**Article printed from CDR - (Commercial Dispute Resolution) | http://www.cdr-news.com**




# Of compliance and controversy

**SHANA TING LIPTON** 06 AUGUST, 2015

**Latin America is a hotbed of investment treaty arbitration. As the winds of change continue to affect oil prices, new investment, and arbitral awards, a snapshot of the current state of Latin American energy sector investment treaty arbitration offers insight into future trends.**

The **World Bank**'s **International Centre For Settlement of Investment Disputes** (ICSID), which boasts the lion's share of filings through the so-called "Washington Convention", saw most of its new cases registered in 2014 (35%) originate in the oil, gas and mining sector, with Argentina and Venezuela leading the regional pack as the most frequent respondents.

One pressing question is how much of a role the ICSID Convention will continue to play as a mechanism for bilateral investment treaty (BIT) arbitration of Latin American energy disputes going forward. ICSID has been rather publicly maligned and abandoned by states such as Venezuela, Ecuador and Bolivia, who argue that a foreign investor-friendly World Bank entity will always decide against them; as well as Argentina, which has considered leaving ICSID.

## ICSID: IN OR OUT?

**Noiana Marigo**, international arbitration group partner at **Freshfields Bruckhaus Deringer** in New York, does not believe Argentina will withdraw from ICSID. "They did not withdraw in the mid-2000s when they had over 40 ICSID claims and the government strongly complained about the system," she says, "today, Argentina is trying to get back into financial markets, has settled several if not all of its final ICSID awards and even settled **Repsol**'s expropriation claim. Argentina seems to be willing to play by the rules now".

**Patricio Grané Labat**, partner at **Volterra Fietta** in London, adds: "If Argentina really intended to withdraw from ICSID, one assumes that it would have done so already, especially under the Kirchner administration, which has been so vocal on its criticism of the system,

particularly in the context of the 'vulture funds' litigation."

Significantly, denouncing the ICSID Convention has not protected Argentina's regional neighbours, Venezuela, Ecuador and Bolivia, from foreign investor-state disputes. "In practical terms I do not think that would limit a country's exposure or the risk of cases being brought under bilateral or multilateral investment treaties," says **José-Manuel García Represa**, an international arbitration partner specialising in energy law and clean technology industries at **Dechert** in Paris.

**Pedro Martinez-Fraga**, a disputes partner at **Bryan Cave** in Miami, echoes his sentiment: "You can certainly abandon the Washington Convention of 1965, i.e. the ICSID Convention, but you cannot abandon your bilateral investment treaties as easily." While being a party to the ICSID Convention establishes the institution and framework through which prospective disputes will be resolved, the right to sue the state is afforded under the BIT (or other legal instrument that expressed the consent of that state to ICSID arbitration).

Consequently, one relatively novel argument, according to Marigo, is surfacing in Latin American energy disputes: that an investor should have the right to ICSID arbitration even against a state that has abandoned the Convention, based on consent to ICSID having been given in a treaty. She recently looked into this question in a case against Bolivia brought by **Pan American Energy**. "I think it is very solid under international law but unfortunately because we settled the case we will not know," she says.

Grané Labat says there are several cases pending before ICSID that may shed light on the issue. He highlights the significance of a recent arbitration between **Venoklim** and Venezuela in which the issue of whether an investor should have the right to ICSID arbitration surfaced. In that case, the tribunal rejected the state's jurisdictional defence that its denunciation of the ICSID Convention before the claimant submitted its arbitration request had immediate effect. "[This] means that Venezuela cannot simply use the jurisdictional argument to stop the cases going to ICSID," he says, adding, "that is why countries like Venezuela, Ecuador, and Bolivia, in addition to denouncing the ICSID Convention, have also denounced that second category of treaties, the BITs".

"Bolivia has been the only country that last year decided to denounce all of its treaties. That was a bold step in my view," says Marigo. In comparison, she says that Venezuela and Ecuador have denounced relatively fewer BITs. One such denunciation by Venezuela saw it retreat from its BIT with The Netherlands, "because many companies, particularly US companies that did not have a treaty between Venezuela and the US were using the Dutch subsidiaries to get protection", adds Marigo.

## UNCITRAL, THE ICC AND UNASUR: OTHER CONSIDERATIONS FOR INVESTMENT ARBITRATION

There is nevertheless more to investment arbitration than ICSID cases. García Represa explains: "Sophisticated and well-advised investors know that equating ICSID and investment arbitration is not necessarily right." Latin American states like Ecuador and Bolivia that have withdrawn from ICSID will likely end up arbitrating under the **United Nations Commission on International Trade Law** (UNCITRAL) Rules, administered by the **Permanent Court of Arbitration** (PCA) in The Hague. "What you are seeing more and more is that the Dutch courts will have an important role to play in investment arbitration as more investment arbitrations under the UNCITRAL Rules are seated in The Hague (home to the PCA), and that includes arbitration with Latin America," says García Represa.

