

*This case summary was prepared in the course of research for
[S Ripinsky with K Williams, Damages in International Investment Law \(BIICL, 2008\)](#)*

Case summary

**Nykomb Synergetics Technology Holding AB
v
The Republic of Latvia**

Year of the award: 2003

Forum: Arbitration Institute of the Stockholm Chamber of Commerce

Applicable investment treaty: Energy Charter Treaty (1994)

Arbitrators Bjørn Haug, Chairman Rolf A. Schütze Johan Gernandt	Timeline of the dispute 11 December 2001 – request for arbitration 16 December 2003 – arbitral award
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I. Executive Summary

Nykomb, a Swedish company, acquired a Latvian subsidiary (Windau) in order to engage in the business of producing and supplying electric power in Latvia. In 1997 Windau entered into a contract with Latvenergo, a State-owned Latvian company and a sole purchaser and distributor of electricity through the national grid. Under the Contract, Windau undertook to construct a power plant and Latvenergo agreed to purchase the electric power from Windau at a price composed of two elements – the general tariff and a multiplier, both set by Latvian laws.

At the time of concluding the Contract, the Latvian law provided for a multiplier of two (a “double tariff”) to be paid during the initial eight years of plant operation. However, that law was modified in October 1998 to provide for 0.75 tariff. After the construction of the plant was finished in 1999, a dispute arose between Windau and Latvenergo about the proper price. Latvenergo refused to pay the double tariff and paid 0.75 tariff instead.

Nykomb initiated arbitral proceedings against Latvia under the Energy Charter Treaty (“ECT”) alleging that the non-payment of the double tariff violated several ECT obligations: on fair and equitable treatment, on arbitrary and discriminatory measures and others. Nykomb claimed damages that have arisen from the price difference both for the past period and for the remainder of 8 years, with the overall amount totalling approx. US\$ 12.8 million (expressed in Latvian currency).

Having examined both the Latvian legislation and the Contract, the Tribunal found that Latvenergo was obliged to pay the double tariff for the first 8 years of plant operation. The Tribunal also found that the non-payment of the double tariff was attributable to Latvia and that this non-payment was discriminatory (Latvenergo had paid the double tariff to two other Latvian producers of electric power). On this basis, the Tribunal concluded that Latvia breached Article 10(1) of the ECT prohibiting discriminatory measures.

The Tribunal found it inappropriate to apply the standard of compensation envisaged for expropriation cases and chose the route of monetary restitution. The Tribunal limited recoverable damages to the losses pre-dating the Award (with regard to the remainder of the 8 years, the Tribunal ordered Latvia to ensure the payment of the double tariff). Notably, the Tribunal did not accept that the investor, Nykomb, suffered the same amount of damages as its investment, Windau. At the same time, there was not enough data to calculate the exact loss suffered by Nykomb. Therefore, the Tribunal awarded, on a discretionary basis, only one third of the missing price difference to Nykomb (approx. US\$ 2.4 million). The Tribunal also awarded simple interest at the rate of 6% p.a. from the dates of breach until the date of payment.

II. Factual Background and Claims of the Investor

Nykomb Synergetics Technology Holding AB (“Nykomb”) is a Swedish company which acquired 100% interest in a Latvian company, SIA Windau (“Windau”). In March 1997, Windau entered into a contract with Latvenergo, a State-owned Latvian

company actively involved in the production of electric power in Latvia, as well as the sole purchaser and distributor of electricity through the national grid.

Under the Contract, Windau undertook to build a “cogeneration plant” in the town of Bauska, which was to produce electric power and heat on the basis of natural gas, the electric power to be purchased by Latvenergo and distributed over the national grid, and the heat to be purchased and distributed by the Bauska municipality. The price of electric power for Latvenergo was composed of two elements – the general tariff and a multiplier, both set in accordance with Latvian laws and regulations.

The dispute arose because according to the Claimant, Windau was guaranteed a multiplier of two (the “double tariff”) for the first eight years of operation, while Latvenergo considered the correct multiplier to be 0.75 of the tariff. The lack of clarity on this issue was due to the evolution of Latvian legislation. Without going into detail, at the time of the conclusion of the Contract, Latvian law provided for a double tariff to be paid during the initial 8 years of production. However, that law was modified in October 1998 to provide for 0.75 tariff.

