in accordance with the guidelines applied to price regulation in sectors comparable with the scope of application of this draft Act, at present depreciation of noncurrent assets financed by grant aid or the justified profitability calculated thereon is not included in the prices charged for services. From the point of view of purposeful implementation of the Act it is essential that it is worded explicitly and that the Competition Authority would not need to argue with water undertakings, when implementing the Act, because of the vagueness of its wording." Cl. PHB, ¶¶484 and 485 and Pikamäe 2nd ER, ¶19.

[898] Cl. PHB, ¶¶482 and 483.

[899] Cl. PHB, ¶¶479 and 486.

[900] **RL-54**, Estonian Administrative Procedure Act (6 June 2001), Art. 3 and 4: "§ 3. Protection of rights (1) In administrative procedure, the fundamental rights and freedoms or other subjective rights of a person may be restricted only pursuant to law. (2) Administrative acts and measures shall be appropriate, necessary and proportionate to the stated objectives. § 4. Right of discretion (1) The right of discretion (discretion) is an authorisation granted to an administrative authority by law to consider making a resolution or choose between different resolutions. (2) The right of discretion shall be exercised in accordance with the limits of

840. The Tallinn District Court confirmed that the terms for determining prices under the 2010 PWSSA remain undefined. The District Court also found that the AMB/2010 PWSSA granted the ECA the appropriate administrative discretion to stipulate the principles according to which tariffs must be determined. The District Court specified that in establishing its methodology, the ECA was not bound by the mechanism applied earlier by the municipalities and characterised the Methodology as an administrative regulation.[901]

841. The Supreme Court confirmed the Tallinn District Court decision regarding the discretion accorded to the ECA and further agreed that the Methodology constituted an administrative regulation. The Supreme Court further found that the choices made by the ECA in establishing the Methodology were among the options reasonably available to it, and emphasised that the evidence failed to demonstrate the existence of a prevailing method for determining water tariffs in Europe or elsewhere.[902]

842. It thus appears, and the Tribunal is satisfied that, as a matter of domestic Estonian law, the ECA properly exercised its discretion to elaborate the Methodology.

843. This does not, of course, dispose of the question whether Estonia breached Claimants' legitimate expectations under international investment law.

e) The Economic Evidence relied on by the Parties

844. The Parties rely on their respective economic experts: Mr Andrew Meaney, for Claimants; and Dr Richard Hern, for Respondent.

845. Before engaging in an analysis of this evidence, it is worth recalling at the outset Claimants' own comments on this point. Claimants allege that the majority of the economic evidence is not relevant to their claims. According to Claimants' primary case, the Tribunal need not and should not engage in an analysis of ASTV's profitability since they had for legitimate expectations that the tariffs would be set in accordance with the Services Agreement and its amendments:

> It is important that the economic evidence in this case is placed in its proper context. Much of the economic evidence is irrelevant to the Claimants' primary claim, which is that they had a legitimate expectation that the privatisation agreements on the basis of which their investment was made, as amended, would be respected, and ASTV's tariffs set in line with the tariff methodology in the Services Agreement. <u>The K factors having been set for the period 2011 to 2020 by the 2007 Amendment, there was no requirement to carry out a further justified profitability analysis when setting ASTV's tariffs for</u>

<u>authorisation, the purpose of discretion and the general principles of justice, taking into account relevant facts and considering legitimate interests.</u>" [Emphasis added]

[901] **C-432**, Tallinn Circuit Court decision of 26 January 2017, ¶22.

[902] Decision of the Supreme Court of 12 December 2017, ¶¶30-34.

2011. ASTV's tariffs should simply have been changed by reference to CPI only (the K factor having been set at zero).[903] [Emphasis added]

846. According to Claimants, to the extent that the Tribunal deems it necessary to measure ASTV's profitability, that profitability should be assessed by way of an internal rate of return (the "**IRR**") analysis using the 2001 Business Plan as a benchmark.[904]

847. In a majority of the Tribunal's view, this position goes to the heart of the question of Claimants' legitimate expectations regarding the method for setting tariffs.

848. In what follows the Tribunal will briefly describe the Parties' positions as to the role of international best practices in the assessment of ASTV's profitability and the main points of disagreements between the Parties in order to direct the discussion of the experts' opinions.

(i) The ECA's Obligations in Adopting the Methodology and Consideration of the Industry Standard

849. The Parties were asked to comment, in their post-hearing submissions, on whether the ECA had the obligation, under Art. 3(1) of the Treaty, to consider international best practice and international water management principles when considering ASTV's tariffs.

850. According to Respondent, the BIT does not require Estonia to consider international water management principles and related international best practices. It nonetheless submits that the ECA's conduct complied with these standards, as crystallised in the Methodology.[905] This is further discussed below.

851. Claimants submit that, at the time of the ASTV's privatisation, the regulatory regime was underdeveloped and out of phase with international best practices, and that a primary purpose of the privatisation was to correct this situation. As a consequence, the privatisation agreements entrusted UUTBV, as the chosen international operator and investor, with the duty to introduce and maintain proper industry standards. Claimants thus infer that the ECA was obliged to consider international practices including as incorporated into the privatisation agreements.[906]

(ii) The Two (2) Types of Methodologies at Stake

852. The first element of disagreement between the Parties' concerns the type of methodology for determining tariffs: on the one hand, the "rate of return" model, as implemented in the ECA's Methodology, and, on the other hand, the Ofwat model, which is the inspiration for the Services Agreement's tariff mechanism.

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903 Cl. PHB, ¶232. See also Cl. Reply, ¶¶130 and 131.

