Applicable Law and Sovereign Immunity

Complex Contract Negotiations in the Energy Sector
Energy Charter Workshop

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I. Applicable law to international transactions

II. Sovereign immunity in international arbitration
I. Applicable law to international transactions

1. Private Autonomy

2. Absence of choice

3. Applicable law to arbitration agreements
1. The reign of private autonomy

Arbitration

**Article 1496**

The arbitrator shall decide the dispute in accordance with the rules of the law chosen by the parties.

**UNCITRAL Model Law on International Commercial Arbitration (1985), with amendments as adopted in 2006**

**French Civil Code, Book IV (1981)**

**Article 21**

Applicable Rules of Law

1. The parties shall be free to agree upon the rules of law to be applied by the arbitral tribunal to the merits of the dispute.

**Arbitration Rules of the International Chamber of Commerce (2012)**
1. The reign of private autonomy

*Which rules of law can be chosen by the parties?*

- **State Law**
  - The law of State X

- **International Conventions**

- **Lex mercatoria**
  - UNIDROIT Principles
  - Incoterms
1. The reign of private autonomy

*Renvoi* and *Dépeçage*

- **Renvoi** (exclusion)
  - The choice of the law of any a State means the application of the rules of law in force in that State other than its rules of private international law

- **Dépeçage**
  - Different aspects of the contract are governed by different norms
1. The reign of private autonomy

Limits to party autonomy

Article 9

Overriding mandatory provisions

1. Overriding mandatory provisions are provisions the respect for which is regarded as crucial by a country for safeguarding its public interests, such as its political, social or economic organisation, to such an extent that they are applicable to any situation falling within their scope, irrespective of the law otherwise applicable to the contract under this Regulation.

2. Nothing in this Regulation shall restrict the application of the overriding mandatory provisions of the law of the forum.

3. Effect may be given to the overriding mandatory provisions of the law of the country where the obligations arising out of the contract have to be or have been performed, in so far as those overriding mandatory provisions render the performance of the contract unlawful. In considering whether to give effect to those provisions, regard shall be had to their nature and purpose and to the consequences of their application or non-application.

1. The reign of private autonomy

Limits to party autonomy

UNCITRAL Model Law on International Commercial Arbitration (1985), with amendments as adopted in 2006, article 34


(2) An arbitral award may be set aside by the court specified in article 6 only if:

(b) the court finds that:

(i) the subject-matter of the dispute is not capable of settlement by arbitration under the law of this State; or

(ii) the award is in conflict with the public policy of this State.

Article V

2. Recognition and enforcement of an arbitral award may also be refused if the competent authority in the country where recognition and enforcement is sought finds that:

(a) The subject matter of the difference is not capable of settlement by arbitration under the law of that country; or

(b) The recognition or enforcement of the award would be contrary to the public policy of that country.
1. The reign of private autonomy

**Investment disputes**

*Article 42*

(1) The Tribunal shall decide a dispute **in accordance with such rules of law as may be agreed by the parties.**

Convention on the Settlement of Investment Disputes Between States and Nationals of Other States (1965)

1. The arbitral tribunal shall apply the rules of law **designated by the parties** as applicable to the substance of the dispute. Failing

UNCITRAL Arbitration Rules (2010), article 35

*Article 22 Applicable law*

(1) The Arbitral Tribunal shall decide the merits of the dispute on the basis of the law(s) or rules of law agreed upon by the parties. In the absence of such agreement, the Arbitral


(6) A tribunal established under paragraph (4) shall decide the issues in dispute in accordance **with this Treaty and applicable rules and principles of international law.**

I. The reign of private autonomy

**Investment disputes**


  “The applicable law is the ECT and applicable rules and principles of international law, which encompasses EU law, which forms not only part of EU member states’ national law but also of international law”

- *AES v. Hungary* (ICSID Case No. ARB/07/22), Award of September 23, 2010

  “Community competition law regime should be considered as a fact, it will be considered by this Tribunal as a fact, always taking into account that a state may not invoke its domestic law as an excuse for alleged breaches of its international obligations”
1. The reign of private autonomy

*Investment disputes*

*Stabilization*

- ECT, article 10(1): “each contracting Party shall, in accordance with the provisions of this Treaty, encourage and create stable … conditions for investors of other Contracting Parties…”

