NETHERLANDS: Ecuador loses set-aside action

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The District Court in The Hague

A court in The Hague has refused to set aside three UNCITRAL awards rendered in favour of US oil company Chevron against Ecuador. **Stan Putter**, an associate at Eversheds in Amsterdam, reports.

Stan Putter

On 2 May 2012, the District Court of The Hague ruled, at first instance, on Ecuador's application to set aside three awards rendered in favour of Chevron and its subsidiary, Texaco, by an UNCITRAL tribunal seated in The Hague and administered by the Permanent Court of Arbitration (case no. 2007-2). The case concerned the failure of the Ecuadorean courts to resolve multiple contractual disputes over 15 years – and is not to be confused with Chevron's other PCA-administered case against Ecuador, which concerns the US$18 billion judgment on environmental liability rendered against the company by a local court.

Background to the case

The arbitral tribunal (composed of **Karl-Heinz Böckstiegel**, **Albert Jan van den Berg** and **Charles N Brower**) rendered three separate awards in that arbitration:

- an award on jurisdiction dated 1 December 2008, in which the tribunal's jurisdiction was upheld;
- an award on liability dated 30 March 2010, holding Ecuador liable for breach of the US-Ecuador bilateral investment treaty because of the undue delay of the Ecuadorean courts in deciding several court cases; and
- an award on quantum dated 31 August 2011, ordering Ecuador to pay over US$96 million (including interest).

Ecuador made two applications to set aside these awards. As a matter of Dutch law, applications for the set-aside of an interim award (on jurisdiction) have to be filed simultaneously with the application for set-aside of a subsequent (partial) final award. Therefore Ecuador first made the application to set aside the award on jurisdiction as well as the award on liability. After the award on quantum was rendered, Ecuador made a second application to set this award aside as well.

The district court decided to assess these related cases together.

Ecuador's set-aside grounds

Ecuador referred to the same set-aside grounds in both cases, namely:

- the lack of a valid arbitration agreement (article 1065(1)(a) of the Dutch arbitration act);
- the arbitral tribunal exceeded its mandate (article 1065(1)(c)); and
- the award has not properly been reasoned (article 1065(1)(d)).

This report will examine Ecuador's arguments concerning each ground and the court's response in turn.

Lack of a valid arbitration agreement

Judicial review of the existence of a valid arbitration agreement is exercised in full in the Netherlands since to do otherwise, thereby allowing parties to disregard the fundamental right to have disputes decided by national courts, would violate both the Dutch Constitution as well as article 6 of the European Convention on Human Rights. The other set-aside grounds are only subject to limited review.

The key question that the district court had to decide was the scope of the full judicial review on the validity of an arbitration agreement in set-aside proceedings in the Netherlands.

Ecuador argued that no valid arbitration agreement existed since article 6 of the Ecuador-US BIT (on dispute resolution) has to be interpreted in connection with article 12 of the BIT, which provides that the BIT is only applicable to those investments which existed on or after the date of the BIT's entry into force. Ecuador argued that only those disputes that existed on or after 11 May 1997 could fall within the scope of the arbitration agreement. Further, as the relevant concession agreement had been terminated and wound-up prior to the BIT's entry into force, Ecuador argued that Chevron and Texaco had no investment within the meaning of the BIT (despite the pending litigation in Ecuador).

The district court in The Hague concluded that its obligation to conduct a full judicial review of the validity of the arbitration agreement does not extend to deciding follow-on questions, such as whether article 12 of the BIT restricts the temporal scope of the arbitration agreement in article 6. The court found that the scope of the protection of the BIT was in the jurisdiction of the arbitral tribunal to decide.

The court concluded that a valid arbitration agreement existed because Ecuador did not contest that:

- the disputes between the parties arose out of or in connection with the concession agreement, which can be defined as an investment agreement in the sense of article 6(1)(a) of the BIT; and
- the dispute concerns an alleged breach of a right created in the BIT with respect to an investment (article 6(1)(c)).

Excess of mandate and lack of reasoning

The court dealt simultaneously with Ecuador's two other set-aside grounds – that the tribunal exceeded its mandate; and the awards were not (sufficiently) reasoned.

Ecuador made three main arguments in this context, alleging that the arbitral tribunal:

- failed to take into account a multitude of Ecuador's essential defences;
- went beyond the scope of the parties' dispute in relation to Ecuador's "*loss of chance*" defence (see below); and
- failed to apply customary international law.

Unlike the full judicial review of the validity of an arbitration agreement, Dutch law allows a judge only a limited review of awards on these set-aside grounds. Regarding the insufficient reasoning ground, Dutch courts will only set aside awards that lack reasoning in their entirety or in which reasoning is so poor that it has to be equated with lack of reasoning (as a sound explanation for the decision cannot be recognised in the award). How explicit the reasoning should be also depends on the nature of the argument seen in light of the entire dispute, but more or less explicit reasoning is required when addressing a party's essential defences.

Ecuador argued that the following five essential defences were not addressed by the arbitral tribunal:

- that the language of article 1(1)(a)(iii) of the BIT (which allows claims for money or performance "associated with an investment") is materially different from article 1139(j) of NAFTA, on which the tribunal relied in interpreting the BIT provision;

- the findings of two Ecuadorean court decisions rendered in 2009, *Amazonas Refinery* and *Imported Products*, relating to causation and quantum;
- that the arbitral tribunal was not allowed to assume the role of the Ecuadorean court by making its own independent judgment of the cases pending in Ecuador;
- the "*loss of chance"* principle (that the tribunal should only award damages corresponding to the likelihood of success the company would have had in the Ecuadorean courts, had a breach of international law not occurred); and
- that the position that Chevron and Texaco took in the *Aguinda* proceedings (a litigation commenced by Ecuadorean plaintiffs in the New York federal courts in 1993, which was dismissed after the companies argued that the Ecuadorean courts were a preferable forum for the dispute) is incompatible with their "*undue delay"* arguments in this arbitration.

In short, the district court found that the arbitral tribunal had provided sufficient reasoning for its dismissal of all these essential defences and that the provided reasoning in each instance was more or less explicit and could not be regarded as equating to no reasoning at all. The application to set aside the awards on the ground that essential defences were not taken into account was therefore dismissed.

Ecuador's request to set aside the awards on the basis of the non-application of the "loss of chance" principle was also found to be not sufficiently substantiated to be considered by the court.

The state's argument that the arbitral tribunal had failed to apply customary international law was also rejected. The court held that the arbitral tribunal had provided sufficient reasons for its decision to regard article 2(7) of the BIT (guaranteeing "effective means of asserting claims and enforcing rights") as a *lex specialis* and not a mere restatement of the customary law principle of *denial of justice*.

Conclusion

In conclusion, the one thing that may be taken away from this judgment, from the perspective of Dutch arbitration law, is that the district court's approach towards judicial review of an arbitration agreement may be interpreted as being more restrictive than the prescribed full judicial review we have previously seen.

An official translation of the Dutch court's decision is accessible here.