Association For International Arbitration

InTOUCH

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AIA

Inside this month's issue:

Report on AIA's Conference on Arbitration and Mediation in the Natural Resources and Energy Sector

Arbitration practitioners and energy sector-related lawyers from all over Europe and worldwide gathered at the offices of Gaz de France – Suez in Brussels, Belgium on the 13th May 2009 for AIA's Conference on Arbitration and Mediation in the Natural Resources and Energy Sector. The one-day event brought forward some interesting presentations and innovative propositions on how to allow ADR to progressively evolve in the somewhat complex energy industry and its commercial relations in today's economy. The large attendance was a living proof of the increased interest in energy dispute resolution under the conflict settlement procedures of the Energy Charter Treaty and other nationally organised arbitration systems. The success of AIA's Conference, however, could not have been made possible without the assistance and contributions of many. First of all, AIA would like to thank all speakers who preserved the necessary spare time in their busy schedule to indulge our audience by providing them with discussion provoking presentations. Moreover, a great deal of gratitude is owed to those that contributed to the organisation of the Conference, in particular those who ensured the facilities at Gaz de France – Suez and our partners: Centre for Energy, Petroleum and Mineral Law and Policy (CEPMLP); Oil, Gas & Energy Law Intelligence (OGEL); Transnational Dispute Management (TDM); International Association of Oil & Gas Producers (OGP) . Most of all, however, AIA wishes to grant a special thanks to all the international visitors who enthusiastically stimulated the interactive debate with all our speakers and Graham Coop, General Counsel with the Energy Charter Secretariat, and Eugene Becker, Senior Principal of Becker Law in New York, who acted as moderators throughout the day.

The Conference was dedicated to pointing out the particularities of energy-related disputes and the way they should be dealt with in arbitration and mediation proceedings, on the one hand, and the manner in which arbitration and mediation as dispute resolving mechanisms can adjudicate typical national, but mostly bi-national energy conflicts, on the other hand. After a warm welcoming

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word of AIA's president Johan Billiet, several academic speakers and experienced energy lawyers took the floor.

The Energy Charter Treaty introduced

Matthew D. Slater, Partner at Cleary Gottlieb Steen & Hamilton LLP, presented the audience with a oversight of the most relevant and peculiar articles of the Energy Charter Treaty (ECT) of 1994, ratified by 46 nations and the European Community and EURATOM, excluding Russia, Norway, Belarus, Iceland and Australia who have signed, yet did not ratify the Treaty. It is designed to promote energy security through the operation of more open and competitive energy markets, while respecting the principles of sustainable development and sovereignty over energy resources. The ECT's main characteristic is its emphasis on inter-state related energy investment opportunities and its efforts on safeguarding the commercial relations between state parties and foreign energy investment companies.

One of the guiding but heavily disputed rules establishing such long-term cooperation agreements is the 'fair and equal treatment'-principle, brought forward in art. 10 (1) ECT, obliging a country to, first of all, protect the reasonable and justifiable expectations that were taken into account by the foreign investor to make the investment in the pre-investment stage. Transparency of the contracting state entity concerning possible energy resources or other assets in negotiating energy investment contracts are paramount in this respect according to the *Plama v. Bulgaria* arbitration. Second, the contracting country should provide the investor with a stable legal framework in which the investment will not suffer the risk of being interfered with discriminatory or unreasonable measures interrupting the management of the investment. This obligation rests upon the state party in the period after which the investment contract has been finalised. In fact, and partially overlapping this principle, art. 10 (2) and (3) ECT prohibits any discriminatory measures on behalf of the state party by which investors would be treated differently and less favourably than their national counterparts or even other foreign investors who are in similar situations and with whom the state party has investment agreements, whichever is the most favourable.

Moreover, art. 10 (1) ECT provides a further duty on the host state to constantly protect and secure the foreign investment against interferences of state actions concerning e.g. arbitrary expropriations or environmental regulations (cfr. Art. 13 ECT) or possibly – and fiercely debated- third party measures interfering with the exploitation of the energy sources. Arbitration tribunals appear to interpret this obligation rather strictly however. An example of accepted interfering legislation is taxation by the contracting state (art. 21 (1) ECT), although the Most Favorable Nation non-discrimination-obligation applies as well in this respect, but not to levied income taxes and capital gain taxes.