904 Cl. Reply, ¶¶131 and 132; Cl. PHB, ¶234.

905 Resp. PHB, ¶¶223-232 and 328.

906 Cl. PHB, ¶¶487-490.

853. According to Respondent, the rate of return model allows a utility to earn a fair level of return after having recovered its costs. This type of regime is applied in the United States, as well as in Portugal, the Czech Republic and Lithuania.[907] This assessment is made on the analysis of historic and projected costs. The regulator includes justified projected costs in the tariff and adds a profit component which is a multiple of WACC and the RAB. Tariffs are next reviewed from time to time when the utility's costs or the WACC change substantially.[908]

854. By way of reminder, the ECA's Methodology stipulates that the undertaking's RAB ought to be compared to nominal WACC, which serves as point of reference for determining justified profitability.[909] RAB is to be calculated according to the formula:

RAB = RABr + WC,

Where

RAB – regulated asset base;

RAB r – residual book value of RAB in the end of a regulation period;

WC – working capital.[910]

855. The Methodology specifies that the ECA ought to assess physical assets according to their NBV,[911] and that the working capital of a water utility company be set at 5% of the value of the regulated assets.[912] Importantly, the regulator determines the appropriate level of costs and profit based on data for the preceding 12-month period.[913]

856. The Ofwat model, which is the model developed by the United Kingdom water regulator, requires the setting of a performance target and tariff reviews at the end of a pre-defined regulatory period (ranging from two (2) to five (5) years). If the utility outperforms the target, it earns the profit derived from this outperformance. At the beginning of each period, profitability

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[907] Resp. PHB, ¶224; **C-241**, Expert report of Andres Root in the administrative matter 3-11-1355 (30 June 2014), p 3852.

[908] Resp. PHB, ¶224, referring to the expert opinions filed in the Estonian proceedings, **C-241**, Expert report of Andres Root in the administrative matter 3-11-1355 (30 June 2014), pp 3852-3853 and **C-240**, Expert report of Andres Juhkam in administrative matter 3-11-1355 (30 June 2014), pp 3780-3782.

[909] Ots 1st WS, ¶93.

[910] **C-188**, ECA's Methodology (12 November 2010), Clause 5.8.

[911] **C-188**, ECA's Methodology (12 November 2010), Clause 5.

[912] Ots 1st WS, ¶92; **C-188**, ECA's Methodology (12 November 2010), Clause 5.9.

[913] **C-188**, ECA's Methodology (12 November 2010), Clause 2.12, which defines the "regulation period." This interpretation was confirmed by Mr Ots during the Hearing, Tr. Day 3 Mr Ots 173:10-22.

and tariffs are reassessed and adjustments are made to account for current market circumstances.[914]

857. It is uncontested that the Ofwat model was used as the reference by the City of Tallinn for the purposes of the privatisation, as confirmed by Mr Sellner.[915]

858. It is also of note that Mr Andres Jukham, the court-mandated expert in the Estonian proceedings, explained that, when applied consistently and correctly, the two (2) methodologies lead to similar results for the owner of the undertaking. They would, though, yield different water tariffs as well as dynamics and timing of free cash flow and revenue.[916]

859. In the Tribunal's view, and indeed as found by the Estonian courts, it cannot be said that one regulatory regime necessarily prevails as a matter of international good practice. Considering that Claimants did not hold legitimate expectations, the adoption of such regime did not run afoul of their rights. It cannot either be stated to amount to bad faith or made with an intent to deprive Claimants of the benefits of their investment.

860. The Tribunal thus conclude that Estonia did not breach the FET standard, whether by violating any protected expectations or otherwise.

B) CLAIMS OF BREACHES OF DUE PROCESS, DISCRIMINATION AND UNREASONABLE MEASURES

861. In addition to a violation of their legitimate expectations, Claimants argue that Estonia has also committed various other breaches of Art. 3(1) of the BIT.

862. In their post-hearing submissions, Claimants divide these claims into three (3) categories:

- Estonia's failure to afford due process to Claimants by rejecting the 2011 Tariff Application and issuing the Prescription;[917]

- Estonia's liability for the public campaign against ASTV;[918]

- Estonia's unreasonable and discriminatory measures against ASTV.[919]

863. The first two (2) categories concern breaches of the FET standard, while the third concerns claims related to the non-impairment standard of Art. 3(1), which provides:

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[914] **C-240**, Expert report of Andres Juhkam in administrative matter 3-11-1355 (30 June 2014), pp 3778-3780; **C-241**, Expert report of Andres Root in the administrative matter 3-11-1355 (30 June 2014), pp 3853-3856.

[915] Sellner WS, ¶24. Mr Sellner testified at the Hearing that the Ofwat model would have been the only suitable point of reference in 2001, Tr. Day 4 Mr Sellner 68:21-69:9.

[916] **C-240**, Expert report of Andres Juhkam in administrative matter 3-11-1355 (30 June 2014), p 3781.

[917] Cl. PHB, ¶¶466 and 467.

[918] Cl. PHB, ¶468.

[919] Cl. PHB, ¶¶469 and 470.

> Each Contracting Party shall ensure fair and equitable treatment of the investments of nationals of the other Contracting Party and shall not impair, by unreasonable or discriminatory measures, the operation, management, maintenance, use, enjoyment or disposal thereof by those nationals.

1) The Alleged Breaches of Due Process

864. Claimants assert that Respondent breached due process in multiple manners. Again, the thrust of their claim lies in the disregard by the ECA of the tariff scheme set out at ASTV's privatisation.

865. More specifically, they submit that they were not availed due process in:

- The elaboration of the Analysis by the ECA and its publication;
- The elaboration of the Methodology by the ECA;
- The Chancellor of Justice's investigation;
- The rejection of the 2011 Tariff Application.

866. The Tribunal will first review the international investment case law regarding breaches of due process and how those breaches may trigger international liability. It will next review the various breaches alleged by Claimants set out above.

a) Due Process in International Investment Law

867. There is no significant difference between the Parties' respective understandings of the relevant standard.

868. The FET standard imposes on a State the obligation to grant due process to investors with respect to their investment.[920]

869. The authorities referred to by the Parties establish that the FET standard does not protect against each and any breach of due process. As noted in *Waste Management v Mexico*:

> [T]he minimum standard of FET under Article 10.5 of CAFTA-DR is infringed by conduct attributed to the State and harmful to the investor if the conduct is arbitrary, grossly unfair or idiosyncratic, is discriminatory or involves a lack of due process leading to an outcome which offends judicial propriety.[921]

870. A breach of due process as understood under domestic law does not necessarily entail a breach of international law; an international investment tribunal does not sit as a reviewing

[920] **CL-2**, *Bayindir Insaat Turizm Ticaret Ve Sanayi A.S. v Islamic Republic of Pakistan*, ICSID Case No. ARB/03/29, Award (27 August 2009), ¶178; Cl. Reply, ¶299.