Although the Bauska plant was built by Windau and was ready to start production in September 1999, it did not start until 28 February 2000 due to a mentioned price dispute between Windau and Latvenergo (“deadlock period”). Since 28 February 2000 the Bauska plant was delivering electric power to Latvenergo according to an interim or settlement agreement of 10 March 2000, at a price of 0.75 tariff, with the remaining part of the double tariff being paid to an escrow account pending the resolution of the price dispute.

In December 2001, Nykomb initiated arbitration proceedings against Latvia claiming several violations of the Energy Charter Treaty (hereinafter “ECT”) (signed 1994, in force 1998), including provisions on expropriation (Article 13(1)), fair and equitable treatment standard, treatment less favourable than required by international law, impairment by unreasonable or discriminatory measures (Article 10(1)). Nykomb argued that the treaty breaches attributable to Latvia caused the following losses totalling approx. 7 million Lats:¹

- During the deadlock period, 17 September 1999 – 28 February 2000, when no energy or heat was generated (667,158 Lats);
- Loss of income during the period 28 February 2000 – 16 September 2002 calculated on the basis of the actual production during that period (2,311,020 Lats);
- Loss of income in the rest of the 8 years’ period, 16 September 2002 – 16 September 2007, calculated on the basis of the 2001 production volume and discounted at 6% per annum (4,119,502 Lats).

Except for the deadlock period, the claimed amounts were calculated on the basis of a price at a double tariff, less the price at 0.75 of the tariff actually paid by Latvenergo to Windau. In other words, the amounts claimed were equal to Windau’s alleged loss of net income for non-delivered heat and electricity in the deadlock period plus Windau’s alleged loss of income for the period after 28 February 2000 due to the fact that Latvenergo has only paid 0.75 of the tariff for delivered electricity.

¹ Approx. US\$ 12.8 million (using the exchange rate at the time of writing the summary).

III. Findings on Merits²

A. Correct Price

After analysing the facts, the Tribunal concluded that the Contract had to be interpreted as fixing the multiplier in effect at the *moment of signing* the Contract. Specifically, the Tribunal found that Windau had both a statutory and a contractually established right to the double tariff for an eight year period. (p.29)

The Tribunal's conclusion was supported, *inter alia*, by judgements of Latvian courts, including the Latvian Supreme Court, in a similar price dispute between Latvenergo and Latelektro-Gulbene Ltd, another independent electricity producer. Relevant court decisions reaffirmed the right of Latelektro-Gulbene to a double tariff. Following the Supreme Court decision in that case, in October 2001 Latvenergo entered into a new agreement with Latelektro-Gulbene clearly assuming the double tariff in the first eight years.

B. Attribution to the State

The Tribunal reasoned that for State responsibility to arise, the “non-payment [of the double tariff] must be caused directly by the Republic or a state organ, or Latvenergo's actions in the contractual relationship with Windau must be attributable to the Republic”. (p.29)

The Tribunal considered that the reason for Latvenergo's refusal to pay was the repeal of the statutory right to the double tariff (Latvenergo had no authority of its own to decide or negotiate purchase prices). Therefore the Tribunal assumed that “Latvenergo felt it to be its duty to deny Windau the double tariff after the legislators' decision to repeal Windau's established statutory right to the double tariff.” (p.30) According to the evidence before the Tribunal, the Latvian government had been fully aware of Latvenergo's refusal to pay the double tariff and, therefore, the Tribunal concluded that “the breach of Windau's contractual rights was allowed to continue, and in that sense was caused, by the government's failure to act in order to correct the situation.” (p.30)

Finally, the Tribunal found that Latvia must be considered responsible for Latvenergo's actions under the rules of attribution in international law because Latvenergo was fully owned and controlled by the State and “clearly an instrument of the State in a highly regulated electricity market” and a “vehicle to implement the Republic's decisions concerning the price setting for electric power.” (p.31) Consequently, Latvenergo's actions concerning the purchase price were attributable to the Republic and the latter must be found responsible for Latvenergo's failure to pay the double tariff. (p.31)

² Before proceeding to the merits, the Tribunal affirmed its jurisdiction over the claims.

