Recent Developments in Energy Arbitration

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Recent US Supreme Court Decisions on Class Action Arbitration

- **AT&T Mobility v. Concepcion** (2011) — Supreme Court invalidated a state law that conditioned enforceability of an arbitration clause on the availability of class arbitration.

- **Oxford Health Plans v. Sutter** (2013) — Supreme Court held arbitrator’s decision that class arbitration could proceed could not be vacated since the parties agreed an arbitrator would decide if their agreement allowed class arbitration.

- **American Express v. Italian Colors Restaurant** (2013) — Courts may not invalidate contractual waiver of class arbitration under FAA because individual costs of pursuing claim would exceed recovery, but courts might invalidate arbitral clause if the arbitral filing and administrative fees are so high as to make access to arbitration impractical.

Arbitrability of Investment Disputes Under BITs in US Courts

- BG Group obtained a $185 million Award against Argentina in a UNCITRAL Rules arbitration in the USA.
- UNCITRAL Rules provide that arbitrators decide jurisdiction issues.
- BG did not file an Argentine case before the BIT arbitration.
- Arbitrators decided government decree prevented filing of Argentine case.
- DC Circuit vacated the Award, holding the BIT provides for filing a lawsuit in Argentina and waiting 18 months as a precondition to filing a BIT arbitration, and held this is a gateway issue to be decided by the courts.
- Professors’ and Practitioners’ Amicus Brief supported granting certiorari because the UNCITRAL Rules provides that arbitrability is an issue for the arbitrators to decide.
- US Solicitor General recommended the Court deny cert.
- US Supreme Court granted cert — Dec. 3 argument set.
Recent 5th Circuit Decisions

• In an issue of 1st impression for the 5th Circuit, it held that a showing of personal jurisdiction is necessary to confirm a foreign arbitral award against award debtor
  – First Inv. Corp. v. Fujian Mawei Shipbuilding, 703 F. 3d 742 (2012)

• In a drilling dispute, 5th Circuit upheld an award based on a settlement agreement when the award amount did not provide an offset for installment payments made and award debtor agreed to waive any challenge to award

BIT Arbitration Decisions
Expropriation of Oil Concessions

• ConocoPhillips v. Venezuela (2013)
• Burlington v. Ecuador (2012)
• Occidental v. Ecuador II (2012)
• Mobil v. Venezuela (pending)
• Repsol v. Argentina (pending)
Expropriation


- Venezuela required oil companies to “migrate” their contracts to a mixed company with PDVSA as majority owner and took over ConocoPhillips’ interests when it failed to agree
- ConocoPhillips filed an arbitration under the Dutch BIT
- Tribunal held: Venezuela had a duty of “good faith negotiations to fix the compensation” consistent with the BIT’s market value standard
- Tribunal noted Venezuela’s approach to compensation was based on book value rather than market value and held Venezuela was “not negotiating in good faith”
- Venezuela was held to have violated the BIT’s compensation section, and the Tribunal held the valuation date would be the date of the award (not the date of the taking) because it was an “unlawful” taking
- Quantum phase pending

Expropriation

Burlington v. Ecuador (2012)

- Expropriation = “substantial deprivation” of property rights
- Majority decision — no “substantial deprivation” through windfall profits taxes
  - 50% windfall profits tax was not expropriatory (effective 38% reduction in company’s take after subtracting operating costs)
  - 99% windfall tax was not expropriatory (effective 65-70% reduction in value of each barrel of oil)
- So even 65-70% reduction in value was held not expropriatory
Expropriation
Burlington v. Ecuador (2012)

Unanimous decision

- State imposed the windfall profits tax but Petroecuador did not comply with its contractual obligation to absorb any new taxes of the Contractor
- Burlington was justified in suspending operations because the contractual tax absorption clauses were not honored
- State’s subsequent physical takeover of the oil blocks = expropriation
- Expropriation was unlawful because no compensation was paid or offered
- Quantum phase pending