[921] **CL-110**, *TECO v Guatemala*, *supra* note 584, ¶454. See also **RL-154**, *AES v Hungary*, *supra* note 487, ¶9.3.40.

body of a domestic decision.[922] Furthermore, where a breach has been remedied, a tribunal will not normally find a violation of the FET standard.[923] The standard of review of the State measure will also vary according to the nature of the decision-making process at issue: administrative proceedings trigger less stringent due process obligations than judicial proceedings.[924] On this latter point, the Tribunal has considered the evidence offered by Mr Märt Rask, one of Respondent's Estonian law experts, who testified that the ECA did not breach Estonian administrative procedure and commented on the Chancellor of Justice's investigation as well as the 2015 decision of the Tallinn Administrative Court.[925]

b) The Due Process Breaches pertaining to the Analysis

871. As discussed above at paragraphs 230 and following, the ECA initiated a market analysis of water tariffs at the end of December 2008. Over 2009, the ECA requested information from several undertakings, including ASTV. Representatives of the ECA and ASTV met, and ASTV shared confidential information with the ECA in its response to the ECA questionnaire. On 30 November 2009, the ECA transmitted the Analysis to ASTV. The day after, Mr Ots publicly stated that ASTV's tariffs should be decreased by 25%.

872. Claimants identify several instances in which Respondent's conduct breached due process in this context, namely:

- The ECA used a market investigation to target ASTV and to obtain confidential information from ASTV;[926]

- The ECA deliberately ignored the privatisation agreements for purposes of the Analysis;[927]

- The Analysis is economically flawed;[928]

- Having claimed to rely only on public information, as it pretends, the ECA failed to consider accurate and complete data;[929]

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[922] **RL-164**, *ECE Projektmanagement International GmbH and Kommanditgesellschaft PANTA Achtundsechzigste Grundstücksgesellschaft mbH & Co v Czech Republic*, PCA Case No. 2010-5 (19 September 2013), ¶4.764 [*ECE v Czech Republic*].

[923] **RL-164**, *ECE v Czech Republic*, ibid, ¶4.805.

[924] **CL-115**, *Waste Management v Mexico*, ¶¶98 and 99; **CL-116**, *International Thunderbird Gaming Corporation v United Mexican States*, UNCITRAL, Arbitral Award (26 January 2016), ¶200.

[925] Rask 1st ER, ¶¶169-200.

[926] Cl. Reply, ¶304.

[927] Cl. PHB, ¶¶323-331.

[928] Cl. PHB, ¶¶333 and 334.

[929] Cl. Reply, ¶315.

- The ECA failed to provide a meaningful opportunity to ASTV to comment and/or react prior to the public release of the Analysis;[930]

- The day after the issuance of the Analysis, Mr Ots held a press conference during which he stated that ASTV's tariffs should be reduced by 25% and made other denigrating comments.[931]

(i) The Use of the Market Investigation to Target ASTV

873. Claimants argue that the ECA used its 2008-2009 market investigation to conduct a targeted analysis of ASTV's tariffs, which was improper.[932]

874. Respondent submits that the market investigation was triggered by real and extensive evidence of regulatory problems prevailing in the Estonian water industry. Far from targeting ASTV, the study encompassed twelve undertakings.[933] Mr Ots explained, and the Tribunal accepts, that the *Competition Act* entrusted the ECA with the power to conduct such investigation and that the ECA had previously investigated and issued recommendations in connection with industries that it did not regulate.[934]

875. Mr Ots testified that the ECA's market investigation was not intended to focus on ASTV. However, as it turned out, the investigation suggested that – in the ECA's opinion – ASTV was the only water undertaking charging such excessive tariffs. This situation warranted further scrutiny, considering among other things that ASTV services one-third of the population of Estonia.[935]

876. The Tribunal does not consider that Mr Ots' testimony on these matters was seriously contradicted, or that there exists any compelling evidence that the market investigation was a pretext to target ASTV or obtain its confidential information. The Tribunal finds that the launch of the market investigation by the ECA was not in itself wrongful.

(ii) The ECA's Failure to Consider the Privatisation Agreements

877. From the Tribunal's perspective, the most significant and serious criticism of the ECA's conduct concerns its alleged disregard of the privatisation agreements and, more generally, of ASTV's privatisation scheme.

878. Respondent does not squarely deny that the ECA did not consider the privatisation agreements in elaborating the Analysis. It submits, however, that Claimants' claim wrongly focuses on the result of the Analysis, as opposed to the process which led to it.[936] Respondent

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[930] Cl. Reply, ¶314.

[931] Cl. Reply, ¶¶311-313.

[932] Cl. Reply, ¶304.

[933] Resp. Rej., ¶435.

[934] Ots 1st WS, ¶14; Ots 2nd WS, ¶¶2 and 7

[935] Ots 1st WS, ¶26 and ¶36; Ots 2nd WS, ¶8.

[936] Resp. PHB, ¶330.

states that the Analysis constitutes merely a non-binding assessment of ASTV's tariffs, which did not carry with any direct legal effect.[937] It contends that, in any event, the findings of the Analysis were correct.[938]

879. The Tribunal partly shares Respondent's view on this point. To the extent that Claimants' allegations pertain to the outcome of the Analysis, and the calculations it derives, in isolation, no breach of due process may be found.

880. However, the Tribunal does not believe that this fully or faithfully reflects Claimants' claim, which includes the allegedly unreceptive attitude of the ECA in assessing ASTV's tariffs. More specifically, the thrust of the claim concerns the ECA's purported knowledge – and wilful disregard – of the privatisation agreements and their tariff mechanism.

