

**INTERNATIONAL CENTRE FOR SETTLEMENT  
OF INVESTMENT DISPUTES**

**IN THE PROCEEDING BETWEEN**

**OCCIDENTAL PETROLEUM CORPORATION  
OCCIDENTAL EXPLORATION AND PRODUCTION COMPANY  
(CLAIMANTS)**

**- AND -**

**THE REPUBLIC OF ECUADOR  
(RESPONDENT)**

(ICSID Case No. ARB/06/11)

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**DECISION ON JURISDICTION**

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Mr. David A.R. Williams, Q.C., Arbitrator  
Professor Brigitte Stern, Arbitrator

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Date: 9 September 2008

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## **I. INTRODUCTION**

1. In this Decision on Jurisdiction, the Tribunal addresses and rules upon objections put forward by the Respondent regarding the Tribunal's jurisdiction over the Claimants' claims in this ICSID proceeding.

2. The Tribunal notes at the outset that the Respondent's jurisdictional objections have been submitted in accordance with Rule 41 of ICSID's Rules of Procedure for Arbitration Proceedings (Arbitration Rules). Rule 41 reads as follows:

### **“Rule 41 Preliminary Objections**

(1) Any objection that the dispute or any ancillary claim is not within the jurisdiction of the Centre or, for other reasons, is not within the competence of the Tribunal shall be made as early as possible. A party shall file the objection with the Secretary-General no later than the expiration of the time limit fixed for the filing of the counter-memorial, or, if the objection relates to an ancillary claim, for the filing of the rejoinder—unless the facts on which the objection is based are unknown to the party at that time.

(2) The Tribunal may on its own initiative consider, at any stage of the proceeding, whether the dispute or any ancillary claim before it is within the jurisdiction of the Centre and within its own competence.

(3) Upon the formal raising of an objection relating to the dispute, the Tribunal may decide to suspend the proceeding on the merits. The President of the Tribunal, after consultation with its other members, shall fix a time limit within which the parties may file observations on the objection.

(4) The Tribunal shall decide whether or not the further procedures relating to the objection made pursuant to paragraph (1) shall be oral. It may deal with the objection as a preliminary question or join it to the merits of the dispute. If the Tribunal overrules the objection or joins it to the merits, it shall once more fix time limits for the further procedures.

(5) Unless the parties have agreed to another expedited procedure for making preliminary objections, a party may, no later than 30 days after the constitution of the Tribunal, and in any event before the first session of the Tribunal, file an objection that a claim is manifestly without legal merit. The party shall specify as precisely as possible the basis for the objection. The Tribunal, after giving the parties the opportunity to present their observations on the objection, shall, at its

first session or promptly thereafter, notify the parties of its decision on the objection. The decision of the Tribunal shall be without prejudice to the right of a party to file an objection pursuant to paragraph (1) or to object, in the course of the proceeding, that a claim lacks legal merit.

(6) If the Tribunal decides that the dispute is not within the jurisdiction of the Centre or not within its own competence, or that all claims are manifestly without legal merit, it shall render an award to that effect.”

3. The Tribunal recalls that this ICSID proceeding was initiated on 17 May 2006 by the Claimants, Occidental Petroleum Corporation (“OPC”) and Occidental Exploration and Production Company (“OEPC”), with the filing of a Request for Arbitration against the Respondent, the Republic of Ecuador.<sup>1</sup>

4. The Tribunal held its First Session with the parties on 2 May 2007. In the Minutes of the First Session, it was contemplated, *inter alia*, that objection(s) by the Respondent to the Tribunal’s jurisdiction, if any, were to be made by no later than 15 September 2007.<sup>2</sup>

5. A request for a postponement of this deadline, however, was subsequently made on behalf of the Respondent who changed its counsel. The process of appointing new counsel was in fact a time-consuming one, with new counsel’s formal appointment only confirmed in late December 2007. In the fullness of time, on 11 February 2008, the Tribunal issued its first Procedural Order directing a revised procedural calendar, including a timetable for the jurisdictional phase of this proceeding.

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<sup>1</sup> The Request was initially directed against both Ecuador and the Ecuadorian entity known as “Petroecuador”, but the Claimants subsequently abandoned their claims against Petroecuador.

<sup>2</sup> See revised Minutes of the First Session at paragraph 16(2).

6. Pursuant to the Tribunal's Procedural Order No. 1, the parties' pleadings in this jurisdictional phase were submitted as follows:

- Respondent's Objections to Jurisdiction dated 7 March 2008;
- Claimants' Answer on Jurisdiction dated 4 April 2008;
- Respondent's Reply on Jurisdiction dated 23 April 2008; and
- Claimants' Rejoinder on Jurisdiction dated 12 May 2008.

7. As directed by the Tribunal's Procedural Order No. 1, a two-day Hearing on Jurisdiction was held in Paris on 22-23 May 2008 (the "Hearing").

8. During the Hearing, the Tribunal heard from the parties' respective counsel who made extensive opening and closing submissions on the various issues raised by the Respondent's jurisdictional challenge. The parties' experts, namely Dr. Juan Pablo Aguilar Andrade for the Respondent, and Mr. Hernán Pérez Loose for the Claimants, also appeared as witnesses at the Hearing.

## **II. FACTUAL BACKGROUND**

9. For purposes of this Decision on Jurisdiction, the Tribunal need not provide a detailed account of the factual background of the dispute between the parties. Rather, the Tribunal will limit itself to summarizing a few facts pertinent to this jurisdictional phase. However brief, this summary is not to be taken as prejudging in any way the issues of fact or law to be resolved at the merits phase of this arbitration.