Energy disputes in front of ICC and LCIA

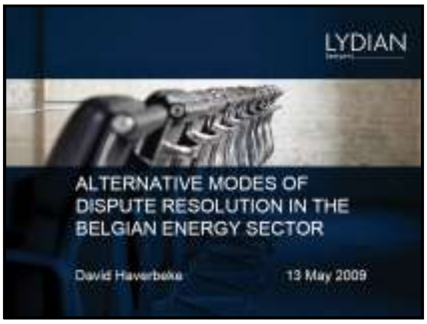
Benoit Le Bars, Partner at Hammonds Hausmann Paris, and Paul Oxnard, Partner and Head of Commercial & Dispute Resolution Hammonds LLP London, presented a comparative overview of ICC's and LCIA's practice concerning energy-related disputes. They pointed out that out of the 599 cases in front of ICC in 2007, approximately 11% deal with conflicts arising out of energy investment contracts, a figure which can be explained by the large advantages institutional arbitration has to offer over *ad hoc* arbitration. Not only does the administration of the disputes proceed more easily and automated, but the arbitrators themselves are also exactly hand-picked by LCIA and ICC for their expertise and experience in the field of energy investment dispute resolution. The arbitration rules of both organizations are well-tested as well and do not necessitate the use of *ad hoc* arbitration procedural models such as the UNCITRAL Rules.

Especially suitable for energy disputes, (institutional) arbitration can offer utmost neutrality by letting the parties chose the seat of arbitration and the applicable law in situations where the energy investment conflict involves several parties based in different jurisdictions and fear exists of possible biased national domestic courts. The best guarantee of avoiding bias is making sure that the appointed arbitrators hold different nationalities than the parties involved and to chose an applicable (arbitration) law that adjudicates the challenge of an arbitral award in case of arbitrator bias. Most importantly, however, arbitral awards rendered after the resolution of the energy dispute are far more easily enforceable in foreign jurisdictions than domestic court decisions, this by the courtesy of the New York Convention of 1958. Even in the unlikely event of an award that has been set aside by a domestic national court, the country in which the winning part of the arbitration seeks enforcement will sometimes still recognise the set aside award, for example in France; not, however, in the UK. Another essential reason pointing to the direction of arbitration is its guarantees of full confidentiality, but only if the parties enter into confidentiality undertakings concerning the information that will be exchanged during the proceedings. Both France and the UK have no explicit provision in their Arbitration Acts to warrant confidentiality but the national courts in both countries have recognised an implied duty of confidentiality on parties entering into an arbitration procedure, albeit somewhat lifted and made public when a party challenges an arbitral award rendered in France. A classical benefit of arbitration proceedings is its relative speed. Where national court proceedings can last up to ten years in France, the ICC can render a decision within 6 months.

Difficulties arise, however, when attributing the evidence brought forward by the parties. Since energy disputes often involve very complex issues, the parties might be tempted to appoint their own energy experts, which makes it difficult for the tribunal to have both of them communicate with each other to come to a concluding statement on certain technical issues. LCIA and ICC would be very suitable arbitration venues as the national courts of both countries support arbitration proceedings where possible, a fact that has been emphasised by the recent ECJ West Tankers-case, prohibiting English Courts from ordering an anti-suit injunction against parties who are conducting parallel court proceedings in another EU Member State.

Alternative Modes of Dispute Resolution in the Belgian Energy Sector

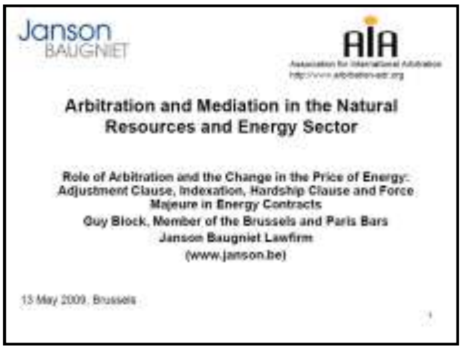
David Haverbeke, Head of Energy & Utilities Practice at Lydian Lawyers, elaborated on the specificities of the Belgian experience in dealing with energy investment-related disputes. Since Belgium is situated at the crossroads of several energy flows from within Europe such as the natural gas flows from the United Kingdom into continental Europe via the Zeebrugge Hub and the electicity flows originating from France and the Netherlands.



According to the European Electricity Directive (96/92/EC) and Gas Directive (98/30/EC), the Member States of the European Union were obliged to install national dispute settlement bodies for the specific purpose of resolving energy disputes. Belgium's complex federal governance system forced the installment of several different federally and regionally controlled dispute settlement bodies. None of these are truly active, which is hardly surprising considering the disadvantages an entity such as the dispute settlement body, created within the Commission for Regulation of Energy and Gas (CREG), has in comparison of the Belgian Centre for Arbitration and Mediation (CEPINA) and other foreign arbitration institutions. First of all, the confidentiality of the information exchanged during the proceedings is not guaranteed as the arbitral awards will be published. Second, and more importantly, the parties are not free to chose their own arbitrators as the dispute settlement body will appoint the arbitrators for them from a prior established list of arbitrators.