881. It cannot be reasonably argued that the ECA had no knowledge of the existence of the privatisation agreements or the mechanism by which ASTV's tariffs were set. Indeed, the Analysis itself provides an overview of the legislation applicable to ASTV's tariffs and of the relevance of the privatisation agreements in this respect, based on information available on ASTV's website.[939] The ECA notably restates the formula agreed between ASTV and the City of Tallinn under the 2002 Amendment and expresses concerns as to whether this regime is cost-based.[940] The ECA also commented on the fundamental differences between that methodology and its own:

> The CA deems it necessary to note in the first place that, leaving aside the actual justifiability of ASTV's prices, barely the manner used by Tallinn City Government for regulating the prices is not appropriate to a proper price regulation. <u>For the purpose of an effective price formation, the assessment of the extent ASTV's prices are based on the costs, should be done in line with the law and the price regulation procedure,</u> <u>but Tallinn City Government is following the agreement signed upon the privatisation of ASTV in establishing the water supply and sewerage prices (CPI, K-coefficient) instead. The CA notes that due to the fundamental differences of the tariff formation mechanisms included in the procedure and the agreement, it is actually not possible to apply them in a parallel way and the two mechanisms would lead to the same tariff rates only in case of an unlikely coincidence</u>. <u>As Tallinn City Government has decided to proceed namely from the agreement signed upon the privatisation of ASTV, then inevitably it has not been</u>

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[937] Resp. C-M, ¶464.

[938] Resp. C-M, ¶465.

[939] "The following overview treats the price regulation from two different aspects. In clause 2.1 the general bases of the price regulation are characterised. In clauses 2.2-2.4 an overview is provided about the bases of the price regulation established by Tallinn City Government and Tallinn City Council – which on the basis of the valid legislation should constitute the price regulation – and in connection with that the impact of the agreement concluded at the privatisation of ASTV on the price formation is studied" (**C-38**, ECA Analysis, p 876).

[940] **C-38**, ECA Analysis, p 881.

sufficiently analysed to what extent the prices of ASTV are based on the costs.[941] [Emphasis added]

882. The ECA expressed the opinion that the City of Tallinn had "inevitably" failed to assess the costs in setting tariff waters since it had relied on contractual commitments, as appears from the citation above.

883. These excerpts of the Analysis indicate that the ECA was well aware of, yet had had no inclination to consider, let alone apply, the tariff scheme set out in the privatisation agreements.

884. At the Hearing, Mr Ots recognised that he did not review the Services Agreement and the other privatisation contracts for the purposes of the Analysis. Members of his team merely gathered information regarding these agreements from ASTV's website and confirmed to him that ASTV had not communicated copy of the contracts to the ECA. Mr Ots further testified that in his opinion the ECA could not have considered these documents because they were not public.[942]

885. Mr Ots also testified that, in any event, the ECA did not need to review the privatisation agreements[943] and that they were irrelevant.[944] Furthermore, he stated that there was "no possibility" that a more detailed analysis could have affected the ECA's conclusions:

> MR WEINIGER: Just before we took that break, I showed you paragraph 8 of your second statement, where you said that the detailed analysis of ASTV's water tariffs was a consequence of your market investigation, not its original purpose.
> Then I was going to take you to paragraph 36 of your first statement, and see if you would agree that based on your initial investigation, you had already concluded that ASTV was charging excessive tariffs?
> A. Yes.
> Q. If we look at paragraph 36 again of your first witness statement, was this a preliminary conclusion that ASTV was charging excessive tariffs?
> A. Exactly, there was a preliminary conclusion.
> Q. Was there a possibility that a more detailed analysis would have led to a conclusion that ASTV was not in fact excessively profitable?
> A. No.
> Q. So there was no possibility that your detailed analysis would have changed your mind in any way?
> A. No.[945] [Emphasis added]

[941] **C-38**, ECA Analysis, p 904.

[942] Tr. Day 4 Mr Ots 108:20-111:12.

[943] Tr. Day 4 Mr Ots 111:17-20.

[944] Tr. Day 4 Mr Ots 142:25-143:5.

[945] Tr. Day 3 Mr Ots 185:15-186:10.

886. This evidence indicates a firm unreceptiveness by the ECA to consider the privatisation agreements and the tariff mechanism they set out, which, it was fully aware, formed the basis on which ASTV operated.

887. Although ASTV did not communicate the contracts to the ECA, there is no indication that the ECA ever sought to obtain a copy of them. It is of note that the ECA's questionnaire did not require that such information on the undertaking and its tariff methodology be provided to the ECA.946 Yet, this did not prevent the ECA from discussing the privatisation agreements and ASTV's existing tariff mechanism in the Analysis, as noted above, nor did it prevent Mr Ots from complaining about the alleged lack of information available to him about ASTV.947 In the Tribunal's view, there is no basis to believe that, had the ECA wished to consider the privatisation agreements or other documents explaining the basis for ASTV's tariffs, such documents would not have been provided to it.

888. With respect to Mr Ots' comments that the Analysis could only refer to public information, Mr Ots himself suggested that this in no way prevented the ECA from considering, though not disclosing, confidential information.[948] Nor is the Tribunal convinced that, had the ECA wished to consider *and comment on* the documents substantiating ASTV's tariffs, the Analysis could not have been released without disclosing confidential information contained in those documents.

889. This generally unreceptive attitude on the part of Mr Ots and the ECA does not, however, mean that due process was breached. As stated above, not every procedural unfairness amounts to a violation of international law. In the situation at hand, notwithstanding the refusal of the ECA to consider the privatisation agreements, it is not at all evident that the outcome would necessarily have been different had the ECA acted otherwise. Although a legitimate expectation is clearly not a condition precedent to a finding of breach of due process, as discussed above the privatisation agreements themselves confirm that they were subject to changes to the legal and regulatory regime governing water undertakings and that future tariffs would be set in accordance with the regime in force at the relevant time.

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[946] **C-37**, ECA Information Request (12 February 2009).

[947] Tr. Day 4 Mr Ots 139:17-140:11: "THE PRESIDENT: That helps clarify matters in my mind, thank you. Just before lunch, if I understood you – again, I am going to look at my notes, bear with me for a second – you were discussing with Mr Weiniger the extent to which in your analysis, and in your work in the 2009/2010 period, you tried to understand the previous regulatory regime.