10. In brief, this arbitration concerns various alleged breaches by Ecuador under both domestic law and international law, as well as under the Treaty between the United States of America and The Republic of Ecuador Concerning the Encouragement and Reciprocal Protection of Investment (the “Treaty” or “BIT”). In addition, the Claimants rely on an agreement referred to as the “Participation Contract” dated 21 May 1999 between OEPC, Ecuador and Petroecuador in connection with the exploration and exploitation of hydrocarbons in what has been labelled “Block 15” of the Ecuadorian Amazon.

11. Pursuant to the Participation Contract and related “Operating Agreements” for the unified fields of Edén-Yuturi and Limoncocha, OEPC was granted the exclusive right to carry out exploration and exploitation activities in the area assigned to it, namely Block 15.

12. In October 2000, OEPC entered into two agreements (the “AEC Farmout Agreement” and the “AEC Operating Agreement”, together the “AEC Agreements”) with City Investing Company Ltd. (now known as AEC Ecuador Ltd., “AEC”), a Bermuda subsidiary of EnCana Corporation, a Canadian oil and gas company. Pursuant to the AEC Agreements, OEPC and AEC concluded a two-phase transaction.

13. In a first phase, OEPC granted to AEC a 40% economic interest in the share of the production from Block 15 that accrued to OEPC under the Participation Contract and the Operating Agreements. In exchange for this share in oil produced from Block 15, AEC agreed to pay to OEPC both (i) a series of certain annual amounts over a four-year period to contribute towards capital investments in Block 15 and (ii) 40% of the operating

costs incurred by OEPC. Section 2.01 of Article II of the AEC Farmout Agreement states that:

“OEPC agrees to [...] farm out and transfer to AEC [...] a 40% economic interest (the ‘Farmout Interest’) in the Farmout Property [...]. The Farmout Interest to be transferred to AEC [...] does not include nominal legal title to an interest in Block 15 or an interest as a party to the [Block 15] Agreements. OEPC shall continue to own 100% of the legal title to the [Block 15] Agreements and to the interest in Block 15 granted or provided for in the [Block 15] Agreements.”

14. In a second phase, it was contemplated that after AEC had made all required payments at the end of the four-year period, and subject to OEPC then obtaining the necessary government approvals, OEPC would assign legal title to AEC. The second stage is described in Section 4.01 of Article IV of the Farmout Agreement:

“[A]fter AEC has made all payments [...] OEPC and AEC shall execute and deliver such documents as are required to convey legal title to AEC in and to a 40% economic interest in the [Block 15] Agreements and Block 15 and to make AEC a party to the [Block 15] Agreements as owner of such 40% economic interest (subject to obtaining required governmental approvals).”

15. On 1 November 2000, OPC issued a press release announcing the AEC Agreements. The press release confirmed that OEPC would remain the operator of Block 15 and that AEC would receive a 40% economic interest in the operations.

16. In 2004, after AEC had made the payments due under the AEC Farmout Agreement, OEPC requested approval from the Ecuadorian government to proceed with the transfer of legal title. The approval was not granted.

17. Rather, on 24 August 2004, citing the AEC Agreements as well as a number of alleged violations represented by the National Hydrocarbons Department (“DNH”) to be breaches of the Participation Contract, the Attorney General of Ecuador issued orders to

the Ministry of Mines and Energy to terminate the Participation Contract and the Operating Agreements through a declaration of “*caducidad*”.

18. On 8 September 2004, the Minister of Energy and Mines instructed the Executive President of Petroecuador to initiate the *caducidad* procedure. The Executive President of Petroecuador did so, on 15 September 2004, by sending OEPC a notice of alleged breaches of the Participation Contract. The notice quoted the allegations that the Attorney General had made in his 24 August 2004 letter, and concluded that *caducidad* should be declared because OEPC had allegedly: (i) transferred rights and obligations under the Participation Contract to AEC without ministerial approval; (ii) entered into a consortium or association to carry out exploration or exploitation operations without ministerial approval; (iii) not invested the minimum amounts required under the Participation Contract; and (iv) repeatedly committed violations of the Hydrocarbons Law and regulations.

19. During the following 18 months or so, OEPC made a number of submissions seeking to rebut the allegations made by the Attorney General, but to no avail.

20. On 15 May 2006, the Minister of Energy and Mines notified OEPC of his decision to terminate the Participation Contract by declaring its *caducidad*. The Claimants filed their Request for Arbitration two days later on 17 May 2006.

21. The relief sought by the Claimants in their Request for Arbitration is set forth as follows:

“Claimants respectfully request an award in their favor,



- (a) Declaring that Respondents have breached their obligations under the Participation Contract and the Operating Agreements, the Treaty, and Ecuadorian and international law;
- (b) Ordering Respondents to declare null and void the *Caducidad* Decree and to reinstate fully OEPC's rights under the Participation Contract and the Operating Agreements;
- (c) Directing Respondents to indemnify Claimants for all damages caused as a result of their breaches, including costs and expenses of this proceeding, in amounts to be determined at the hearing, which Claimants believe will exceed US\$1 billion;
- (d) Directing Respondents to pay Claimants interest on all sums awarded, in amounts to be determined at the hearing, and to order any such further relief as may be available and appropriate in the circumstances."