Expropriation
Occidental v. Ecuador II (2012)

- Ecuador learned Oxy had transferred a 40% interest in the PSC to a non-affiliated company without governmental permission
- Ecuador terminated Oxy’s PSC
- Tribunal found the termination was a disproportionate response to the unauthorized transfer of interest
- Tribunal found the termination = expropriation
- Tribunal found contributory negligence by Oxy of 25%
- Compensation was reduced 25% to $1.8 billion
Expropriation — Pending Cases

• *Mobil v. Venezuela* (decision pending)
  – Nationalization of the Cerro Negro extra-heavy oil projects in the Orinoco belt

• *Repsol v. Argentina* (pending)
  – US$ 10.5 billion claim following the nationalization of Repsol’s 51% stake in YPF

International Arbitral Decisions on Contractual Stabilization Clauses

• *Burlington Resources v. Ecuador* (2012)

• *ConocoPhillips v. PDVSA* (2012)

• *Mobil Cerro Negro v. PDVSA* (2012)
Contractual Stabilization Clauses  
**Burlington Resources v. Ecuador (2012)**

- “. . . the Tribunal considers that the PSCs provided for the following rights: (i) the right to receive and sell the contractor’s share of oil production irrespective of the price of oil and its internal rate of return, . . . and (ii) the right to the application of a mechanism that would absorb the effects of any tax increase affecting the economy of the PSCs, i.e. a right to tax absorption under certain conditions.” (Award at ¶ 335)

- But as the parent company, Burlington could not assert a contract breach claim based on its subsidiaries’ contracts

- Burlington subsidiaries were not parties to the case

- For tax issues, parent-shareholder limited to expropriation claim

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Contractual Stabilization Clauses  
**ConocoPhillips v. PDVSA (2012)**

- Parties entered into a Side Agreement requiring that the state-owned oil company would absorb any OPEC-imposed production cuts from its share of production

- “The aim of the Side Letter was to ensure at all times a minimum level of production in order to ensure the financial viability of the Project . . . in case production cuts were imposed by the government in implementation of its OPEC commitments and affecting the level of production required by the Project, such cuts would be absorbed by the state-owned entity to the Project, i.e. Maraven, out of its own production. . . . [T]he Arbitral Tribunal finds that the production curtailments for which Claimants seek redress fall within the scope of the Petrozuata Side Letter.” (Award at ¶¶ 209-11)

- ConocoPhillips awarded $67 million
Contractual Stabilization Clauses
*Mobil Cerro Negro v. PDVSA (2012)*

- In the event of governmental Discriminatory Measures as defined in the Association Agreement (“AA”), an arbitral tribunal could either recommend amendments to the agreement to restore the economic equilibrium or award compensation payable by the state-owned oil company per a formula with a cap.

- The Government unilaterally terminated the AA.

Stabilization Clauses
*Mobil Cerro Negro v. PDVSA (2012)*

- AA Art. 15.2 provided a limitation on compensation to the Foreign Party for Discriminatory Measures.

- “In the Tribunal's view, these provisions foresee an ongoing concession and intention to maintain the economic benefit of the Foreign Party for the duration of the AA within the limitations contained in that Agreement. In the event of a termination of the contract and the seizure of all of the Claimant's interest, the application of the limitation contained in Article I5.2(a) is made more difficult and the Arbitral Tribunal's authority to make recommendations on amendments to the AA that would restore the economic benefit to the Foreign Party absent the Discriminatory Measure is defeated.” (Award at ¶ 604)

- Tribunal held Art. 15.2 did not prevent compensation when the Government terminated the AA.