A. (In English) Yes, we have tried to understand, but of course when we have conducted our analysis by 2009, then we got very, very little information about this regulation made by the City of Tallinn, because we just got the letter from the City of Tallinn, this was by my mind two pages, and the rest of the information we got from the publicly available sources, like the webpage of Tallinna Vesi or the webpage of the City of Tallinn. And based on that, we have studied the regulatory regime implemented by the City of Tallinn, but honestly to say there was not too much information, but based on that information what we got, we made our results." [Emphasis added]

[948] Ots 1st WS, ¶47: "ASTV had asked us to treat the non-public data we received from them confidential. We respected their request and based the Analysis only on publicly available data, including ASTV's detailed financial statements. However, the confidential data that we had also analyzed led to the same material conclusions. We explicitly pointed this fact out in the Analysis." [Emphasis added]

(iii) The Economic Flaws of the Analysis

890. Claimants contend that the economic flaws in the Analysis consist in another breach of due process because they flow from the application of an incorrect methodology. They submit that, even if it were appropriate for the ECA not to consider the Services Agreement, the Analysis compounds errors insofar that: (i) it only considers one year of data (2007-2008), which is inconsistent with the long-term nature of the privatisation, (ii) it took a period from the return phase of the investment out of context, and (ii) it based the RAB on the NBV, in lieu of the privatisation value.[949]

891. Again, as stated above at paragraphs 878 and 879, these allegations, even if true, cannot in themselves lead to a breach of due process. A breach, if any, would rather lie in the failure to hear ASTV's representatives on this matter. The Tribunal will therefore not engage with them.

(iv) The Public Release of the Analysis

892. Claimants also impugn the ECA's conduct surrounding the release of the Analysis, in particular: the refusal to allow ASTV more than 24 hours to prepare for the release; the fact that the Analysis was drafted in Estonian; the fact that ASTV had not previously expected that the ECA would call into question the tariff methodology set out in the Services Agreement.

893. According to Claimants, Mr Ots declined Mr Plenderleith's request to delay the publication of the Analysis so as to allow for time to translate the Analysis into English and for ASTV's management to read it and issue a stock exchange announcement.[950] Mr Plenderleith further testified that in their previous meeting, in November 2009, it was never suggested that the ECA might challenge ASTV's tariff methodology.[951]

894. Claimants also criticise the public statements made by Mr Ots in the wake of the publication of the Analysis:

> "In such a way that a long-term agreement is concluded, where the price of water shall be increased each year, like that is done perhaps only in Africa," added Ots. According to him in developed countries the price of water is based purely on how much has been invested into the provision of the service. […]
>
> According to Ots the CA has not interfered in the formation of the price policy of water service. "The main regulator is Tallinn City Government," he added. "It is wrong to look for the guilty one, but the final outcome should be that the water price reduces by up to 25%, confirmed Mr Ots.[952]

895. Respondent points out that it was not required under Estonian law to obtain approval from the subject of an investigation prior to the publication of its findings. It relies in this regard on the

[949] Cl. PHB, ¶¶333 and 334

[950] Cl. Reply, ¶314; Cl. Mem., ¶167.

[951] Plenderleith 2nd WS, ¶¶12 and 13.

[952] **C-158**, Äripäev press article (2 December 2009), p 2721.

expert opinion of Mr. Rask, who as mentioned above, explains that due process requirements are relaxed with respect to a non-binding decision:

> In addition, it must be taken into account that an administrative procedure is subject to requirements that are as stringent as the extent of the procedure's effect on a person. Thus, for example, the general right to be heard does not apply in every kind of administrative procedure, but hearing the subject of an administrative act is mandatory where a decision is being made to the detriment of a person (APL § 40(3)(3)). Likewise, according to § 56(1) of the APL, justifying an administrative act in writing is mandatory only in the case where the administrative act is issued in writing or if the issuance of a beneficial administrative act is refused. Also, according to § 56(4) of the APL, the reasoning of an administrative act does not have to contain a description of the factual circumstances giving basis to the administrative act, if the application of the subject of the administrative act is being granted, and rights and freedoms of third parties are not restricted.
>
> Therefore, in the cases where the administrative procedure is directed towards a non-binding result (as e.g. in the case of the Competition Authority's market survey) or where no decision is made to the detriment of any party or restricting anyone's rights or freedoms, the principles applicable to the form of the administrative procedure are more relaxed. In the Expert's opinion, the Competition Authority did not breach any principles of administrative procedure when conducting the non-binding market survey of the water sector, and it had the express legal basis to conduct it (§ 55(2) of the Competition Act).[953] [Emphasis added]

896. In any event, Respondent emphasises that the ECA nonetheless provided ASTV with advance notice of the public release of the Analysis.[954] According to Respondent, it was also entirely appropriate for the ECA to communicate with ASTV in Estonian.

897. Respondent claims that during their 3 November 2009 meeting, Mr Ots in fact explained to Mr Plenderleith the ECA's findings regarding ASTV's excessive profits.[955] Mr Ots testified in writing[956] and at the Hearing that further comments from ASTV after the Analysis was completed but before it was published could not have affected those findings:

> Q. If we look at paragraph 12 of your second witness statement, we see in the second sentence: "I am also certain that ASTV's comments on the analysis would not have affected our results." That's your belief, isn't it?
> A. Yes.

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[953] Rask 1st ER, ¶¶177 and 178; Resp. C-M, ¶461.

[954] Resp. Rej., ¶180.

[955] Ots 2nd WS, ¶13.

[956] Ots 2nd WS, ¶12.

> Q. In the second sentence of paragraph 13, you say: "The Competition Authority did not fail to engage with ASTV's points as alleged by Claimants." Do you see that in paragraph 13?
> A. Exactly.
> Q. What I would like to put to you is that if you are certain, as you say in paragraph 12, that nothing ASTV would have said could have changed your mind or affected the results, it doesn't seem to me that you were really
> open to a discussion with ASTV about the analysis.
> A. No, what do you mean, in what way? I do not agree.
> Q. ASTV wanted to discuss the analysis with you before it was published, and you didn't give them an opportunity, did you?
> A. I agree.
> Q. You say that's because you didn't think that their comments would have affected your findings?
> A. Exactly.[957]

898. Regarding the public comments made by Mr Ots, Respondent submits that Mr Ots only provided a short television interview, which he felt compelled to give due to the wide public interest and concern over ASTV' tariffs, and that it was not the first time that the ECA would have publicly commented on some of its findings.[958]

899. The Tribunal finds that Claimants have failed to demonstrate any breach of due process in relation to the release of the Analysis.