22. The Claimants' prayer for relief was subsequently articulated as follows in their Memorial on Damages dated 17 September 2007:

"Claimants respectfully request the Tribunal:

- (a) To declare that Ecuador has breached its obligations under the Treaty and international law;
- (b) To declare that Ecuador has breached its obligations under the Participation Contract and Ecuadorian law;
- (c) To order Ecuador to pay Claimants the fair market value of the Participation Contract, in the amount of \$2.705 billion;
- (d) To order Ecuador to pay Claimants consequential damages in the amount of \$201.2 million;
- (e) To order Ecuador to pay interest on the amounts under (c) and (d) at the monthly rate of United States T-Bills compounded monthly, through the date of full and affective payment of those amounts; and
- (f) To order Ecuador to reimburse Claimants all their reasonable legal costs and fees."

23. It is against this background that the Respondent maintains that the Tribunal does not have jurisdiction over the Claimants' claims.

### **III. OVERVIEW OF THE JURISDICTIONAL OBJECTIONS**

24. At the outset, the Tribunal observes that the Respondent has submitted two separate objections to jurisdiction. Firstly, the Respondent argues that the Tribunal does not have jurisdiction over the parties' dispute because adjudication of this dispute is subject to Clauses 21.4 and 22.2.1 of the Participation Contract which, it maintains, "carve out" and/or waive *caducidad* from arbitration. This, according to the Respondent, is the inevitable consequence of the Ecuadorian law principle according to which *caducidad* decrees such as the one at issue in this arbitration carry a presumption of legality and may only be challenged before the Ecuadorian administrative courts. Secondly, the Respondent maintains that the Claimants failed to comply with the six-month waiting period under the Treaty before submitting their Request for Arbitration and, furthermore, that the Claimants' claims are premature.

25. The Respondent has articulated the relief it seeks in this jurisdictional phase as follows:

"Accordingly, for the reasons given in Ecuador's Objections to Jurisdiction and in this submission, and reserving the right to further develop and expand its submissions in view of the Claimants' subsequent written and oral submissions, Ecuador reaffirms its request for the following relief:

- (i) a declaration that the Tribunal has no jurisdiction over the Claimants' claims;
- (ii) an order that the Claimants pay the costs of these arbitral proceedings, including the cost of the Tribunal and the legal and other costs incurred by Ecuador on a full indemnity basis; and

- (iii) interest on any costs awarded to Ecuador, in an amount to be determined by the Tribunal.

In the alternative, should the Tribunal find that it has jurisdiction over the Claimants' claims, Ecuador requests:

- (i) an order that this arbitration be stayed until OEPC challenges the *Caducidad* Decree in the competent Ecuadorian administrative court and that court issues a final ruling on such challenge;
- (ii) an order that the Claimants pay the costs of these arbitral proceedings, including the cost of the Tribunal and the legal and other costs incurred by Ecuador on a full indemnity basis; and
- (iii) interest on any costs awarded to Ecuador, in an amount to be determined by the Tribunal.”

26. In response, the Claimants argue that neither Clause 21.4 nor Clause 22.2.1 exclude *caducidad*-related disputes from arbitration. The Claimants observe that Clause 21.4 is part of Section 21 of the Participation Contract which is entitled “Termination and *Caducidad* of this Participation Contract”. This section, they point out, sets forth the various procedures to be followed prior to proceeding to lawful termination of the parties' agreement. According to the Claimants, Clause 21.4 establishes that procedure where the termination is requested for reasons other than *caducidad*. The Claimants also dismiss the contention of the Respondent that Clause 22.2.1 can be construed as a waiver of ICSID jurisdiction over *caducidad*-related disputes. They allege that there is no clear and unequivocal language to this effect in the clause.

27. The Claimants add that even if the Respondent's interpretation of Clause 21.4 and/or Clause 22.2.1 were accepted by the Tribunal, OPC's and OEPC's Treaty claims would survive, as would OEPC's contract claims by virtue of Article VI.2 of the Treaty.

28. As for the Respondent's allegation that the Claimants have failed to comply with the six-month waiting period under the Treaty, the Claimants maintain that this objection is incompatible with the Respondent's first objection which is based on the Participation Contract, not the Treaty. They add that the dispute at issue in fact arose as early as September 2004 (over eighteen months prior to the *Caducidad* Decree) and that in any event, an investor is not required to respect a waiting period if attempts at a negotiated solution have proven futile. The Claimants also reject the Respondent's contention that their claims are premature.

29. The Claimants accordingly request that the Tribunal dismiss the Respondent's jurisdictional objections in their entirety, and further award all the costs of this phase of the proceeding to them.

30. At this juncture, before addressing the parties' submissions in more detail, the Tribunal will recite certain provisions of the Participation Contract and the Treaty which it is called upon to interpret and analyze in order to decide the Respondent's jurisdictional challenge.

31. The Participation Contract contains the following dispute resolution framework:

**“TWENTY: CONSULTANTS AND ARBITRATION.**

**20.1 Consultants.-** Disagreements arising between the Parties over technical matters that involve economic considerations and vice-versa, except those matters which under this Contract or the Law must be submitted to decision by competent authority, shall be submitted to the consideration of the legal representatives of the Parties for resolution. If within a period of ten (10) days after one of the Parties has sent the disagreement to the other, same has not been resolved, the Parties shall submit the disagreement to a Consultant, except if the Parties have agreed in writing to extend this term in specific cases.

[...]