C. Unreasonable and Discriminatory Measures

The Claimant contended that Windau had been subject to a discriminatory measure because Latvenergo had been paying the double tariff to two other companies in Latvia. The Tribunal determined that Windau was comparable to these other companies but subject to different treatment, therefore it found Latvia had acted in a discriminatory fashion in violation of Article 10(1) of the ECT. (p.34)

D. Expropriation and Other Claims

The Tribunal found that there had been no expropriation of the investment because there had been no taking of Windau or its assets, no interference with the shareholder's rights or with the management's control over the enterprise. (p.33)

The Tribunal considered that in order to establish Latvia's liability, it was sufficient to find a violation of one of the relevant provisions because multiple violations would not change the amount of the damage or loss caused by the non-payment of the double tariff. Having found that the non-payment of the double tariff was discriminatory, the Tribunal decided not to adjudge the other ECT violations asserted in the arbitration. (p.34)

IV. Findings on Damages

A. Law Applicable to the Determination of Damages

In its award of damages, the Tribunal applied the ECT and international law.

B. Standard of Compensation

The ECT spelt out the principles of compensation only in relation to cases of expropriation (Article 13(1)) and the Tribunal decided that those principles were not applicable to the assessment of damages caused by other treaty violations. Instead, the Tribunal resorted to customary international law which it considered to be authoritatively restated in the ILC Draft Articles on State Responsibility. (p.38)

In particular, the Tribunal referred to Draft Articles 34 and 35 which imposed on a responsible State an obligation to "make restitution, that is, to re-establish the situation which existed before the wrongful act was committed". The Tribunal decided that a monetary restitution was an appropriate remedy in that case; the assessment had to be made on the basis of the difference between the contractually established double tariff and 0.75 of the tariff actually paid.

C. Damages Claimed

As noted above, Nykomb requested a relief equal to Windau's alleged loss of net income on heat and electric power in the "dead-lock" period, 16 September 1999 – 28 February 2000, and Windau's alleged loss of sales income on electric power for the rest of the eight years' period to 16 September 2007, namely the difference between the double tariff and the 0.75 of the tariff actually paid, or expected to be paid.

D. Damages Awarded

The Tribunal limited compensation to damages suffered by Nykomb up to the time of the Award and declined to compensate future damages. Instead, the Tribunal ordered Latvia to pay the double tariff for the remainder of the eight years. (p.41)

As regards, the quantum of damages suffered up to the date of the award, the Tribunal reasoned as follows.

1. Damages to the investment v. damages to the investor

First, the Tribunal found that the reduced flow of income into Windau did not cause an identical loss for Nykomb as an investor:

“[I]t is clear that the higher payments for electric power would not have flowed fully and directly through to Nykomb. The money would have been subject to Latvian taxes etc., would have been used to cover Windau's costs and down payments on Windau's loans etc., and disbursements to the shareholder would be subject to restrictions in Latvian company law on payment of dividends. An assessment of the Claimant's loss on or damage to its investment based directly on the reduced income flow into Windau is unfounded and must be rejected.” (p.39)

This quote suggests that the damages to the investor must be something less than a difference between the double tariff and the 0.75 tariff multiplied by volume of electricity supplied.

2. Loss of the investor (Nykomb)

In spite of its finding that the damages did not flow to the investor in full, the Tribunal stated that “the non-payment of the double tariff to Windau has caused a *substantial reduction of the economic value* and security of the Claimant's investments in the Windau enterprise.” (p.39, emphasis added) The Tribunal reasoned that “a substantial reduction of Windau's earnings as demonstrated in this case must be considered as

convincing evidence that a substantial damage to or loss on the Claimant's investment has been suffered.” (pp. 39-40)

The Tribunal also noted positive effects that a payment of the double tariff would have brought to both Windau and Nykomb. For Windau, “the higher income flow would have served to consolidate [its] financial position, provided means for paying back bank loans and other credits, and ensured a quicker pay-back on the investments in the cogeneration plant. For Nykomb as an investor the effect would be increased security for its investments in credits, shares and subordinated loans.” (p.40)

