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GERMAN FIRM FAILS TO PASS JURISDICTIONAL HURDLE IN CLAIM AGAINST ARGENTINA; DECISION PROVOKES QUESTIONS ABOUT THE SCOPE AND APPLICABILITY OF MFN PROTECTION

By Elizabeth Whitsitt

An ICSID tribunal has declined jurisdiction in a claim brought by a German firm against the government of Argentina, in a decision that highlights the unpredictability over whether a claimant can invoke a Most-Favoured-Nation (MFN) clause to access an expedited arbitration process.

The claimant, Wintershall Aktiengesellschaft, alleged that the Argentine government took measures which negatively impacted its oil and gas operations by: (i) preventing it from receiving dividend payments from its Argentine subsidiary (ii) impairing the legal and contractual rights of its Argentine subsidiary, and (iii) violating a number of the substantive protections afforded investors under the Argentina–Germany bilateral investment treaty (BIT), including the prohibition against direct or indirect, expropriation.

Notwithstanding a provision in the Argentina-Germany BIT that requires disputes to first be brought to the Argentine courts, Wintershall submitted its claims directly to arbitration. Invoking the MFN clause in the Argentina-Germany BIT, the company argued that it was entitled to utilize what appears to be more favourable dispute settlement procedures found in the Argentina-United States BIT.

Finding that it did not have jurisdiction to hear the case, the tribunal based its determination on two primary findings: (1) that the claimant could not avoid prior compliance with the procedural requirements in the Argentina-Germany BIT before initiating arbitration proceedings and (2) that the Claimant could not rely on the most-favoured-nation clause in Article 3 of the Argentine-Germany BIT to avoid compliance with those requirements.

> *"The ruling of the tribunal confirms, however, that nothing is certain or predictable when it comes to examining the scope and applicability of MFN protection in international investment law."*

The tribunal focused, in its 8 December 2008 decision, on the clear language of the text of Article 10(2) in the Argentina-Germany BIT and stated:

> " manner in which Article 10 of the BIT is worded (and it is words that determine the intention of the Parties when interpreting a treaty) it is apparent that reference to

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ARGENTINA TAKES THE OFFENSIVE AS SIEMENS ADMITS TO CORRUPTION

By Damon Vis-Dunbar

Argentina has refused calls by Siemens to suspend proceedings at the International Centre for the Settlement of Investment Disputes (ICSID) in which a committee is considering Argentina's request to revise a 2007 award, following the admission that the firm's Argentinean subsidiary paid government officials in order to obtain a lucrative contract.

On 15 December 2008, Siemens AG, a German corporation, acknowledged that its employees paid government officials in several countries in order to win contracts, and fudged internal records to hide the payments. In a deal struck with U.S. and German authorities, Siemens will pay US$1.36 billion in penalties.

Among the confessions was that Siemens' Argentinean subsidiary colluded with government officials in order to obtain a contract for a US$1 billion national identity card project.

When that contract was cancelled in 2001, Siemens responded by filing a claim for violations of the German-Argentina bilateral investment treaty. Some six years later, the tribunal awarded Siemens US$217 million in damages.

"Among the confessions was that Siemens' Argentinean subsidiary colluded with government officials in order to obtain a contract for a US$1 billion national identity card project."

Argentina is attempting to have the award revised, and will no doubt use the Siemens' confession to bolster its argument that the award should not stand.

Argentina had raised the issue of corruption during the arbitration proceedings, although an effort to submit evidence on the matter was rejected by the tribunal, on the grounds that Argentina had waited too long to do so.

However, since the 2007 award various investigations and court proceedings in the United States and Germany brought strength to the corruption allegations. In the summer of 2008, a Siemens official admitted in a German court to paying illegal fees to government officials in Argentina. Based on this new evidence, Argentina submitted a request to ICSID for a revision of the award, pointing to several investment treaty cases in which tribunals have declined jurisdiction on the grounds that the investment was not made in accordance with domestic laws.

Under ICSID rules, a party can request a revision to an award "on the ground of discovery of some fact of such a nature as decisively to affect the award, provided that when the award was rendered that fact was unknown to the Tribunal and to the applicant and that the applicant's ignorance of that fact was not due to negligence."

Following its admission on 15 December 2008, Siemens wrote to the ICSID committee hearing Argentina's request for a revision to the 2007 award, asking for a three-month suspension of the proceedings. However, Argentina has declined this invitation, telling the committee that it wishes to see proceedings continue without delay.

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ICSID arbitration is expressly conditioned upon *inter alia* a claimant-investor first submitting his/its dispute to a Court of competent jurisdiction in Argentina, during an 18–month period (and a three month further waiting period) and then proceeding to ICSID arbitration.