- AES v. Hungary: “The stable conditions that the ECT mentions relate to the framework within which the investment takes place. Nevertheless, it is not a stability clause. A legal framework is by definition subject to change as it adapts to new circumstances day by day and a state has the sovereign right to exercise its powers which include legislative acts”
1. The reign of private autonomy

*Investment disputes*

- Burlington v. Ecuador

“Modification to the tax system: In the event of a modification to the tax system or the creation or elimination of new taxes not foreseen in this Contract, which have an impact on the economics of this Contract, a correction factor will be included in the production sharing percentages to absorb the impact of the increase or decrease in the tax”
2. In absence of choice by the parties

Who will judge?

- Purely commercial dispute
  - National tribunals or courts of a State
  - Arbitral Tribunal (e.g., under the ICC Rules of Arbitration)

- Investment Dispute (e.g., under the Energy Charter Treaty)
  - Courts or administrative tribunals of the State party to the dispute
  - Arbitral Tribunal
    - ICSID Convention
    - UNCITRAL Arbitration Rules
    - Arbitration Rules of the Stockholm Chamber of Commerce
2. In absence of choice by the parties

*Arbitration rules*

- **Arbitration Rules of the Stockholm Chamber of Commerce, article 22:**
  - The law or rules of law which the tribunal considers to be *most appropriate*

- **ICC Arbitration Rules, article 21:**
  - The rules of law which the tribunal determines to be *appropriate*. The tribunal shall take account of the provisions of the contract, if any, between the parties and of any relevant trade usages

- **UNCITRAL Arbitration Rules, article 35:**
  - The law which it determines to be *appropriate*. In any case, the tribunal shall decide in accordance the terms of the contract and the usages of the trade applicable to the transaction
2. In absence of choice by the parties

Which are the appropriate rules of law?

- UNCITRAL Model Law, article 28:
  - The law determined by the conflict of laws rules which it considers applicable
  - The terms of the contract and the usages of the trade applicable to the transaction
2. In absence of choice by the parties

*Which are the appropriate rules of law?*

- The “Rome I Regulation”, article 4:
  - The *characteristic performance*
  - The law of the country with which the contract is most closely connected
2. In absence of choice by the parties

*The ICSID Convention*

- ICSID Convention, article 42:
  - The law of the Contracting State party to the dispute (including its rules on the conflict of laws) and such rules of international law as may be applicable
3. Applicable Law to the arbitration agreement

Concluding remarks on applicable law

- The parties can choose the rules of law applicable to their contracts and disputes. When they agree on arbitration, the parties have even broader freedom to choose the applicable law pursuant to domestic arbitration statutes.

- While, in absence of choice, the law or rules of law that may apply can be predicted to some extent, parties should always choose the applicable law to avoid unnecessary delays.

- The law governing the contract does not necessarily applies to the arbitration agreement.

- Domestic regulations often restrict the State or State-owned entities’ discretion to choose a foreign law to govern their contracts.

- International transactions concerning economic activities in the Energy Sector are often governed by the law of the country where the activity is being performed. Investment disputes under the ECT, are governed primarily by the ECT.
II. Sovereign immunity in international arbitration

1. Definition of sovereign immunity: immunity from jurisdiction vs. immunity from execution

2. Exceptions and waiver of immunity
   - From jurisdiction
   - From execution

3. Model clause for waiver of immunity
1. Definition of sovereign immunity

“Concerns the privileges and rights given to a state, its government, representatives and property within the national legal systems of other states” (Dixon, 2007:182)
1. Definition of sovereign immunity

2004 UN Convention on Jurisdictional Immunities of States and Their Property

**Article 5**

**State immunity**

A State enjoys immunity, in respect of itself and its property, from the jurisdiction of the courts of another State subject to the provisions of the present Convention.
1. Definition of sovereign immunity

Immunity from **jurisdiction** vs immunity from execution

- **Immunity from jurisdiction**
  - Limits foreign courts’ adjudicatory powers
  - Protects States from judicial proceedings in foreign courts

- **Immunity from execution**
  - Limits foreign courts or other organs’ enforcement powers
  - Protects States’ property from seizure
1. Definition of sovereign immunity
   Immunity from *jurisdiction* vs immunity from execution