900. Certainly there is conflicting evidence as to the nature of the exchanges that occurred between ASTV and the ECA's representatives prior to the release of the Analysis. But in any event, the Tribunal can find no breach of Estonian law, let alone international law, in the circumstances surrounding the public release of the Analysis.

(v) Conclusion on the Alleged Breaches of Due Process pertaining to the Analysis

901. For the reasons explained above, the Tribunal concludes that Estonia did not, under international law, fail to afford due process to Claimants. This is so whether one considers the breaches alleged by Claimants in isolation or cumulatively.

c) The Chancellor of Justice's Investigation

902. Claimants also allege that they were not afforded due process in the context of the investigation conducted by the Chancellor of Justice, discussed above at paragraphs 246 and following.

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[957] Tr. Day 3 Mr Ots 181:1-24.

[958] Ots 2nd WS, ¶¶21 and 22.

903. Claimants' most significant criticism lies in particular in their claim that the Chancellor of Justice pursued legal action without conducting an independent analysis,[959] which, they assert, had a detrimental impact on the value of ASTV's shares.[960]

904. Respondent contends that the Chancellor of Justice complied with the due process applicable to constitutional reviews and points out that the Chancellor effectively had no choice but to conclude that the City's regulation of ASTV did not comply with the law since it failed to provide an explanation to him.[961]

905. The Supreme Court of Estonia dismissed the Chancellor of Justice's application to enforce his recommendation to decrease ASTV's tariffs. The Court noted that the City of Tallinn's regulation may be challenged before the Administrative Court. The Chancellor subsequently terminated his investigation but in statements to the media invited consumers to commence legal proceedings against ASTV.[962]

906. The Tribunal does not find any breach of due process here. In particular, the Tribunal does not consider that the Chancellor's reliance on the Analysis prepared by the ECA, a specialised agency, to be inappropriate. In any event, there is no evidence that the Chancellor's actions caused damage to Claimants. Even if these events may have negatively influenced ASTV's stocks, no evidence has been offered as to how this loss actually crystallised.

d) The Due Process Failure in the Development of the Methodology

907. Claimants argue that the ECA did not comply with due process in developing the Methodology.[963] In particular, they say, the ECA failed to consider ASTV's comments and those of the EVEL, which raised similar concerns than ASTV's.[964]

908. Respondent argues that the ECA duly considered Claimants' and the EVEL's submissions in the elaboration of the Methodology. They cite the following excerpt of Mr Ots' testimony:

> Q. Is Mr Plenderleith correct to be complaining that the latest draft of the methodology did not contain any responses to the points and questions that he had included with his previous letter?

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[959] Cl. PHB, ¶338.

[960] Cl. Reply, ¶328; **C-175**, Blog post by Andrus Alber Arvamused, "Tallinna Vesi "supported" the discussion on AMB with 500m EEK" (14 September 2010).

[961] Resp. PHB, ¶¶201 and 202; Resp. Rej., ¶187.

[962] **C-192,** Decision of Estonian Supreme Court in case No. 3-4-1-6-10, "Petition of the Chancellor of Justice to declare invalid § 1 of regulation no. 75 of the Tallinn City Government" (22 November 2010); **R-329**, Press Release of the Estonian Supreme Court, "Supreme Court: The water prices in the City of Tallinn could have been challenged in the administrative court"; **C-144**, Various press articles (30 January 2009 to 23 November 2010).

[963] Cl. PHB, ¶¶362-365.

[964] **C-177**, Letter from KPMG Baltic SIA to Estonian Water Works Association (24 September 2010); **C-182**, KPMG Baltic SIA report on the ECA's Proposed Methodology (26 October 2010); **C-179**, Letter from City of Tallinn to the ECA (27 September 2010); Plenderleith 1st WS, ¶¶101-106.

A. No, I do not agree with that.
Q. Did you include ASTV's comments?
A. We asked ASTV to send in their comments, and to the extent it was possible, in accordance with the Estonian legislation, so as I said, we are following the legal framework, and as much as possible we included them.[965]

909. Respondent also underlines that the Tallinn Circuit Court ruled that ASTV had the opportunity to express its views regarding the Methodology.[966] Furthermore, it is noted that the Supreme Court found that the ECA benefits from wide discretion in preparing an administrative act such as the Methodology.[967]

910. The Tribunal also takes note, once again, of certain elements of Mr Ots' evidence which, in its view, suggests a relatively closed-minded approach to the work of the ECA:

- Mr Ots testified that he did not agree that a regulatory system is best implemented with the involvement of all industry participants.[968]

- Mr Ots recognised that the AMB does not mandate a one-year regulatory period and that no other country takes this approach, as per Dr Hern's expert report.[969]

- Mr Ots was highly critical of the Ofwat approach but accepted that the ECA is required to monitor and be aware of the international situation.[970]

- Mr Ots explained that he sought to instigate a change in regulatory approach, and that he did not deem it necessary to ensure a certain consistency with the previous regime.[971]

911. As indicated above, the Supreme Court of Estonia has found that the directives set out in the Methodology fall within the options available to the ECA in the reasonable exercise of its discretion under Estonian law. The Tribunal having been presented with no compelling factual or legal evidence sufficient to demonstrate otherwise, it can hardly find that the ECA committed a wrong in adopting the Methodology.

912. Furthermore, the Tribunal acknowledges the ECA's efforts to gather comments from stakeholders, including ASTV and the EVEL, during the process leading to adoption of the Methodology. Similarly, the ECA may not have had the obligation to tailor its directives, which would apply nationwide, to ASTV's particular situation.

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965 Tr. Day 3 Mr Ots 193:10-19.

966 **C-432**, Tallinn Circuit Court Decision of 26 January 2017, ¶23.