He adds that, although not specific to the energy sector, increasingly states and foreign investors are likely to adopt the International Chamber of Commerce (ICC) rules administered by the **International Court of Arbitration**. Traditionally, the Paris-based organisation has been perceived as facilitating international commercial arbitrations but, according to Grané Labat, in the last few years it has been "trying to tell its users that in addition to commercial arbitration, it can also handle investment treaty arbitration".

In Latin America, Ecuador has proposed a new Union of South American Nations (UNASUR) investment arbitration centre that would offer an alternative to ICSID. The centre is likely to be more favourable to its region's states; UNASUR is presently reviewing the plan. This could materialise in the next couple of months, according to Martinez-Fraga who maintains: "In my opinion, it will not have legitimacy and therefore it will not be important in the world."

Marigo does not see UNASUR's centre as having any major role to play in the short term. "Leaving other considerations aside and assuming that investors would be willing to submit disputes to UNASUR, we would still need new investments, coupled with arbitration clauses or treaties submitting disputes to UNASUR, and then we would wait for the disputes to occur. This could take years."

## DISCOUNT RATES ON AWARDS

In the eyes of a Latin American state such as oil-dependent Venezuela, whose economy is in the throes of collapse under declining oil prices, such a regional arbitration mechanism may seem promising, as the state hopes to stop the financial haemorrhaging precipitated by heavy-duty awards against it. In one case against Venezuela won by the claimant **OI European Group** (OEIG) (which instructed Volterra Fietta), the state was ordered to pay USD 455 million for its unlawful expropriation of the company's majority interest in two Venezuela plants, reportedly the fourth largest ICSID award on record.

The case highlighted an issue regarding arbitration awards that has recently been brought centre stage; when discount rates are set based on factors such as the risk of illegal expropriation, the resulting percentage produces lower awards for claimants. Grané Labat, who worked on the OEIG case, argued on behalf of the claimant regarding the amount of compensation owed to foreign investors. He reasoned that the discount rate in the investment valuation should not incorporate expropriation in the country risk analysis, as that risk is entirely within the government's control.

"Everyone in the arbitration community is looking at this issue now because it has a huge impact on the compensation investors are awarded and might affect the way we present cases and what arbitrators we might appoint," says Marigo.

The discount rates and awards issue will undoubtedly be addressed, as disputes against states like Ecuador and Venezuela lodged by existing investors under ICSID play out in tribunals. Such cases are of course rooted in earlier financial cycles from the 1990s when a wave of investments poured into the aforementioned states, as well as in the mid to late 2000s due to developments like nationalisation. Marigo foresees Peru and Colombia, and other Central American countries, which are receiving significant investment now, being among the new wave of respondents in the next five to eight years.

## POTENTIAL FUTURE CLAIMANTS

China, which has invested in copper mines in Peru and has injected approximately USD 250 billion into Latin America overall, may seem a likely future claimant in disputes against states

in the region. “There will be potential disputes with China. China is still a relatively new player in the system,” confirms Grané Labat. However, he emphasises that China’s BITs tend to have limitations as they are very different from those of Ecuador, Argentina, Venezuela and Bolivia, particularly in those protections to foreign investors, including the right to bring international arbitration against the host state.

While China does hold BITs with the aforementioned Latin American states, as well as with Chile, Colombia, Mexico, Peru, Uruguay and Cuba, Grané Labat points out: “You cannot assume because there is a BIT that investors have unbridled access to ICSID. Every BIT needs to be looked at closely to determine the true scope and extent of its protections and limitations.” García Represa doubts that there will be a wave of Chinese-Latin American disputes in the near future adding that “any future threat of Chinese state-owned companies bringing energy claims against Latin American states would first and foremost depend on bilateral relations and politics”.

Marigo highlights how Japan has been investing in Latin America for many more years than China and “still has more investments than China in the region”. She explains that despite this, Japan does not have many BITs in place with Latin American countries, “so Japanese investors are starting to realise that they need to restructure their investments in order to obtain BIT protection, in particular those investing in high-risk countries” so they have access to neutral international tribunals to resolve disputes.

Although ICSID has dominated Latin America’s energy sector disputes, the continually developing roles of UNCITRAL, the ICC and UNASUR in the region may see a diversification of the way investment arbitration is carried out. It remains to be seen, however, whether potential future claimants such as China or Japan will become key claimants in disputes against other states in the region.

**Tagged with:** Arbitration & ADR - Arbitration - Freshfields Bruckhaus Deringer - Investment Treaties - Dechert - Bryan Cave - ICC - Peru - Argentina - ICSID - Venezuela - Energy - Volterra Fietta