Contractual clauses raised in arbitration to challenge energy prices

After discussing the evolutions of the energy pricing mechanism from a technical point of view and the steady increase of oil prices until its dramatic downfall in October 2008, Guy Block, Partner and Head of the Energy Department at Janson Baugniet, raised several key questions concerning the influence of energy pricing in arbitration proceedings. When dealing with disputes concerning the appropriate pricing of an energy delivery contract, one must always look at the contractual method the supplier uses to adapt its energy price to certain occurring or reoccurring circumstances. An adaptation or indexation clause, on the one hand, will normally stipulate that the energy price will be automatically raised in case of an increase in indexation, a supplementary tax levy or augmenting other types of duties and contributions to a public authority. An arbitrator trying to solve the dispute of a party refusing to accept the automatic price adaptation is dependent on the factual and circumstantial information given to him by the parties if he is to arrange a new price. The parties' intent itself is usually not enough to reach a profound conclusion. The reason for choosing an arbitrator over an independent expert to determine the new adapted price is the fact that energy disputes mostly involve several parties from different countries, making it more attractive to achieve an enforceable award under the New York Convention instead of a non-enforceable expert determination. It is not uncommon, however, to combine the bests of both worlds, appointing 2 experts as arbitrators and having a lawyer presi-



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ding the arbitral tribunal, especially when dealing with long-term contracts between state suppliers.

Hardship clauses, on the other hand, apply only when unforeseen events such as new regulations, environmental calamities, technical difficulties, political instability or economical distress affect the equilibrium of the contractual relations and render its execution abnormally difficult. Instead of an automatic increase in price, the consequences of these contractual aforementioned events will be very different. The parties can stipulate to renegotiate the price using a third party expert or experienced dispute resolving arbitrator, or the parties can primarily, or possibly only in absence of a reached pricing agreement, terminate the entire contract. Parties need to be attentive, however, on the possible inferences a national court might draw from the mere presence of an energy price adaptation or hardship clause on the energy pricing itself, for instance by being more reluctant to conclude that a sudden increase in prices frustrates the contract. The primary question arbitrators need to address is whether or not the clause is in fact a hardship clause and not a mere indexation or *force majeure* clause. Again, full information disclosure will be paramount for the arbitrator to reach a viable decision. Only then can the arbitrator fully restore the economic equilibrium between both parties after the occurrence of the unforeseen event.

Another type of clause used in arbitration when discussing energy prices, is the *force majeure* clause that stipulates that the execution of the contract itself is rendered completely impossible by the occurrence of an unforeseen event beyond the reasonable control of a party. Sudden price increases on the overall energy market are not accepted as *force majeure* reasons, nor as hardship events as demonstrated by several ICC cases in the aftermath of the 1970s oil crisis.

Interim relief in energy disputes and stabilization clauses in contract negotiations

Johannes Koepp of Baker Botts LLP, presented a more detailed view of possibility of interim measures in arbitration proceedings concerning energy disputes. Whereas ICC 's and most other arbitration institutions' rules explicitly allow parties to seek interim relief in front of a national court, ICSID will only grant the same possibility in case of an explicit party agreement thereto. The availability might be postponed until the proper constitution of the arbitration tribunal. Concerning these interim measures, national courts are usually supportive towards parties in an arbitration agreement asking for a freezing order to prevent assets of a certain party to become dissipated by removal or value diminishment during the course of arbitration. A party will nevertheless need to prove a certain urgency for the interim measure, for instance of fear of immanent or fraudulent removal of assets. In *Mobil Cerro Negro Ltd. v.*

PDVSA an English court did not grant such a freezing order on several assets in Venezuela in support of an ongoing ICC arbitration in New York, due to a lack of urgency and a lack of a connecting link between at least some of the assets in question and the United Kingdom's jurisdiction.

Another peculiar instrument often used in energy contract negotiations is the stabilization clause, protecting energy suppliers from direct or indirect state expropriation or another unilateral exercise of a state's sovereign power to change contractual terms, especially envisaging long-term contracts where political instability may affect these capital-intensive energy projects. The provision might take the form of a freezing clause, obliging the host state not to take intrusive measures concerning the property or licensing agreements of the investor. Newest in trend, however, is the economic balancing clause, obliging both parties to renegotiate the terms of the investment contract in case of unfavourable legislation concerning the exploration, development or production of the energy source in question that damages the economic interests of the investor. Be aware though that several countries such as the United Kingdom and Norway do not offer these types of clauses to investors.

