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Arbitration Watch:

1. Occidental Wins Investment Arbitration Against Ecuador; Ecuador Vows "Appeal",
By Luke Eric Peterson

In an award handed down on July 1, 2004, an UNCITRAL arbitral tribunal has ruled that Ecuador violated the provisions of the US-Ecuador bilateral investment treaty (BIT), and awarded some \$75 million to the affected investor, US-based Occidental Petroleum.

The arbitration, which had been commenced in October of 2002, arose out of a dispute over refunds of Value-Added Tax (VAT) paid by Occidental to Ecuadorian tax authorities.

In 1999 Occidental concluded a so-called "participation contract" with Petroecuador (a state-owned oil company) and agreed to undertake exploration and production of oil.

In the course of these exploration and exploitation activities, the firm incurred various expenses and paid VAT on a number of goods and services. For a time, the firm was able to claim a refund of these taxes, however in 2001 the Ecuadorian tax authorities began denying the reimbursement applications of Occidental and other companies operating in the oil industry. The authorities also demanded that oil firms return the amounts which has been previously reimbursed to them by the government.

This change in policy gave rise to a large amount of litigation by foreign oil companies (including Occidental) in Ecuadorian courts, as well as at least two international arbitrations - that of Occidental, and another by the Canadian firm Encana under the Canada-Ecuador BIT. The latter case is still pending before a separate UNCITRAL tribunal.

In the award handed down this month, the tribunal in the Occidental arbitration found several violations by Ecuador of the US-Ecuador BIT, including those on National Treatment, Fair & Equitable Treatment, and Full Protection and Security.

Notably, the tribunal rejected the contention by Ecuador that Occidental should have been ineligible to mount a claim under the treaty because it had triggered the so-called fork-in-the-road provisions contained in the US-Ecuador BIT.

While the tribunal noted that Occidental had mounted 4 cases in local courts, the tribunal ruled that these cases (which are still pending) deal with questions of Ecuadorian tax law, whereas the international arbitration claim addresses "different questions to different mechanisms of dispute resolution".

The tribunal also upheld Occidental's arguments that provisions of the US-Ecuador BIT, which limit the circumstances in which claims can be asserted with respect to taxation, did not prevent the firm from using the treaty's dispute settlement mechanism to challenge its treatment in Ecuador.

The tribunal did reject at the outset, however, a claim by Occidental that the taking of its VAT refunds amounted to an "expropriation" of its investment. At the admissibility stage, the tribunal found this particular claim wanting.

The tribunal professed difficulty with characterizing a refund as an investment per se. Moreover, the tribunal noted that, even on a generous interpretation of "indirect expropriation", it could not be argued that there had been a "deprivation of the use of reasonably expected economic benefit of the investment, let alone measures affecting a significant part of the investment."

However, Occidental did convince the tribunal that it was the victim of discrimination, and in an important development, the tribunal agreed with Occidental's argument that its treatment should be compared to that of actors in other (i.e. non-oil) economic sectors - who were entitled to VAT refunds under Ecuadorian tax law. The tribunal expressly rejected a WTO/GATT style analysis of National Treatment, which would restrict its comparison to products which are "directly competitive or substitutable products".

Relying, in part, on the investment treaty language - which referred to the need for national treatment "in like situations" - the tribunal applied a generous interpretation to that concept: comparing Occidental's situation to that of companies involved in the export of other goods, including flowers, mining and seafood products.

The tribunal also held that Occidental had not received fair & equitable treatment under the treaty, notwithstanding the fact that the tribunal believed Ecuadorian tax authorities to have acted in good faith with respect to the dispute over eligibility for VAT refunds. The tribunal looked unfavorably upon the fact that the firm faced a vague and unstable legal and business environment, noting that: "The tax law was changed without providing any clarity about its meaning and extent and the practice and regulations were also inconsistent with such changes."

Having found that Ecuador was in breach of the Fair & Equitable treatment standard, the tribunal held that this had the effect of also constituting a breach of the related guarantee for the provision of Full Protection and Security.

Counsel for Occidental told INVEST-SD that it was very pleased with the tribunal's ruling, characterizing it as a "complete victory" for Occidental. Counsel for Ecuador did not return a call from INVEST-SD at press time. However, press reports out of Ecuador suggest that the Republic may seek to "appeal" the award - a seeming reference to a possible challenge to the award under the domestic arbitration law of the country where the arbitration was legally sited (the United Kingdom).

INVEST-SD will continue to monitor developments, as well as any subsequent commentary and analysis of the tribunal's award.

Sources:

Final Award, In the matter of an UNCITRAL arbitration between Occidental Exploration and Production Company and The Republic of Ecuador, (London Court of International Arbitration Administered Case No. UN 3467), July 1, 2004

INVEST-SD Interviews

"Ecuador Plans to Appeal Arbitration Loss to Occidental", By Mercedes Alvaro, Dow Jones Newswires, July 13, 2004

2. Enron case at ICSID in partial abeyance; one claim still proceeding, By Luke Eric Peterson

Two ICSID claims by the Enron corporation against the Argentine Republic have diverged, with one of those claims being suspended, while the other continues to proceed towards a decision on jurisdiction.

In April of 2001, the energy trading firm launched its initial claim against the Argentine Republic in an effort to challenge the levying of stamp taxes on Enron-owned

investments in the Republic. Enron has characterized those taxes as tantamount to expropriation under the terms of the US-Argentina bilateral investment treaty. (See "Tribunal Finds Jurisdiction to Hear Enron Claim Against Argentina", INVEST-SD News Bulletin, March 25, 2004)

Subsequent to the filing of that claim, the firm filed a later claim against the Republic related to the controversial emergency laws introduced during the Argentine financial crisis.