**20.2 Arbitration.-** If the disagreements are related to any other matter not included within the scope of Clause 20.1, or if the Parties agree that, for whatever reason, submitting the disagreement to a consultant does not provide a final and mandatory decision, all controversies shall be substantiated through arbitration under law, as established in Art. 10 of the Hydrocarbons Law and the Law on Arbitration and Mediation published in the Official Gazette No. 145 of September 4, 1997, and in accordance with the rules and procedures in this clause.

[...]

**20.3** Notwithstanding the foregoing provisions, from the date on which the Agreement on the Settlement of Differences Relative to Investments among States and the Nationals of Other States (the ‘Agreement’) signed by the Republic of Ecuador as a Member State of the International Bank for Reconstruction and Development, on January 15, 1986 and published in Official Gazette No. 386 of March 3, 1986, is ratified by Congress of Ecuador, the Parties agree to submit their controversies or differences that are related to or arise from the performance of this Participation Contract, to the jurisdiction and competence of the International Center for the Settlement of Investment-Related Differences (‘CIADI’) so that they be arranged and resolved according to the provisions of said Agreement. Under this system of arbitration, the following provisions shall be applied:

[...]

**20.4** Additionally, and without prejudice to the provisions in Clauses 20.2. and 20.3. of this Participation Contract, the Parties agree to submit any difference relating to investments to Treaties, Conventions, Protocols and other acts under international law, signed and ratified by Ecuador in accordance with the Law.”

32. Clause 21.4 of the Participation Contract, which is at the heart of the Respondent’s jurisdictional challenge, reads as follows:<sup>3</sup>

“**21.4.** The termination of this Participation Contract for any reason other than those that result in *caducidad* may be requested by either of the Parties, subject to

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<sup>3</sup> This is the translation put forward by the Respondent. The Claimants subsequently submitted that the translation of Clause 21.4 “was not very elegant”. They accordingly produced the following new certified translation: “The termination of the Participation Contract for any cause other than those that result in *caducidad* may be requested by either of the Parties following the procedures stipulated in Clause 20, absent an agreement between them.” The Respondent rejects this new translation, and maintains that the Respondent’s original translation accurately reflects the Spanish original. The Claimants have confirmed that “they are perfectly happy to work with either version”.

procedures stipulated in Clause 20 in the event that they fail to reach agreement.”<sup>4</sup>

33. Clause 22.2.1 of the Participation Contract is also noted:

“**22.2.1** In the event of controversies that may arise as a result of the performance of this Participation Contract, in accordance with Ecuadorian law, Contractor expressly waives its right to use diplomatic or consular channels, or to have recourse to any national or foreign jurisdictional body not provided for in this Participation Contract, or to arbitration not recognized by Ecuadorian law or provided for in this Participation Contract. Lack of compliance with this provision shall constitute grounds for the forfeiture of this Participation Contract.”

34. Moreover, of significance to the issue of jurisdiction is the following provision of the Treaty:

#### “ARTICLE VI

1. For purposes of this Article, an investment dispute is a dispute between a Party and a national or company of the other Party arising out of or relating to (a) an investment agreement between that Party and such national or company; (b) an investment authorization granted by that Party’s foreign investment authority to such national or company; or (c) an alleged breach of any right conferred or created by this Treaty with respect to an investment.

2. In the event of an investment dispute, the parties to the dispute should initially seek a resolution through consultation and negotiation. If the dispute cannot be settled amicably, the national or company concerned may choose to submit the dispute, under one of the following alternatives, for resolution;

(a) to the courts or administrative tribunals of the Party that is a party to the dispute; or

(b) in accordance with any applicable, previously agreed dispute-settlement procedures; or

(c) in accordance with the terms of paragraph 3.

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<sup>4</sup> The English translation of the Participation Contract attached to the Claimants’ Memorial on Liability (Exhibit CE-2) translates the word “*caducidad*” as “forfeiture”. Both the Claimants and the Respondent refer to the term “*caducidad*” in their pleadings since, pursuant to Clause 3.2, the original Spanish version of the Participation Contract prevails over any other version, including the English translation.

3. (a) Provided that the national or company concerned has not submitted the dispute for resolution under paragraph 2 (a) or (b) and that six months have elapsed from the date on which the dispute arose, the national or company concerned may choose to consent in writing to the submission of the dispute for settlement by binding arbitration:

(i) to the International Centre for the Settlement of Investment Disputes ('Centre') established by the Convention on the Settlement of Investment Disputes between States and Nationals of other States, done at Washington, March 18, 1965 ('ICSID Convention'), provided that Party is a party to such convention; or

(ii) to the Additional Facility of the Centre, if the Centre is not available; or

(iii) in accordance with the Arbitration Rules of the United Nations Commission on International Trade Law (UNCITRAL); or

(iv) to any other arbitration institution, or in accordance with any other arbitration rules, as may be mutually agreed between the parties to the dispute.

(b) Once the national or company concerned has so consented, either party to the dispute may initiate arbitration in accordance with the choice so specified in the consent.

4. Each Party hereby consents to the submission of any investment dispute for settlement by binding arbitration in accordance with the choice specified in the written consent of the national or company under paragraph 3. Such consent, together with the written consent of the national company when given under paragraph 3 shall satisfy the requirement for:

(a) written consent of the parties to the dispute for purposes of Chapter II of the ICSID Convention (Jurisdiction of the Centre) and for purposes of the Additional Facility Rules; and

(b) an 'agreement in writing' for purposes of Article II of the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards, done at New York, June 10, 1958 ('New York Convention').

5. Any arbitration under paragraph 3(a)(ii), (iii) or (iv) of this Article shall be held in a state that is a party to the New York Convention.

[...]"