967 Supreme Court Decision (12 December 2017), ¶32.

968 Tr. Day 3 Mr Ots 192:6-21.

969 Tr. Day 3 Mr Ots 168:17 and 173:25.

970 Tr. Day 3 Mr Ots 177:15 and 178:25.

971 Tr. Day 4 Mr Ots 116-117.

e) The Due Process Failure in the Rejection of the 2011 Tariff Application

913. In their Memorial Claimants again argue that the ECA failed to consider the Services Agreement and, more generally, ASTV's privatisation – but this time, with respect to the rejection of the 2011 Tariff Application.[972]

914. Respondent argues that the ECA's rejection of the 2011 Tariff Application was subject to several remedial mechanisms.[973] More specifically, upon receipt of the Tariff Application, the ECA requested that ASTV complete the questionnaire and provide additional information, and allowed ASTV to revise its application.[974] Respondent stresses that the ECA met with ASTV on several occasion to discuss the application. The ECA even engaged proactively with ASTV, to ensure that it understood the scope of additional information needed for the ECA's assessment and an opportunity to update its application.[975] In any event, ASTV's application on its face required its rejection, *inter alia* for its failure to comply with the directive to eliminate price discrimination between private and commercial customers. Respondent also refers to the mistake included in the Tariff Application, included the EUR 98 million overstatement, and the fact that ASTV did not provide the *pro forma* projections to the ECA.[976]

915. Again, the Tribunal does not identify any breach of due process. Rather, the criticisms made by Claimants largely recoup their claim of breach of the FET standard, which have already been dismissed.

2) The Alleged Negative Publicity Campaign against Claimants

916. Claimants assert that members of the ECA and key figures of the Estonia Central Government, including the sponsors of the AMB in the Estonian Parliament, the EOKL, the Chancellor of Justice and Mr Ots, engaged in a publicity campaign against ASTV. They attribute these actions to the State and argue that they breached the FET standard[977] and negatively affected the value of ASTV's shares.[978]

917. According to Respondent, the conduct of private entities and individuals, such as the EOKL and its members (even if those members are also members of parliament), is not attributable to the Estonian State. With regards to the statements of the Chancellor of Justice, Respondent considers them to be objective criticism of the facts that will prompt the regulation of ASTV's tariffs. More generally, Respondent underlines that these statements, stemming from private entities and officials, form part of a legitimate debate, albeit critical of ASTV, that does not breach the FET standard.[979]

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[972] Cl. Mem., ¶218. Claimants do not seem to raise this point elsewhere than in their Memorial.

[973] Resp. C-M, ¶464; Resp. PHB, ¶¶333-335.

[974] Resp. Rej., ¶440.

[975] Resp. C-M, ¶¶466 and 467.

[976] Resp. PHB, ¶¶333-335.

[977] Cl. Mem., ¶219; Cl. Reply, ¶¶322 and 326; Cl. PHB, ¶468.

[978] Cl. Reply, ¶328.

[979] Resp. C-M, ¶469; Resp. Rej., ¶¶444-446; Resp. PHB, ¶336.

918. The Tribunal agrees with Respondent. ASTV's tariffs undoubtedly attracted great criticism in Estonia. However, the Tribunal does not consider that these actions may be attributed to the State (with the possible exception of the conduct of the Chancellor), or, in any event, that Claimants have demonstrated that they give rise to a violation of international law or caused any quantified damage to Claimants.

3) The Alleged Unreasonable and Discriminatory Measures

919. In addition to their claims for breach of legitimate expectations and due process, Claimants submit that Respondent contravened the non-impairment standard of Art. 3(1) of the BIT through unreasonable and discriminatory measures.

920. This claim focuses on the targeting of ASTV in the course of the legislative reform of the water tariffs regime, as laid out at paragraphs 768 and following, above.

921. According to Claimants, Respondent further discriminated against ASTV, primarily in the application of the AMB to ASTV and by failing to consider ASTV's specific circumstances.

922. In both instances, Claimants place particular emphasis on the objective sought by Estonia in adopting and implementing the AMB with respect to ASTV, that is, to lower ASTV's tariffs.[980] This conduct, they say, would have impaired Claimants' enjoyment of their investment by preventing them to earn the return anticipated at the time of the privatisation.[981] The damages complained of by Claimants under these claims thus correspond to those complained of in relation to their FET claims.[982]

923. The Tribunal considers that Claimants' claims of impairment of the investment are redundant, and it does not believe it necessary to address them here: Claimants allege that Estonia's conduct was unreasonable because (i) it was not justified by the so-called Low Tariff Problem, and (ii) the Estonian authorities' allegations of excessive tariffs are based on a miscalculation of ASTV's tariffs[983] – both of which allegations have already been considered and addressed by the Tribunal.

C) CLAIM OF BREACH OF THE UMBRELLA CLAUSE

924. Claimants also bring a claim under the "umbrella clause" contained at Art. 3(4) of the Treaty, by which Estonia undertook "to observe any obligation it may have entered into with regard to investments of nationals of the other Contracting Party."[984]

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[980] Cl. PHB, ¶469.

[981] Cl. PHB, ¶¶469 and 470.

[982] As a matter of fact, Claimants' submissions on the quantum of damages and their prayer for relief do not discriminate between the various claims they assert, Cl. PHB, ¶¶576-580, Cl. Reply, ¶¶602-604 and Cl. Mem. 226-232.

[983] Cl. Reply, ¶343.

[984] **C-1**, BIT.

925. Claimants principally allege that Respondent violated this obligation by its failure to implement the tariff mechanism of the Services Agreement and to apply the K-coefficients determined in the 2007 Amendment.[985] As with their FET claim, they rely on the suite of privatisation agreements, but place special emphasis on two (2) provisions of the 2007 Amendment: (i) Article 4.1.2, which sets the K factors to zero (0) until 2020, and (ii) Article 6.2, by which the Parties undertook to ensure that the amendment is complied with in a manner that "will not reduce the shareholder value of the Company."[986]

926. Respondent argues that (i) Claimants cannot rely on an agreement with the City of Tallinn for purposes of their umbrella clause claim, (ii) the City's contractual undertakings were in any event subject to modifications and future requirements of Estonian law, (iii) the City of Tallinn's commitments cannot bind the ECA, (iv) UUTBV cannot benefit from the umbrella clause because it is not a signatory of the Services Agreement and (v) the tariff formula set out at Article 7 of the Services Agreement is invalid under Estonian law.[987]

927. The Tribunal does not consider it necessary to explore this claim, which, as framed, is effectively duplicative of Claimants' claim for violation of their legitimate expectations. The claim advanced by Claimants is premised on the non-respect or the disregard of the privatisation agreements and, more particularly, the determination of the K-factors. However, the non-respect of these agreements does not at heart arise from a failure to abide by a contract, but rather from a change in the legislative and regulatory framework under which the privatisation agreements were executed. This is most notably illustrated by the finding of the Estonian courts[988] that, upon the entry into force of the AMB, the ECA did not become bound by the privatisation agreements. The umbrella clause does not then capture the essence of Claimants' claim, which is better considered through the lens of a purported breach of the FET standard. In any event, in view of the finding that the privatisation agreements themselves undermine the legitimate expectations claims, there is no need to further address this issue.