[...]

In the present case the Contracting Parties, (i.e. the Republic of Argentina and the Federal Republic of Germany) have been left free to provide, (and have specifically provided for) a local-remedies clause before resorting (ultimately) to ICSID arbitration. Since the Claimant (a German national) can only make a claim under the Argentina-Germany BIT, and under no other document, when the Claimant Wintershall so makes a claim (as it has done in the present case) it has no option but to comply with the closely interlinked conditions mentioned in Article 10, before exercising its right to ICSID arbitration, simply because that is the expressed will of the Contracting States."

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PERU WINS DISPUTE WITH AMERICAN ENERGY FIRM OVER THE SCOPE OF A STABILIZATION AGREEMENT

By Fernando Cabrera Diaz

The Republic of Peru has defended itself successfully against a claim initiated by Delaware-based Aguaytia Energy LLC (AEL). AEL had sought US$142 million as compensation for what it claimed was Peru's violation of a stabilization agreement. However, in an 11 December 2008 decision, the tribunal disagreed and instead held that the stability agreement did not provide for the substantive rights that the investor was claiming.

In the early 1990s, as Peru privatized its hydrocarbon and the electric power sectors, so-called legal stability agreements were offered to investors, under which the state promised to keep certain rules and judicial frameworks, such as tax codes, stable for a given number of years.

The claimant, through its Peruvian subsidiary, invested in the Aguaytia integrated energy project, a natural gas development project in the Aguaytia gas fields of eastern Peru, which contain an estimated 302 billion cubic feet of recoverable gas reserves. In addition to an agreement to exploit the gas field, electricity generation and transmission concessions, Aguaytia agreed to a legal stability agreement in which Peru guaranteed the stability of the tax system, the right to free remittances, and the right to non-discrimination, among other things.

This last guarantee—stability of the right to non-discrimination—was at the crux of the dispute. According to the claimant, Peru violated this guarantee when it offered a more advantageous investment model to 'favoured investors'. In particular, AEL refers to a Build, Operate, Own and Transfer (BOOT) concession which Peru, after an international tender process, awarded to the Colombian energy firm ISA in 2001.

Under the ISA BOOT Concession, ISA assumed obligations for constructing transmission lines and in turn received various incentives, including a stable remuneration scheme, independent of the actual load flow of electricity. In light of the ISA BOOT contract, AEL sought to have its transmission lines re-classified in order to take advantage of the same remuneration scheme, first through Peruvian administrative channels and then domestic courts.

"The issue of stability agreements was recently taken up by a tribunal in an ICSID arbitration, Duke Energy vs. Peru. As reported previously by ITN, in an August 2008 decision, that tribunal adopted a more expansive view of stability agreements in the context of tax stabilization, by providing substantive protections."

While AEL was partially successful, certain issues, including the classification of two of its lines, were not decided to its satisfaction, leading to AEL's ICSID claim, registered in May 2006. In its claim, AEL argued that the guarantee of the stability of the right to non-discrimination included substantive protection against discrimination in the treatment of investors, such as the BOOT Concession investor.

Peru, however, maintained that the Stability Agreement guaranteed the stability of the right to non-discrimination as set out by Peruvian law, but no separate substantive right to non-discrimination. Ultimately the tribunal sided with Peru, and held that the provision in question only guaranteed that the specified Peruvian laws protecting against discrimination would not be modified as they applied to AEL during the term of the Agreement, rather than creating a substantive protection against discrimination.

This finding, according to the tribunal, ended the matter "because the Claimant asserts no case based on detrimental legislative or other legal framework change, and it is common ground that the Peruvian courts, and not this Tribunal, have jurisdiction over any alleged breach by the state of its anti-discrimination laws."

It is "clear from the wording of the Agreement that the guarantees it contains concerning juridical stability do not convey a most favored investor status," added the Tribunal.

On costs, the tribunal followed the language of the Stability Agreement and concluded that each side must pay its own legal costs and their share of ICSID arbitration fees.

White & Case partner Jonathan C. Hamilton, who represented Peru, said that the Tribunal's decision affirmed that stability agreements reduce the political risk of investing in emerging markets by freezing certain existing laws for a fixed period of time, but do not create new substantive rights.

The issue of stability agreements was recently taken up by a tribunal in an ICSID arbitration, Duke Energy vs. Peru. As reported previously by ITN, in an August 2008 decision, that tribunal adopted a more expansive view of stability agreements in the context of tax stabilization, by providing substantive protections. Duke Energy controls AEL.