35. Against this background, the Tribunal now turns to the parties' respective contentions regarding jurisdiction. As the Respondent is the moving party, the Tribunal

will consider its arguments first. The Tribunal will then review the Claimants' arguments.

#### IV. THE PARTIES' POSITIONS

##### ***1. The Respondent's First Objection: Adjudication of the Parties' Dispute Is Governed by the Participation Contract, Which Allegedly Excludes Caducidad from Arbitration***

###### **A. The Respondent's Position**

36. As indicated earlier, the Respondent's first jurisdictional objection is based on the allegation that the parties' dispute is governed by the Participation Contract, Clause 21.4 of which allegedly excludes *caducidad* from arbitration. The Respondent argues that the Claimants freely agreed that *caducidad* was to be non-arbitrable. In the words of the Respondent, "[t]hey cannot escape that agreement now".

37. According to the Respondent, Clause 21.4 of the Participation Contract is meant to serve as an exception to the availability of ICSID jurisdiction in the circumstances of the present case. Relying, *inter alia*, on this provision, the Respondent submits that Ecuadorian law, not the ICSID Convention, governs challenges to declarations of *caducidad*:

"The Ecuadorian Constitution confers exclusive jurisdiction to review the legality of unilateral administrative acts by the State to a contentious-administrative district court, which can then be appealed to the Contentious-Administrative Chamber of the Supreme Court. That exclusive jurisdiction is reflected in Article 1 of the Ecuadorian Law on Arbitration and Mediation (to which the Participation Contract is subject), which renders non-arbitrable those matters that fall within the exclusive jurisdiction of the courts – i.e., matters that are not susceptible to 'transaction' between the parties.

[...]



Having agreed that Ecuadorian law governs the Participation Contract, the Claimants were therefore bound to follow Ecuadorian law in challenging the *Caducidad* Decree. In particular, they were required to seek annulment of the *Caducidad* Decree before the Ecuadorian administrative courts by either filing a complaint against the Decree itself (*recurso de plena jurisdicción*) or by filing a claim of nullity (*recurso de nulidad*) seeking only to annul the Decree. They did neither. Thus, all other bodies, including this Tribunal, must presume the legality of such decisions and have no jurisdiction to adjudicate them.”

38. The Respondent avers in its Reply that disputes arising out of *caducidad* cannot be characterized as “contractual disputes”.<sup>5</sup> Rather, such disputes are “extra-contractual” in nature and, according to the Respondent, they are non-arbitrable pursuant to Article 4 of the Ecuadorian law on Mediation and Arbitration. The Respondent states that Clause 21.4 of the Participation Contract is merely a reflection of this principle, and further contends that its position on this point is supported by the ICSID case of *Repsol YPF Ecuador SA v. Empresa Estatal Petróleos del Ecuador (Petroecuador)*:<sup>6</sup>

“This interpretation is fully confirmed by international case law. The ICSID tribunal in *Repsol YPF Ecuador SA v. Empresa Estatal Petróleos de Ecuador (Petroecuador)* held that issues relating to the legality of administrative acts, such as the *Caducidad* Decree, are non-arbitrable under Ecuadorian law. Attempting to avoid the devastating implications of *Repsol*, the Claimants mischaracterize it as confirming ICSID jurisdiction over an administrative act with *res iudicata* effect. In fact, *Repsol* stands for precisely the opposite proposition.

[...]

Thus, the reasoning of the ICSID tribunal is twofold: (i) if the decision of the DNH had the effect of unilaterally modifying the contract, it would transform the issue from contractual into non-contractual (administrative); and (ii) only contractual issues are subject to ‘transaction’ and arbitration. This ‘transaction’ language is the same language reflected in Article 1 of the Ecuadorian Law on Arbitration and Mediation (to which the Participation Contract is subject), which

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<sup>5</sup> The Tribunal notes that, in its Objections to Jurisdiction, the Respondent argued the opposite. It wrote that *caducidad* was a contractual issue, not an extra-contractual one.

<sup>6</sup> ICSID Case No. ARB/01/10, Award dated 20 February 2004.

renders non-arbitrable those matters that fall within the exclusive jurisdiction of the courts – *i.e.*, matters that are not susceptible to ‘transaction’ between parties.”

39. In this connection, the Tribunal recalls that, in their written and oral pleadings, the Claimants stress that they are advancing both Treaty and contract claims, whereas the Respondent argues that the Claimants’ claims are fundamentally contractual in the sense that “the Participation Contract, by its terms, occupies the field with regard to a *caducidad* decree, such that the Claimants cannot seek recourse based on a declaration of *caducidad* in any other forum [*i.e.* the traditional avenues provided by Ecuadorian law]”.

40. At the Hearing, the Respondent expanded its Clause 21.4 argument by submitting that, in the event of a conflict between Ecuadorian law and the Participation Contract, the former trumps the latter. This, according to the Respondent, flows from the application of Clause 22.1.4 of the Participation Contract, which states:

**“22.1.4 Legal Framework:** Norms applicable to this Participation Contract, at the time of its execution, include but are not limited to the following:

**1.-** The Hydrocarbons Law, published in Official Gazette No. Seven hundred and eleven. (711) of November fifteenth (15), nineteen hundred and seventy eight. (1978).

[...]

**13.-** Arbitration and Mediation Law, published in Official Gazette No. One hundred and forty five (145), of September four (4), Nineteen hundred and ninety seven (1997).

[...]