- Mobil was awarded US$908 million (US$747 million after counterclaim/setoffs).
**Force Majeure**  
**Mobil Cerro Negro v. PDVSA (2012)**

- “Regardless of whether an act of government emanates from the same public entity that is a party to the contract or from another public entity, Respondents have a responsibility to compensate Claimant for acts of government in so far as such a responsibility is expressly provided for in the AA, and particularly in its Article 15.” (Award at ¶ 524)

- “The Tribunal thus concludes that Article 15 AA . . . allocates the risk for actions of the Republic of Venezuela that might otherwise be force majeure. . . . Therefore, the Tribunal rules that any responsibility found for the Respondents for Discriminatory Measures due to Article 15 AA is not excused by force majeure.” (Award at ¶ 545-46)

**Environmental Settlement Agreement — Diffuse Rights**

- TexPet and Ecuador settled environmental claims in 1995
- Issue — whether Settlement barred 3rd Party claims
- “Diffuse rights are indivisible entitlements that pertain to the community as a whole, such as the community’s collective [Constitutional] right to live in a healthy and uncontaminated environment” (quoting Joint Experts’ Report)

- “[T]he Tribunal concludes that . . . the 1995 Settlement Agreement and . . . the Final Release preclude any claim by [Ecuador] against any Releasee [including Chevron as TexPet’s future parent company] invoking diffuse constitutional rights . . . But these releases also preclude any third person making a claim against a Releasee invoking the same diffuse constitutional right . . ., not being a separate and different claim for personal harm (whether actual or threatened).”

- Tribunal reserved the issue of whether the Lago Agrio case involved a diffuse rights claim, which is “forever” “settled in full”  
US Discovery in Aid of Foreign Proceedings Under 28 USC § 1782

- An application for discovery may be made to a US federal court in aid of a proceeding before a “foreign or international tribunal”
- In 2004, US Supreme Court suggested in dicta that § 1782 could encompass an international arbitral tribunal (Intel case)
- Since 2010, Chevron and Ecuador have filed more than 35 discovery proceedings under § 1782 involving witnesses in US
- Most federal courts now hold that § 1782 discovery can be obtained for use in an international arbitration (see Chevron/Ecuador cases)
- But the 5th Circuit holds § 1782 does not contemplate an arbitral proceeding — El Paso, 341 Fed. Appx. 31 (2009)
- 5th Circuit recently granted § 1782 discovery based on judicial estoppel because a party had obtained § 1782 discovery in other circuits by arguing an arbitral tribunal is an “international tribunal” — Republic of Ecuador v. Connor (2013)

Interim Measures

- “… the Tribunal hereby orders:

  (i) the Respondent (whether by its judicial, legislative or executive branches) to take all measures necessary to suspend or cause to be suspended the enforcement and recognition within and without Ecuador of the judgments by the Provincial Court of Sucumbíos . . . against the First Claimant [Chevron] in the Ecuadorian legal proceedings known as “the Lago Agrio Case”

  — Chevron Corp. & Texaco Petroleum Co. v. Ecuador, Second Interim Award on Interim Measures (Feb. 2012) at ¶ 3
Fair & Equitable Treatment (“FET”) Under Bilateral Investment Treaty (“BIT”)

• “The Tribunal considers that, in the same way as one can speak of creeping expropriation, there can also be creeping violations of the FET standard. According to the case-law, a creeping expropriation is a process extending over time and composed of a succession or accumulation of measures which, taken separately, would not have the effect of dispossessing the investor but, when viewed as a whole, do lead to that result. A creeping violation of the FET standard could thus be described as a process extending over time and comprising a succession or an accumulation of measures which, taken separately, would not breach that standard but, when taken together, do lead to such a result.”

– El Paso v. Argentina, Award at ¶ 518 (2011)

BIT Umbrella Clause

• “Each Party shall observe any obligation it may have entered into with regard to investment”

– US-Ecuador BIT, Art. II(3)(c)
Umbrella Clause
*Burlington Resources v. Ecuador* (2012)

- BIT case was brought by parent company, not by the subsidiaries who entered into contracts with Petroecuador.