However, the Tribunal admitted that it was difficult to quantify the loss suffered by Nykomb as an investor. This difficulty was aggravated by the “rather limited” documentation presented by the Claimant. (p.40) In these circumstances, the Tribunal said it was “compelled to make an assessment, taking into regard the requirements under applicable customary international law of *causation, foreseeability and the reasonableness of the result.*” (p.41, emphasis added)

The Tribunal decided that a “*discretionary award* of one third of the estimated loss in purchase prices of electricity up to the time of this award may serve as a reasonable basis for quantification of the Claimant’s assumed losses up to the time of this award” (p.41, emphasis added). On this basis, the Tribunal assessed a compensation of Lats 1,600,000³ as reasonable (this figure also includes interest up to the date of the Award, see below). (p.41)

Finally, the Tribunal stated that in its assessment and award it used the Latvian currency (Lats) because this is the currency that the Claimant had used in its prayer for relief. (p.41)

E. Claim for Future Profits

Regarding the claim for future losses (from the date of the Award for the remainder of the 8-year period), the Tribunal considered that claim to be “too *uncertain and speculative* to form the basis for an award of monetary compensation”. As noted above, instead of providing relief on this claim, the Tribunal ordered Latvia “to ensure the payment at the double tariff for electric power delivered under the Contract for the rest of the eight year period”. (p.41)

F. Interest

The Tribunal referred to Article 26(8) of the ECT which provided that arbitral awards may include an award of interest. The Tribunal found it “reasonable” to award *simple* interest at the rate of 6% p.a., both for pre-award and post-award interest. The Tribunal mentioned that the rate of 6% was accepted by parties as a “prevailing rate in Latvia”.

³ Approx. US\$ 2.4 million (using the average exchange rate at the time of writing the summary).

Nykomb claimed the post-award interest at the rate of 18% – the rate stipulated in the Contract between Windau and Latvenergo in the event of late payment. However, the Tribunal stated that that rate was inapplicable to the compensation to the Nykomb for its own damages (not to Windau) under the ECT.

G. Costs

The Tribunal decided that arbitration costs should be borne by parties in equal shares. As regards the expenses for legal representation, the Tribunal took into account that the Claimant was successful on liability and awarded a “reasonable amount” of SEK 2,000,000 (the claimed amount of SEK 8,354,000 was considered too high).

V. Implications/ Initial Analysis

- Where the damages are caused by a **single measure**, it does not play a role whether the measure is in violation of one or several of treaty obligations.
- The Tribunal declined to apply the **expropriation standard of compensation** in this non-expropriation case. Presumably, this is because the ‘fair market value’ standard would not be helpful, as there was nothing to value. Apparently, the application (or non-application) of the expropriation standard in non-expropriation cases depends on circumstances of a particular case, i.e. on the type of damage caused to the investor. In this case, the investment did not “sink” completely but remained a “going concern”.
- The Tribunal accepted that the **Draft Articles on State Responsibility** were a restatement of customary international law on issues of damages and compensation.
- This case raises a point of the **flow of damages** from the investment to the investor and suggests that damages suffered by the investor may be different from (less than) those suffered by the investment. Nykomb requested payment of 100% of the difference between what was contractually due and what was actually paid - for the past and the future - to itself. It relied on the theory of the “**economic unity**” of the investment enterprise and the parent investor (contrary to the ICJ *Barcelona Traction* judgement). The Tribunal, however, effectively rejected the theory of the “economic unity” and chose to award only the **indirect damages** suffered by the investor – a discretionary 1/3 of the missing difference between what was paid and what was due.
- The Tribunal suggested that **causation, foreseeability and the reasonableness of the result** were requirements under customary international law in relation to quantification of damages. It appears that in practice, the Tribunal did not consider (or at least, it did not discuss) causation and foreseeability but based its award on its view of what was reasonable. The Tribunal also applied the test of reasonableness for interest and costs.
- **Proper currency** of the award – the Tribunal followed the Claimant’s prayer for relief. (This is OK if the respondent does not object?)

- The claim for future profits was rejected as too **uncertain** and **speculative**. Instead, the Tribunal ordered Latvia to comply with the Contract in future (by paying the double tariff). This is an example of application of two different remedies (compensation and specific performance) in conjunction with each other.
- **Simple** interest awarded, without discussion. Contractual interest rate (18%) rejected because the parties to the dispute were different from the parties to the contract.