Investment arbitration and possible EU competence

Sophie Nappert, Arbitrator with Gray's Inn London, emphasised investor-to-state arbitration as the cornerstone of many bilateral and multilateral investment treaties. The question arises what neutral forum will be available for (third country) investor-to-state dispute resolution in case the EU on behalf of its Member States enters into agreements with third states using the rules laid down in the 'European Minimum Platform on Investment', adopted by the European Council on 27 November 2006, and providing protection mechanisms for foreign investments on EU territory, including Most-Favoured-Nation treatment but specifically excluding investor-to-state arbitration from its scope. The fact that the European Court of Justice has avoid making judgments on the extent of the EU's shared or exclusive competence concerning these matters, is not helping either.

It would be advisable to establish a neutral investor-to-state arbitration mechanism in future agreements incorporating the Platform rules with jurisdiction to interpret in accordance with international law in order for the development of EU investment law to become gradually compatible with international investment law and its broader protection mechanisms. Assisting the achievement of this goal, a procedure of preliminary reference of questions (art. 234 EC Treaty) of arbitration tribunals to the European Court of Justice could be installed.

Soft law in investment arbitration

Aloysuis Gng, PhD Candidate at the University of Dundee, approached the so far untouched topic on the use, implementation and judicial effects of soft law in investment arbitration disputes. Depending on the perspective, arbitration is either blessed or cursed due to the lack of procedural standards by which arbitrators can conduct proceedings, especially in gathering evidence and hearing arguments. Procedural soft law however is unsuccessfully attempting to judicialise certain procedural elements of which the arbitrator nowadays still has a broad autonomy to do whatever the tribunal deems or considers appropriate. Soft law instruments such as the IBA Guidelines on Conflicts of Interest, the CIArb Guidelines on

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http://arbitration-adr.org/activities/publications.html the Interviewing of Prospective Arbitrators for future appointment reasons are clear examples of soft law intrusions in international arbitration and should be dealt with with extreme caution in international investment disputes.

In conclusion, AIA is utmost grateful for the very interesting topics and lively debates raised during the Conference on Arbitration and Mediation in the Natural Resources and Energy Sector. To read up on all the aforementioned topics, AIA has published the comprehensive booklet "Alternative Dispute Resolution in the Energy Sector" covering the subjects related to the Energy Charter Treaty not only from a theoretical point of view, but also from practical experiences in France, the United Kingdom and Belgium. Moreover, this publication is original in that it addresses the issue of soft law in investment arbitration and includes a fictional case elaborating on the influence of different interest groups in energy disputes.

Arbitration in the Financial Sector: bear or bull?

The difficulties of today's financial markets as the backbone of modern economy have been extensively commented over the last 9 months. Nevertheless, the consequences of the worldwide recession will undoubtedly take its toll on litigation and arbitration as well, but to what extent, remains to be seen. In the area of financial arbitration new opportunities can arise for ADR to facilitate disputes not only concerning economic cross-border mergers of financial institutions who roam the market looking unique bargains (B2B), but also dealing with consumer protection against intrusive credit contracts compelling lenders to provide security and/or forcing them to agree to an unwanted arbitration clause (B2C). In both cases, financial arbitration disputes demand specific expertise of the arbitrators and counsel involved, due to the complexity of the proceedings concerned, the sheer number of participating international parties in large scale contracts and the fast-evolving nature of financial practice and markets in contrast to the tardiness to which legislation can adapt itself to changing financial innovations. Furthermore, financial services comprise of so much more than simply banking services to consumers. Insurance activities are to be included as well.

Recent developments have shown a growing interest for arbitration and ADR in general in the field of the financial services sector, irrespective of today's negative economic prospects. First of all, the ICC records a gradual increase of registered cases relating to financial arbitration over the last 10 years. Second, China has acknowledged that their economy-on-the-rise needs a stable financial institutional basis that includes effective, alternative dispute settlement procedures. For that reason and to achieve such a purpose, China has constituted the Shanghai Court of Financial Arbitration, which deals with both domestic and foreign financial disputes and functions as a attractive forum for international financial institutions. Thirdly, Liechtenstein is planning on joining the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards and adapting its 1895 originating arbitration law in accordance with the 'Futuro' project on perspectives for the future of the Liechtenstein financial center. With the revision it hopes to become a respected venue for foreign disputes in order to diversify its financial center and include areas of trust matters, proprietary claims and asset and succession planning. Lastly, also Dubai has recently adopted a new arbitration law enabling a international partnership between the Dubai International Financial Centre (DIFC) and the London Court of International Arbitration (LCIA). The joined cooperation will meet the demands of leading financial institutions and companies across the globe to get access to a high standard regulatory environment and achieve efficient dispute resolution services. Where the LCIA will govern the supervision of the arbitral proceedings and organisatory aspects, the DIFC will act as a threadstone offering the facilities of the joint venture to the sectors in which it has over 500 active members, including the banking sector, capital markets, insurance and re-insurance players, asset management and fund registration.