EL SALVADOR WARNED OF CAFTA-DR LAWSUIT BY MINING COMPANY

By Damon Vis-Dunbar

A Canadian mining company and its American subsidiary have threatened the government of El Salvador with a lawsuit after it failed to receive regulatory approval to begin digging for gold and silver in an area some 65 km from San Salvador. The proposed mine has drawn intense opposition from civil society and church-based groups, although the mining company maintains that it enjoys broad public support in El Salvador.

Pacific Rim, a company head-quartered in Vancouver, has explored its El Dorado property for metals, but, like other potential mines in the El Salvador, it has not been granted license to begin mining as the government wrestles over proposed changes to the country's mining laws.

On 9 December 2008, Pacific Rim and its Nevada-based subsidiary, Pac Rim Cayman LLC, served El Salvador with a Notice of Intent under the Dominican Republic – Central America – United States Free Trade Agreement (DR-CAFTA), setting in motion a 90-day cooling-off period before the companies can serve a claim.

Pacific Rim invested US$77 million exploring El Dorado on the pretence that a permit to mine was eminent, said the company's President and CEO, Tom Shrake, in a conference call. The company will seek hundreds of millions of dollars in lost profits if the dispute proceeds to arbitration, said Shrake.

"In July 2008, Oxfam America published a report that threw doubt on the economic benefits that derive from mining sector in El Salvador, noting that manufacturing is up to 50 times more important than mining in terms of its contribution to the country's GDP. "

During the same conference call, Shrake lashed out at non-governmental organizations, including Oxfam America, for their opposition to the mine, calling their resistance "anti-development".

In July 2008, Oxfam America published a report that threw doubt on the economic benefits that derive from mining sector in El Salvador, noting that manufacturing is up to 50 times more important than mining in terms of its contribution to the country's GDP. Some civil society groups say that Pacific Rim's proposed mine would also compete for scarce water supplies and pollute rivers that cross large swathes of Central America.

Counsel for Pacific Rim, Timothy McCrum of Crowell & Moring, LLP, who also took part in the 9 December conference call, said that the NAFTA case Metalclad v. Mexico set a positive precedent for Pacific Rim.

Metalclad, a California-based company, sued the government of Mexico after it was denied a permit to construct a hazardous waste landfill by a municipality. The landfill faced opposition from the local community, who feared that it would lead to health problems in the area.

In a decision that sparked some controversy, the Tribunal held in 2000 that Mexico failed to provide transparent rules and procedures when it decided to not approve Metalclad's permit. Metalclad was awarded some US$16 million for actions on the part of Mexico that were deemed tantamount to expropriation.

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In determining that the Wintershall could not overcome the unambiguous language in Article 10(2) by virtue of the MFN clause, the tribunal made a number of findings. Of particular interest is the tribunal's reasoning respecting the importance of consent as the foundational principle upon which its jurisdiction is grounded. In response to the claimant's assertion that the application of the MFN clause in the Argentine-Germany BIT did not affect issues of jurisdiction, consent to arbitration or the substance of the dispute settlement mechanism, the tribunal noted that the 18-month requirement to pursue local remedies in Article 10(2) "is part and parcel of Argentina's integrated 'offer' for ICSID arbitration; this 'offer' must be accepted by the investor on the same terms."

The tribunal also noted that the dispute resolution clause in Article 10 of the Argentina-Germany BIT provides for ICSID as the ultimate and only arbitration forum, whereas Article VII of the Argentina-US BIT invoked by the claimant (in lieu of Article 10 of the Argentina-Germany BIT) prescribes "a different system of arbitration" because it provides an investor a choice of

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MERITS OF INVESTOR-STATE ARBITRATION DEBATED AT INTERNATIONAL ARBITRATION SEMINAR HOSTED BY ECUADOR'S ATTORNEY GENERAL

By Fernando Cabrera Diaz

On 1-2 December Investment Treaty News attended a two-day seminar on international arbitration in Quito, Ecuador, hosted by Ecuador's Attorney General's Office. The seminar focused on international investment arbitration and its relation to state sovereignty.

Opinions from different sides of the debate were voiced, including from Ecuadorean government officials and international lawyers and arbitrators representing some of the most respected law firms in the field.

Ecuador's Attorney General Diego García Carrión opened the seminar by noting that investment arbitration had recently attracted a lot of press Ecuador.

In the past year, Ecuador has attempted to withdraw its natural resource sectors from the jurisdiction of the World Bank's International Centre for Settlement of Investment Disputes (ICSID), terminated multiple bilateral investment treaties (BITs) and adopted changes to its constitution, notably Article 422, which makes it unconstitutional for the Andean nation to submit itself to arbitration unless it is with a Latin American citizen and in a Latin American forum.