In the event of a conflict between the above mentioned documents, the order of priority amongst them shall be the following: Laws, Regulations and this Participation Contract.” (emphasis added)

41. On the basis of this provision of the Participation Contract, the Respondent submitted as follows at the Hearing:

“With this in mind I would suggest to you that this is a further and strong reason to interpret Clause 21.4 exactly as Ecuador has stated, because that is the interpretation that avoids the conflict, and one should always presume that the parties did not enter into a contract which contained a fundamental conflict. But, if you don’t agree with that, then you end up with the conflict, and you must follow the directions in Clause 22.1.4 which says that the law on arbitration and mediation supersedes anything that conflicts in the contract.”

42. The Respondent characterizes its first jurisdictional objection as a double-hurdle.

In the words of the Respondent:

“There are two separate and distinct reasons why OEPC’s claims are non-arbitrable. First, disputes regarding a declaration of *caducidad* are inherently non-arbitrable under Ecuadorian law, which both Parties agree governs the Participation Contract. Second, the Participation Contract itself precludes ICSID arbitration regarding *caducidad*. Importantly, the Tribunal must overcome *both* hurdles before it can exercise jurisdiction of OEPC’s claims.” (emphasis in original)

43. The Respondent maintains that the Claimants are unable to overcome either hurdle.

44. In its Reply, the Respondent constructed an additional argument on the basis of Clause 22.2.1 of the Participation Contract which contains the following waiver language:

“**22.2.1** In the event of controversies that may arise as a result of the performance of this Participation Contract, in accordance with Ecuadorian law, Contractor expressly waives its right to use diplomatic or consular channels, or to have recourse to any national or foreign jurisdictional body not provided for in this Participation Contract, or to arbitration not recognized by Ecuadorian law or provided for in this Participation Contract. Lack of compliance with this provision shall constitute grounds for the forfeiture of this Participation Contract.” (emphasis added)

45. The Respondent contends as follows:

“ICSID arbitration in relation of *caducidad* is simply not an arbitration ‘recognized by Ecuadorian law or provided for in this Participation Contract,’ within the meaning of Clause 22.2.1. As set forth more fully below, Clause 20.4 does not change that interpretation, because Clause 21.4 and the other provisions discussed above operate as a limitation on the scope of treaty claims that potentially could be asserted by OEPC in connection with that Clause. Accordingly, OEPC clearly and unambiguously waived recourse to arbitration of *caducidad*-related matters in Clause 22.2.1 of the Participation Contract. The Tribunal should reject Claimants’ attempt to simply disregard the contractual limitations on the scope of ICSID jurisdiction.”

46. Finally, again as part of its Reply, the Respondent distinguishes its jurisdictional analysis as it relates, firstly, to OEPC and, secondly, to OPC. The former is a signatory to the Participation Contract, whereas the latter is not. Thus, according to the Respondent, OPC lacks standing to assert claims as an investor. Alternatively, the Respondent maintains that OPC is bound by the alleged exclusion of ICSID jurisdiction agreed by OEPC under the Participation Contract.

## **B. The Claimants’ Position**

47. In response to the Respondent’s first jurisdictional objection, to the extent that it is based on Clause 21.4, the Claimants maintain that it is both wrong and irrelevant for the following reasons:

“(i) Section 21 of the Participation Contract is not an arbitration clause. Rather, it is merely a provision which sets forth procedures to be followed in order to proceed to lawful termination of the Participation Contract. Clause 21.4 set forth therein is accordingly not meant to carve out disputes arising out of a declaration of *caducidad* from Clause 20.3 arbitration;

(ii) Even if the Respondent’s interpretation of Clause 21.4 were accepted – *i.e.* that it reflects a contractual agreement not to arbitrate unilateral termination

disputes – OPC’s Treaty claims would nonetheless survive because it is not a signatory to the Participation Contract;

(iii) The Respondent’s interpretation of Clause 21.4 – and the objection it advances on the basis of this interpretation – is based on the premise that the Claimants’ claims result from allegations of breach of the Participation Contract. Both OPC and OEPC, however, have primarily submitted Treaty claims, which survive regardless of the Respondent’s interpretation of Clause 21.4; and

(iv) OEPC’s contract claims survive regardless of the Respondent’s interpretation of Clause 21.4 because Article VI.2 of the Treaty entitles OEPC to choose ICSID arbitration instead of any contractual or statutory selection of the Ecuadorian administrative courts for the adjudication of its contract claims.”

48. At the outset, the Claimants stress that they have submitted their dispute with the Respondent to the Tribunal pursuant to the Treaty, not the Participation Contract. In the words of the Claimants:

“It is Claimants’ case that Article VI alone vests the Tribunal with jurisdiction over Claimants’ entire dispute with Ecuador, and only the terms of the provision govern the scope of the jurisdiction thus conferred. Only if the Tribunal were to find that Article VI does not vest it with jurisdiction over OEPC’s *contract* claims, Claimants submit that it would have such jurisdiction pursuant to Clause 20.3 of the Participation Contract.” (emphasis in original)

49. In any event, the Claimants contend that Clause 21.4 of the Participation Contract neither carves out disputes arising out of *caducidad* nor contains any affirmative choice in favor of the Ecuadorian administrative courts. Rather, according to the Claimants, Section 21, including Clause 21.4, sets forth procedures to be followed prior to proceeding to lawful termination. The Claimants’ interpretation of Clause 21.4 is articulated as follows:

“Turning to what Clause 21.4 *does* say, it is important first to note that Clause 21.4 comes shortly after Clause 21.2, which provides that if the State wants to terminate for causes of *caducidad*, it must first follow an administrative procedure concluding with a decision by the Minister of Energy declaring the

termination. This right of Ecuador to terminate the contract after submitting to an administrative procedure is a reflection of the State's *poderes exorbitantes*, 'exorbitant powers,' in administrative law. HPL ER III ¶ 44.