Nevertheless, some indications are rising that arbitration might not be positively induced in financial crisis situations. Many financial institutions in practice draft their terms of reference in way to force their customers to arbitrate their disputes, this to the detriment of the consumers who are not familiar with the culture and proceedings of ADR in general, let alone arbitration in particular, and are obliged to waive their right to legal claims before national courts. The 3rd Circuit Court of Appeals of New Jersey, however, questioned the validity of these arbitration clauses in *Homa v. American Express Co.*, decided in (USA) on 24 February 2009. In the case at hand American Express neglected a payment to *Homa* agreed upon in a credit contract in violation of the New Jersey Consumer Fraud Act. For the dispute Utah law was chosen to be the applicable law according to the arbitration clause. Progressive in its kind, Utah law specifically allows individual arbitration and class waiver provisions in consumer credit agreements, hereby forcing *Homa* to arbitrate, notwithstanding his argumentation to only apply New Jersey law which explicitly forbids these class-arbitration waivers. Judging in first instance, the District Court followed *American Express* but faced a reversing judgment of the Third Circuit Court of Appeals allowing *Homa* to find relief before a federal court in New Jersey. Its *ratio decidendi* brought forward the public interest for consumers as being the most important reason for holding similar class-arbitration waivers unconscionable.

In this respect, the Arbitration Fairness Act of 2009 will change several aspects of the legal framework surrounding consumer arbitration. It will determine provisions requiring arbitration of employment, consumer, or franchise disputes unvalid and unenforceable and may therefore lead to an augmentation of consumer litigations in the financial sector.

Dutch enforcement of set aside Russian arbitral award: Yukos Capital v. Rosneft

On Tuesday 28 April 2009, the Amsterdam Court of Appeal accepted the enforcement in the Netherlands of four Russian arbitral decisions concerning *Yukos Capital v. Rosneft*. Yukos Capital, a Luxemburgian company and OJSC Yuganskneftegaz, a Russian company but vested in a larger Yukos-group structure, included an arbitration clause in the four loan agreements they concluded with each other, committing themselves to arbitrate in case of a dispute concerning the loans and the impossibility of renegotiation the terms of the contract. After the fusion of Yuganskneftegaz with the Russian state-owned Rosneft, Yukos Capital requested the execution by Rosneft of the four arbitral awards previously ordered againstYuganskneftegaz to pay a certain amount of the loans back to Yukos Capital. The Arbitrazh Court of the City of Moscow, however, set aside all awards due to Rosneft's complaint of several procedural violations on behalf of the arbitral tribunal, including the partiality of an arbitrator who attended a seminar organized by Yukos Capital's lawyer.

Nevertheless, Yukos Capital sought enforceability of the awards in the Netherlands, the country where several assets of Rosneft were located, but came across the First Instance Court in the Netherlands that upheld the non-recognition and unenforceability of these awards due to the fact that the decision by the Russian civil courts needed to be respected unless general public policy provisions concerning due process such as the principles of impartiality and independence of the judicia-

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ry power were violated by the Russian courts, an allegation that was not adequately proven by Yukos Capital who primarily used newspaper articles to establish the Russian state's influence on Russian courts' judgments in cases where the Russian state was acting as a party or was indirectly involved, e.g. by having a majority shareholder in one of the parties concerned. The Amsterdam Court of Appeal, however, found the same arguments brought forward by Yukos and backed up by several reports and evidenciary case law sufficient to establish the partiality and dependence of the Russian judges when setting aside the four arbitral awards in question. As these reasons constitute a violation of Dutch *ordre public*, the judgment of the Russian courts is to be ignored under the New York Convention and does not hinder the enforcability of the four awards in the Netherlands.

Upcoming events

- 4 and 5 June 2009: International Law Conference on Commercial Contracts and Dispute Resolution during the Economic Crisis, organised by Capital Business Events Ltd. together with the Chamber of Commerce and Industry of the Russian Federation in Moscow
- 11 and 12 June 2009: Latin American Arbitration Conference, organised by the Center for the Studies of Law, Economy and Politics in Asuncion, Paraguay

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