The seminar was staged in order to inform Ecuador's in-house legal team about investment treaty arbitration, as well as to clarify Ecuador's position with respect to its actions in the field, explained García. The Attorney General attempted to dispel the notion that Ecuador was anti international arbitration, pointing out that the government was defending itself in a number of investor claims and had even initiated an arbitration claim of its own against Brazil's state-bank.

ITN asked García about Ecuador's recent move to withdraw from over a dozen BITs. Mr. García explained that the decision to terminate the BITs was not due to any dislike for or unwillingness to sign BITs on the part of Ecuador. Rather, the decision was made solely for the reason that these BITs were determined not to have helped attract foreign investment into Ecuador.

"In the past year, Ecuador has attempted to withdraw its natural resource sectors from the jurisdiction of the World Bank's International Centre for Settlement of Investment Disputes (ICSID), terminated multiple bilateral investment treaties (BITs) and adopted changes to its constitution, notably Article 422, which makes it unconstitutional for the Andean nation to submit itself to arbitration unless it is with a Latin American citizen and in a Latin American forum."

When asked whether Ecuador would be renegotiating its existing BITs to conform to Article 422, Mr. García said it was an issue that would be decided by Ecuador's Executive, not his office. He also refused to speculate on whether Ecuador would be signing new BITs in the future.

Prominent lawyer and former Ecuadorean Supreme Court Justice Dr. Alberto Wray, another speaker at the seminar, took Ecuador to task for its constitutional changes that attempt to curb arbitration suits against the state from outside Latin America. He said investor-state arbitration could not exist without the consent of the state in the first place, and so it should not infringe on state sovereignty.

Dr. Wray acknowledged, however, that there were some problems raised by investor-state arbitration, given that the jurisprudence in this area is relatively young. One of the problems he noted was the challenge in determining which types of indirect expropriation required compensation and which should not.

This issue had come to the fore in the high-profile NAFTA cases of Methanex Corp. v. the United States and Metalclad v. Mexico: arbitrations that have been used as examples to argue that investor-state arbitration was a threat to governmental policy space. Dr. Wray said tribunals were deciding such claims on a case-by-case basis as opposed to adopting a general theory.

However, Dr. Wray called the path adopted in Article 422 of Ecuador's Constitution, which was approved by a September referendum, an overreaction to these sorts of uncertainties. Instead, he favoured drafting future BITs and arbitration agreements to include clauses similar to the one found in the Dominican Republic-Central American Free Trade Agreement (CAFTA-DR), which better clarify the limits of indirect expropriation.

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TRIBUNAL REJECTS ECUADOR'S JURISDICTIONAL OBJECTIONS IN DISPUTE WITH CHEVRON

By Fernando Cabrera Diaz

A tribunal has determined that it holds jurisdiction to hear a claim brought by Chevron Corporation against Ecuador for alleged violations of the Ecuador-United States bilateral investment treaty (BIT).

Chevron claims that Ecuador violated the BIT by failing to deal fairly with multiple breach-of-contract cases filed against the state by Texaco Petroleum (Chevron acquired Texaco in 2001.)

From the outset Ecuador objected to the tribunal's jurisdiction, in part by arguing that Chevron's claim amounts to an abuse of right. Ecuador accuses Chevron of using the arbitration to discredit Ecuador's judiciary in order to undermine a potential award against it in a court case in Lago Agrio, Ecuador.

The Lago Agrio claim is led by a group of Ecuadorian citizens for alleged environmental degradation caused by the Texaco's drilling activities. These citizens had originally filed a claim in the United States (*Aguinda v. Texaco*), but Texaco convinced U.S. courts that the Ecuadorean courts are the proper forum for settling the dispute.

Despite its earlier endorsement of the Ecuadorian judiciary, as Chevron argued in favour of having the Aguinda case moved to Ecuador, the company alleges that since 2004 the Ecuadorean courts have ceased to be independent in the wake of several political purges of Ecuador's Constitutional, Electoral and Supreme Courts.

Giving Chevron the benefit of the doubt, the tribunal's 1 December 2008 jurisdictional decision states that it could not "exclude the possibility that subsequent developments or other factors sufficiently explain any potential conflicts between the submissions before the U.S. courts and those before this Tribunal about the fairness of Ecuadorian courts."

Among the other jurisdictional objections, Ecuador argued that the claimant's investments were wrapped up well before 1997, the year the BIT entered into force. The tribunal also rejected this position, holding that while Texaco had concluded its drilling operations before 1997, the claims before Ecuadorian courts constituted part of the investment, and therefore fell under the BIT's jurisdiction.