This second claim was subsumed under the existing ICSID case number, and the same tribunal - consisting of Francisco Orrego Vicuña, Héctor Gros Espiell, and Pierre-Yves Tschanz - has been presiding over both claims.

In January of this year, the tribunal issued a decision on jurisdiction, finding jurisdiction to hear the stamp-tax claims. Hearings were held in April to examine the question of jurisdiction with respect to the challenge to Argentina's emergency legislation. A decision on jurisdiction related to that claim is likely to emerge sometime this summer.

In the mean time however, following a recent ruling by the Argentine Supreme Court dealing with other stamp tax claims by foreign investors in Argentina, Enron has requested the ICSID tribunal to suspend proceedings on the stamp tax portion of its claim. It is understood by INVEST-SD that the investor wishes to see how the Argentine Supreme Court will resolve the remainder of the stamp tax claims which are still pending before the Court. Favorable rulings by the Supreme Court might obviate the need for Enron to continue to pursue the stamp tax portion of its ICSID claim.

In a procedural order issued on June 10, the ICSID tribunal agreed to suspend the proceedings related to the stamp tax claim for a period of 8 months.

Contrary to published media reports in Argentina - which have cast that partial suspension as putting an end to Enron's entire case at ICSID - two separate sources tell INVEST-SD that the suspension is only temporary, and that the remainder of Enron's claim has not been suspended. An ICSID tribunal continues to deliberate over that part of the case which relates to Argentina's emergency legislation.

Sources:

INVEST-SD interviews

"Tribunal Finds Jurisdiction to Hear Enron Claim Against Argentina", By Luke Eric Peterson, INVEST-SD News Bulletin, March 25, 2004, available at: http://www.iisd.org/pdf/2004/investment_investsd_mar25_2004.pdf

3. Cargill Challenges Polish Agricultural Quotas at ICSID, By Luke Eric Peterson

US-based agricultural giant Cargill has had a claim registered against Poland at the International Centre for Settlement of Investment Disputes (ICSID).

The claim alleges breaches of the 1994 Business and Economic Relations Treaty between the US and Poland - an agreement which incorporates many of the standard provisions of the better-known US bilateral investment treaties.

Based upon press reports and interviews by INVEST-SD, Cargill's claim is known to pertain to national quotas on isoglucose production which had been set by Poland several years prior to its accession to the European Union in May of this year.

Since the late 1990s, Cargill has been Poland's only producer of isoglucose, a wheat-based product which competes with sugar as a sweetener used in soft drinks and confectionary.

When Poland introduced quotas on isoglucose production in advance of its accession to the European Union (which was slated for May of 2004), the Polish government came under fire from Cargill and US government officials.

In the summer of 2002, during a visit to Poland, Assistant Secretary William H. Lash III of the US Department of Commerce criticized the government for imposing a quota which did not accommodate the entire production capacity of Cargill's Polish operations.

Later that year, the Government raised its national quota on isoglucose, and reduced the quota for sugar.

While still failing to meet Cargill's full demands, the increase in the quota also angered foreign investors in the Polish sugar industry.

British Sugar Overseas (BSO) criticized the quota changes and began litigation in the summer of 2002 in Polish courts in an effort to overturn the changes.

An official with BSO Poland told the Warsaw Business Journal that the changes decreased the value of BSO's investments because the firm had invested in state-owned sugar firms based upon the sugar quotas which existed at that time.

Stanislaw Dziedzic, the business development director for BSO Poland said: "As foreign investors, we are disillusioned with this move by the government. It undermines the investment to date and any future investment."

At the same time, Cargill remained unhappy with the increase in Poland's isoglucose quota, with officials telling the Warsaw Business Journal that the enhanced quota still represented only 50% of Cargill's production capacity.

(With Poland's accession to the EU in May of 2004, the isoglucose quota was slated to be lowered even further - although accounts differ as to the level at which this final EU quota has been set for Polish isoglucose.)

Following its failure to persuade the Polish government to increase its national quota for isoglucose further, Cargill turned to arbitration at ICSID.

According to the Time of London, Cargill is seeking some \$130 million US.

The firm alleges that it has received treatment less favorable than its competitors in the Polish sugar industry - contrary to international treaty guarantees. Cargill also alleges that Poland's national isoglucose quota, by virtue of falling significantly below Cargill's production capacity, amounts to an expropriation of its Polish operations.

Sources:

"Cargill Sues Poland", The Times (London), January 7, 2004

"EU (sic) Quota Threatens WROC AW Plant", By Timothy Sifert, Warsaw Business Journal, January 20, 2003

INVEST-SD Interviews

4. Head of NAFTA Arbitration Division Moves Back to Private Sector

The Head of the US State Department's NAFTA arbitration division has resigned his position with the US government and is moving back to private arbitration practice this autumn.

Barton Legum, who led the defence of the first arbitrations against the US under the NAFTA's investment chapter, told INVEST-SD News Bulletin that he will rejoin his "old friends" at the international dispute resolution practice of Debevoise & Plimpton LLP, "where (he) practiced for twelve years before joining the State Department."

Legum will be based in the firm's Paris office and expects to focus on international arbitration, including investment treaty arbitration.

David W. Rivkin, head of the firm's international dispute resolution practice, told INVEST-SD that he is "very excited" to see Legum rejoin its practice - describing him as an "outstanding lawyer" who has "had a great string of successes for the US while at the State Department".

Commenting on his former brief at the US State Department, Legum told INVEST-SD that "I leave the defense of the remaining cases in the strong and capable hands of my colleague Andrea J. Menaker, who has succeeded me as Chief of the NAFTA Arbitration Division."

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