VIII. COSTS

928. It is trite to state that a tribunal constituted under the ICSID Convention is accorded broad discretion in awarding costs (including fees and expenses), as provided at Art. 61(2) of the ICSID Convention and Rule 47 of the Arbitration Rules.

929. In their submissions, both Parties argue that the Tribunal's discretion should be guided by the so-called "costs follow the event" approach, that is, the winning party should be awarded its costs.[989] The Tribunal notes, as do Claimants, that an increasing number of ICSID tribunals have considered this approach.[990]

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[985] Cl. PHB, ¶471.

[986] Cl. Reply, ¶368.

[987] Resp. C-M, ¶¶471-492

[988] See above at paragraph 829.

[989] Claimants' Submissions on Costs, ¶¶4-10; Respondent's Statement of Costs, ¶2.

[990] Claimants' Submissions on Costs, ¶¶7-9.

930. In view of the agreements of the Parties on this point, the Tribunal will take into consideration the overall outcome of these arbitral proceedings, in which Respondent has prevailed on the merits despite having lost on the issue of jurisdiction.

931. The Parties further agree that in awarding costs the Tribunal is entitled and should take into consideration specific aspects of the procedure and of the parties' conduct. According to Claimants, two (2) aspects of Respondent's conduct in particular should be sanctioned in any award of costs: (i) Respondent's unreasonable arguments in the arbitration, including as to the legality of the Services Agreement; and (ii) Estonia's "negative campaign against ASTV."[991]

932. Respondent, for its part, criticises Claimants for making their case a "moving target" especially with the filing of their Reply. Estonia recalls that, in its Counter-Memorial, it demonstrated that Claimants' economic expert, Mr. Meaney, had overstated ASTV's RAB in his first report by including the purchase price,[992] in response to which Claimants revamped their case by alleging that they had expectations regarding a 15-year tariff path, in lieu of alleging that the modification to the PWSSA was per se a breach of the FET standard. Respondent further criticises Claimants' submissions for their lack of clarity as to the alleged basis of their legitimate expectations and the contractual rights they were seeking to enforce.

933. By way of reply, Claimants recall that the error of their expert only related to a "cross-check" calculation, and did not affect their principal case. They also dispute that they changed their case accordingly.[993]

934. In the Tribunal's opinion, it is fair to say that Claimants appear to have adjusted their pleadings between the first and second rounds of submissions. In any event, the Tribunal considers that Claimants' case was characterised to a noticeable extent by a lack of consistency and precision in respect of certain key elements of both liability (in particular the nature of the alleged legitimate expectations) and quantum.

935. The Tribunal nonetheless agrees with Claimants that Respondent's arguments as to the legality of the Services Agreement, on which it did not prevail (and on which it arguably had limited chances of success in view of the findings of the Estonia courts), consumed significant time and effort. Moreover, Estonia's objection to the Tribunal's jurisdiction, including its several requests to brief certain aspects of the issue – notably in regard to *Achmea* – also added significantly to the time and costs of the arbitration.

936. The costs incurred by the Parties in relation to these proceedings may be broken down as follows:

[991] Claimants' Reply Submission on Costs, ¶¶15-17.

[992] Respondent's Statement of Costs, ¶3, referring to Resp. Rej., ¶¶2-5 and Resp. C-M, ¶¶231 and 232.

[993] Claimants' Reply Submission on Costs, ¶¶7-12.

Description	Costs Incurred
Claimants' legal and related costs (including disbursements, expert services and other costs related to the arbitration)[994]	EUR 5,207,672.06
Claimants' share of the advance on costs	USD 749,985.00
Respondent's legal and related costs (including expert services)[995]	EUR 1,997,966.77
Respondent's share of the advance on costs	USD 749,965.00

937. The arbitration costs include the fees and expenses of the Tribunal and the costs for the use of the facilities of the Centre, the exact amount of which shall be subsequently notified in writing to the Parties by the Centre.[996]

938. In the exercise of its discretion the Tribunal considers that Claimants should reimburse Respondent an amount equivalent to 25% of (i) its legal costs, fees and expenses as well as of (ii) the arbitration costs it incurred (i.e. the expended portion of Respondent's share of the advance on costs).[997]

[994] Claimants' Submissions on Costs, ¶12.

[995] Respondent's Submission on Costs, ¶¶9-12, 14-16.

[996] A detailed statement of account will be provided to the Parties.

[997] The final statement of account will show, inter alia, the expended portion of each Party's share of the advance on costs. The remaining balance on the case account will be reimbursed to the Parties in proportion to the advance payments that they made in the proceeding.

IX. AWARD

939. For the reasons set forth above, the Tribunal decides and orders:

(1) The Tribunal has jurisdiction over all claims presented in this arbitration;

(2) Claimants' claims for breach of the fair and equitable treatment standard under Art. 3(1) of the BIT are dismissed;

(3) Claimants' claims for breach due process under Art. 3(1) of the BIT are dismissed;

(4) Claimants' claims for breach of non-discrimination under Art. 3(1) of the BIT are dismissed;

(5) Claimants' claims for breach the umbrella clause at Art. 4(3) of the BIT are dismissed;

(6) Claimants shall pay Respondent an amount equivalent to (i) 25% of Respondent's legal costs, fees and expenses, plus (ii) 25% of the expended portion of Respondent's share of the advance on costs.

[signed]

Prof. Brigitte Stern
Arbitrator

Date: June 20, 2019

[signed]

Sir David A.R. Williams QC
Arbitrator

Date: June 20, 2019
Subject to the attached Dissenting Opinion

[signed]

Mr Stephen L. Drymer
President of the Tribunal

Date: June 20, 2019