Mark Clodfelter, counsel for Ecuador, told ITN: "While we are disappointed in the decision, we are gratified that the Tribunal wishes to further consider the issues of Chevron's and Texaco's abuse of rights in having praised the Ecuadorian judicial system for so many years to obtain dismissal of cases against them in U.S courts."

The Chevron-Ecuador dispute is rooted in a 1973 contract between Texaco and Ecuador, under which Texaco was granted exploration and exploitation rights to several oil reserves in the country. Texaco agreed to sell Ecuador a share of the crude oil to meet domestic consumption needs, at a set price, while any excess crude was to be sold by the company at the higher prevailing international price.

Between 1990 and 1993, Texaco filed seven breach-of-contract claims against Ecuador and its state organs, alleging that the country had violated the 1973 contract by overstating domestic consumption needs.

"Ecuador alleges that since 2004 the Ecuadorean courts have ceased to be independent in the wake of several political purges of Ecuador's Constitutional, Electoral and Supreme Courts."

According to Chevron, in a series of six cases Texaco took all necessary steps under Ecuadorean law to demand final decisions from Ecuadorean courts. Yet, the company alleges that twelve different judges in three different courts have so far failed to render a decision. Meanwhile, since Chevron's notice of arbitration was provided to Ecuador in May of 2006, the company alleges that politically controlled courts have unjustly ruled against it in several of its cases.

Ecuador has countered that "what Chevron portrays as bona fide lawsuits were in fact, as its own internal documents show, commenced solely to obtain tactical advantage in its negotiations with the Republic while it was withdrawing completely from the country.

"The delays that Chevron portrays as aimed at [Texaco] were in fact the ordinary delays suffered by derelict plaintiffs of all nationalities in Ecuador's overtaxed judicial system," adds Ecuador.

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fora (either ICSID or UNCITRAL) in which to settle its disputes. As a result, the tribunal found that it could reject the claimant's arguments respecting the scope and applicability of MFN protection. In so finding, the tribunal stated:

> ...[A] different dispute settlement provision under another treaty, whether or not "alien" to the basic treaty, is sufficient to negate the submission that the most-favoured-nation clause (in Article 3) applies to dispute resolution justifying abandoning the dispute resolution clause in the Argentine – Germany BIT and adopting Article VII of the Argentine – US BIT.

Given that previous arbitral tribunals had granted investors direct access to arbitration in the face of similar procedural hurdles, the claimant's attempt to invoke MFN protection in this case might have seemed to some an easy and predictable jurisdictional question to answer[1]. The ruling of the tribunal confirms, however, that nothing is certain or predictable when it comes to examining the scope and applicability of MFN protection in international investment law.

[1] See e.g. *Emilio Agustin Maffezini v. Kingdom of Spain* (2003), 124 I.L.R. 9 (International Centre for Settlement of Disputes), (Arbitrators: Francisco Orrego Vicuña, Thomas Buergenthal, Maurice Wolf), also online: WorldBank <http://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=showDoc&docId=DC565_En&caseId=C163 [*Maffezini*]; *Siemens AG v. Argentine Republic* (3 August 2004), ARB/02/8 (International Centre for Settlement of Disputes), (Arbitrators: Dr. Andrés Rigo Sureda, Judge Charles N. Brower, Professor Domingo Bello Janeiro), online:WorldBank <http://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=showDoc&docId=DC508_En&caseId=C7> [*Siemens*].

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Annex 10C of CAFTA-DR states that "Except in rare circumstances, nondiscriminatory regulatory actions by a Party that are designed and applied to protect legitimate public welfare objectives, such as public health, safety, and the environment, do not constitute indirect expropriations."

When asked what would happen to BITs and arbitration agreements signed before the new constitution in light of Article 422, Dr. Wray responded: "Nothing. They must be withdrawn or terminated to be made void."

Meanwhile, a prominent Paris-based lawyer and arbitrator, who asked to remain anonymous, criticized what he viewed as the liberal application of BIT protections by certain international tribunals. In particular, this person blamed what he called the artificial distinction made by tribunals between treaty and contract claims for creating a situation where governments could no longer rely on dispute settlement mechanisms in contracts.

He cited several examples in which foreign companies had contractually agreed to limit themselves to resolving disputes through national courts, only to then seek international arbitration under a BIT when they were unhappy with results. In such cases, it was common for international tribunals to overlook the terms of the relevant contract and accept jurisdiction by artificially dividing claims into contract and treaty components. It used to be said that states simply needed to negotiate good contracts to protect their sovereignty, but that is no longer the case, he said.

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