- “… it is certain that the majority of the ICSID case law supports the Tribunal’s conclusion that the protection granted under the *umbrella clause requires privity between the investor and the host State*. For these reasons, the majority concludes that the Tribunal has no jurisdiction over Burlington’s umbrella clause claims according to which Ecuador would have failed to adjust the contractor’s oil production share and to guarantee the contractor’s participation in oil production.” (Award at ¶¶ 233-34)

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Umbrella Clause

- “It is the submission of this arbitrator that the right conclusion should have been that the entity whose interest in the investment is protected under the treaty is also entitled to benefit from the protection of an umbrella clause devised to ensure the observance of obligations concerning that investment. … An interpretation to the effect that only the corporate entity having signed the contract can rely on the protection of the umbrella clause will inevitably lead to a negation of the protection in question depriving the treaty of all meaning in this context. Such a view entails extending the treaty protection to its beneficiaries, including the umbrella clause, with the one hand, and then denying such protection with the other hand.” (Orrego Vicuña Dissenting Opinion at ¶¶ 9-10)
**NAFTA — Performance Requirements for the Oil Industry**

- NAFTA Art. 1106 prohibits countries from imposing performance requirements on foreign investors requiring them to purchase or prefer goods or services produced in the host country's territory.

- In 2004, the Canadian Newfoundland and Labrador Offshore Petroleum Board adopted Guidelines for R&D Expenditures.

- Claimants argued these would require offshore petroleum investors to pay $ millions per year for R&D in Newfoundland.

- Tribunal found the R&D and E&T (education and training) requirements imposed by the Guidelines to be “services” within the meaning of NAFTA Art. 1106 and therefore were performance requirements prohibited by Art. 1106.

  — Mobil & Murphy Oil v. Canada (2012)

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**Gas Pricing / LNG Disputes**

- Recent disputes under long-term gas sales contracts or in connection with LNG projects, particularly involving European buyers and Russian and Middle-Eastern/North-African producers.

- From 2009 onwards, the de-coupling of oil prices (the basis of gas price formulas under long-term contracts) and gas re-sale prices on European markets has threatened buyers with considerable losses.

- Regional market-based gas pricing has emerged in Continental Europe.
Gas Pricing / LNG Disputes
(based on published news reports)

• *PGNiG v. Gazprom*
  – US$1 billion price reduction settlement

• *RWE Transgaz v. Gazprom*
  – Buyer prevails on take-or-pay issue

• *GasTerra v. ENI*
  – Seller prevails on price issue (€833 million)

• *Edison v. Rasgas*
  – €450 million price reduction

• *Gas Natural v. Sonatrach*
  – Settled with seller obtaining US$1.9 billion

IBA Guidelines on Party Representation in International Arbitration (2013)

• 1st set of ethical guidelines for counsel in international arbitration

• Guidelines cover:
  – *ex parte* communications
  – duty of candor and honesty
  – creating conflicts with an arbitrator
  – document production obligations
  – preparation of witness statements

• Who may enforce them? — The arbitral tribunal to the extent necessary to ensure the integrity and fairness of the proceedings
2012 ICC Arbitration Rules

- Emergency arbitrator:
  - Provide an arbitral forum for emergency relief (in the form of interim measures) prior to the constitution of the arbitral tribunal
  - Emergency arbitrator decision does not bind the arbitral tribunal
  - Emergency arbitrator procedure does not prevent recourse to the courts for urgent interim or conservatory measures

2012 ICC Arbitration Rules
Efficiency

- Duty to arbitrate in good faith — Parties are under a duty to use their best efforts to conduct the arbitration in an expeditious and cost-effective manner and comply with the orders of the Tribunal (Art. 22)

- Arbitrators must sign a statement of availability in addition to the statements of impartiality and independence (Art. 11)
Increasing Emphasis in Investment Arbitrations on Contractual Protections Against Political Risks

- Arbitration clauses
  - breadth of clauses (more than contract disputes)
  - *situs* of arbitration — neutral country
  - parties — state-owned company and government

- Stabilization, adaptation and renegotiation clauses (and creative hybrids)

- Economic risk allocation clauses—allocating costs or risks of increased costs or taxes to state-owned companies