- **Absolute vs Restrictive sovereign immunity**
  - Recent move from absolute to restrictive immunity
    - Exceptions to state immunity
    - State consent

- **Immunity as a rule-exception relationship**
  (Finke, 2011)
2.1. Exceptions and waiver of immunity from jurisdiction

- *Acta jure imperii* vs *Acta jure gestionis*
- Implicit waiver through arbitration agreement

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2004 UN Convention on Jurisdictional Immunities of States and Their Property

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**Article 17**

**Effect of an arbitration agreement**

If a State enters into an agreement in writing with a foreign natural or juridical person to submit to arbitration differences relating to a commercial transaction, that State cannot invoke immunity from jurisdiction before a court of another State which is otherwise competent in a proceeding which relates to:

(a) the validity, interpretation or application of the arbitration agreement;
(b) the arbitration procedure; or
(c) the confirmation or the setting aside of the award, unless the arbitration agreement otherwise provides.
2.2. Exceptions and waiver of immunity from execution

- The purpose of the property seized
  - Immunity will generally be **granted** for **property serving sovereign purposes**
  - Immunity will generally **not be granted** in connection with **property serving non-sovereign purposes**

- Is there an implicit waiver of immunity from execution when there is an arbitration agreement?
2.2. Exceptions and waiver of immunity from execution

The ICSID Convention

1965 Washington Convention on the Settlement of Investment Disputes (ICSID Convention)
2.2. Exceptions and waiver of immunity from execution
The ICSID Convention

“Article 55 may be seen as the **Achilles’ heel of the Convention**. The otherwise effective machinery of arbitration has its weak point when it comes to the actual execution against States of pecuniary obligations under awards.” (Schreuer, 2009: 1154)
2.2. Exceptions and waiver of immunity from execution
The ICSID Convention

- **CMS Gas Transmission Company v. Argentina** (Case No: 12-4139-CV) The US Court of Appeal’s decision on the challenge to execution of enforcement order due to sovereign immunity

- **AIG Capital Partner, Inc. and others v. The Republic of Kazakhstan** (Case No: 2004/536) The High Court of England and Wales’s decision on the challenge to execution of enforcement order due to sovereign immunity
2.2. Exceptions and waiver of immunity from execution
The New York Convention

1958 Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the “New York Convention”)

Article III

Each Contracting State shall recognize arbitral awards as binding and enforce them in accordance with the rules of procedure of the territory where the award is relied upon, under the conditions laid down in the following articles. There shall not be imposed substantially more onerous conditions or higher fees or charges on the recognition or enforcement of arbitral awards to which this Convention applies than are imposed on the recognition or enforcement of domestic arbitral awards.
2.2. Exceptions and waiver of immunity from execution

The New York Convention

- **Seldemayer v. Russian Federation**
  - Case No. Ö 170-10/NJA 2011 s. 75: Decision of the Swedish Supreme Court on the challenge to execution of enforcement order due to sovereign immunity, July 1\textsuperscript{st} 2011
  - Case No. 92/W2: Decision of the German Federal Supreme Court on the challenge to execution of enforcement order due to sovereign immunity
2.2. Exceptions and waiver of immunity from execution
The New York Convention

- Noga v. Russian Federation
  - Case No. 00/04888: Decision of the French Rennes Court of Appeal on the challenge to execution of enforcement order due to sovereign immunity
3. Model clause for waiver

Based on the Model Mine Development Agreement of the International Bar Association

*The State irrevocably waives any claim to state or sovereign immunity: (i) in respect to proceedings on the merits of any claim which is the subject matter of the arbitration* [insert cross reference to the arbitration clause]; (ii) in respect of proceedings to recognize or to enforce or to execute any arbitration award including, without limitation, immunity from service of process and from the jurisdiction of any court; and (iii) in respect of the execution of any such award against the assets or property of the State assets held by the State for commercial purposes or otherwise.
Conclusions on sovereign immunity

- In principle, States enjoy an immunity from jurisdiction and an immunity from execution.
- There has been a gradual move from absolute to restrictive immunity.
- An arbitration agreement can be considered as an implicit waiver of immunity from jurisdiction, not necessarily from execution.
- There is significant variation in the application of immunity from execution across national jurisdictions.