Clause 21.4 complements Clause 21.2 by providing that if either party wants to terminate for causes *other than those of caducidad* and the parties cannot reach an agreement, the terminating party must first seek authorization to do so from the Clause 20.3 arbitrator. See HPL ER III ¶¶ 44, 45. Pursuant to Clause 21.1, such other causes include, for instance, a claim by the contractor of a situation of force majeure lasting for more than 12 months without interruption.

Clauses 21.2 and 21.4 thus mirror each other, each setting forth the relevant procedures to be followed by the parties *before* they can terminate for causes of *caducidad*, on the one hand, and other causes, on the other hand. Clause 21.4 requires the parties to seek authorization from the arbitrator if they want to terminate for causes other than those of *caducidad* and cannot reach agreement. Clause 21.2 requires the State to commence an administrative procedure concluding with a positive decision by the Minister of Energy if it wants to terminate for causes of *caducidad*, as in fact occurred here. See HPL ER III ¶¶ 44-46.

Therefore, when Clause 21.2 provides that if the parties cannot reach agreement, either one of them may *request* termination for causes other than those that result in *caducidad* following the arbitration procedures of Section 20, it simply provides the procedure a party must follow *before* it can lawfully terminate. However, Clause 21.4 does not say anything about the procedures to be used for the resolution of disputes arising out of a *declaration of caducidad*, *after* the Clause 21.2.2 procedure has come to an end and the declaration has been issued. See HPL ER III ¶¶ 46, 48-50, 53(1).

[...]

Each of these provisions confirms with different terms that Clause 21.4 simply states the parties' obligation to seek arbitral authorization before they can proceed lawfully with unilateral termination for causes other than those of *caducidad*; and that Clause 21.4 does not exclude disputes arising out of *caducidad* declarations from arbitration or refer such disputes to the Ecuadorian administrative courts. This is consistent with Ecuadorian law, which recognizes the arbitrability of administrative acts, including *caducidad* declarations. CA-409, *Arbitral Award No. 003-07/004-07*, at 46-47 (asserting jurisdiction to decide whether the administrative acts of *caducidad* issued by the Ecuadorian Tribunal Supremo Electoral was consistent with Ecuadorian laws and procedures and whether there was a cause for *caducidad*); CA-364, *Repsol* ¶ 43 (dismissing Respondent's claim that the Tribunal lacked jurisdiction over an administrative act with *res judicata* effect if Article 25 of the ICSID Convention conditions were otherwise met). HPL ER III ¶¶ 32-38, 53 (e)(f)(g)." (emphasis in original)

50. The Claimants add that even if the Tribunal were to accept the Respondent's interpretation of Clause 21.4, OPC's Treaty claims would nonetheless survive because OPC is not a signatory to the Participation Contract. Likewise, the Claimants contend that the Respondent's interpretation of Clause 21.4 is irrelevant for purposes of OEPC's Treaty claims because the Participation Contract does not contain a waiver to that effect.

51. Similarly, regarding OEPC's contract claims, the Claimants consider the Respondent's interpretation of Clause 21.4 to be of no consequence to the Tribunal's jurisdiction given the terms of Articles VI.2 and VI.3 of the Treaty. They submit:

“The terms of Article VI.2 merit the full quotation that Ecuador omitted from its papers:

If the dispute cannot be settled amicably, the national or company concerned may *choose* to submit the dispute, under one of the following *alternatives*, for resolution:

(a) to the courts or administrative tribunals of the Party that is a party to the dispute; *or*

(b) in accordance with any applicable, previously agreed dispute-settlement procedures; *or*

(c) in accordance with the terms of paragraph 3. (emphasis added)

Article VI.3 of the Treaty goes on to confirm that the investor can ‘*choose* to consent in writing to the submission of the dispute for settlement by binding arbitration . . . to the International Centre for the Settlement of Investment Disputes . . .’ (emphasis added)

To exercise that right, the Treaty requires that the investor has not ‘submitted the dispute for resolution under paragraph 2 (a) or (b)’ (i.e., ‘to the courts or administrative tribunals of the Party that is a party to the dispute’ or ‘in accordance with any applicable, previously agreed dispute-settlement procedures’). As long as the investor does not submit the dispute to either of those alternative forums, it has the Treaty right to submit it to an ICSID tribunal *instead of* those alternative forums, including a contractually chosen forum.” (emphasis in original)

52. The Claimants accordingly summarize their position on jurisdiction as being essentially based on a Treaty right to choose ICSID arbitration over the Ecuadorian administrative courts, namely the *Tribunal de lo Contencioso-Administrativo* or “TCA”, and draw the following conclusion:

**“In conclusion**, it follows from the plain language of Article VI.2 and its object and purpose that Claimants had the right under that provision to submit the dispute to either ICSID or UNCITRAL arbitration instead of the TCA, whether the TCA would otherwise have jurisdiction by law or contract. Either the contract does not provide for ICSID arbitration regarding *caducidad*-related disputes, and then the TCA is a domestic ‘court or administrative tribunal’ within the meaning of Article VI.2(a); or the contract provides for the jurisdiction of the TCA over such disputes, and then the TCA may be a ‘previously agreed dispute resolution procedure’ within the meaning of Article VI.2(b). Either way, Claimants were entitled to choose this Tribunal over the TCA pursuant to Article VI.2(c).” (emphasis in original)

53. The Claimants further reassert that notwithstanding Article VI.2 of the Treaty, both Claimants are entitled to submit their Treaty claims to ICSID arbitration. More particularly, they articulate their position regarding OEPC as follows:

**“First**, the plain language of clause 20.3 refers to ‘controversies or differences that are related to or arise from the performance of this Participation Contract.’ It does not say ‘controversies or disputes that are related to or arise from alleged breaches of the Treaty.’ Had the parties wanted to extend the scope of this arbitration clause to cover Treaty claims, they would have said so. In addition, as shown above, if Ecuador accepts that the forum selection clause in the *SGS Philippines* contract did not extend to treaty claims, it is estopped from arguing that Clause 20.3, which is not worded any more broadly than the SGS clause, does extend to treaty claims.

**Second**, had the parties intended to cover Treaty claims in clause 20.3, they would not have included clause 20.4 (stating that ‘[a]dditionally, and without prejudice to the provisions in Clause 20.2 and 20.3 of this Participation Contract, the parties agree to submit any difference relating to investments to Treaties, Conventions, Protocols and other acts under international law’) in the Participation Contract. Ecuador’s reading of Clause 20.3 renders Clause 20.4 entirely superfluous.

**Third**, tribunals have systematically rejected the argument that similarly worded forum selection clauses in investment agreements could affect a treaty tribunal’s



jurisdiction over treaty claims. In *SGS (Pakistan)*, for instance, the tribunal interpreted the scope of an arbitration clause referring ‘[a]ny dispute, controversy or claim arising out of, or related to this Agreement or breach, termination or invalidity thereof’ to a local arbitrator. The tribunal explained that:

Pakistan has argued before us that the arbitrator seized of claims grounded on violation of the PSI Agreement would have jurisdiction not only over such contract claims but also over the BIT claims. We are not persuaded that SGS’s BIT claims against Pakistan are subject to the jurisdiction of the Islamabad arbitrator if only because such claims are based not on the PSI Agreement, but rather allege a cause of action under the BIT. RLA-8, *SGS (Pakistan)* ¶ 154.

*See also* CA-9, *Eureko* ¶¶ 92, 114 (relying on *Vivendi (Annulment)* to dismiss respondent’s objection that a contractual provision referring to the local courts any ‘conflicts between Parties arising from the Agreement’ affected the tribunal’s jurisdiction over claimant’s treaty claims); CA-355, *Azurix (Jurisdiction)* ¶¶ 26, 76 (holding that a contractual provision referring ‘all disputes that may arise out of the Bidding’ to the local courts did not preclude the tribunal’s jurisdiction over claimant’s treaty claims, ‘[e]ven if the dispute as presented by the Claimant may involve the interpretation or analysis of facts related to performance under the Concession Agreement.’) (emphasis in original)

54. As for OPC, the Claimants refute the Respondent’s allegation of lack of standing and conclude that OPC is exercising its Treaty rights in good faith and in fulfillment of its duties towards its shareholders.

55. Finally, the Claimants emphasize that, in any event, Ecuadorian law itself does not preclude arbitration of disputes relating to *caducidad*. They contend that a *caducidad* declaration is plainly discretionary and that neither the legal relationship between the parties nor the *caducidad* declaration are extra-contractual in nature. According to the Claimants, *caducidad*-related disputes are thus fully arbitrable.

**1. The Respondent's Second Objection: The Claimants Have Allegedly Failed to Comply With the Six-Month Waiting Period Under the BIT**

**A. The Respondent's Position**

56. The Respondent's second jurisdictional objection is based on Article VI.3 of the Treaty which establishes a six-month waiting period for submission of a dispute to arbitration.<sup>7</sup>

57. The Respondent contends that by filing their Request for Arbitration two days after the *Caducidad* Decree, the Claimants acted in procedural and substantive bad faith:

“Ecuador’s second objection to jurisdiction is that the Claimants failed to comply with the six-month waiting period set forth in Article VI.3 of the BIT. In a flagrant disregard for the provisions of the BIT, the Claimants made no effort whatsoever to adhere to the prescribed ‘cooling off’ period to negotiate a solution to this dispute – precisely for which the waiting period was designed. Instead, they filed their Request for Arbitration a mere *two days* after Ecuador issued the *Caducidad* Decree and the *same day* the government assumed control of operations in Block 15.

The Claimants’ disregard for the provisions of the BIT is procedural and substantive bad faith. Indeed, the Claimants elected to initiate this arbitration and pursue provisional relief rather than do what they had specifically agreed to do in the Participation Contract – namely, to *not* arbitrate declarations of *caducidad* but, rather, to follow the dictate of Ecuadorian law should they chose to challenge the declaration of *caducidad*.” (emphasis in original)

58. The Respondent also argues that such a mandatory waiting period is a true jurisdictional requirement.

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<sup>7</sup> See *supra* at paragraph 34.

59. Finally, the Respondent contends that the Claimants' claims are premature because they made no attempt to challenge the *Caducidad* Decree before the Ecuadorian administrative courts.

## **B. The Claimants' Position**

60. As noted earlier, the Claimants maintain that the Respondent's second jurisdictional objection, based on the Treaty, is incompatible with its first one, based on the Participation Contract. They add that the dispute in fact arose as early as September 2004 (over eighteen months prior to the *Caducidad* Decree) and that in any event, an investor is not required to respect a waiting period if attempts at a negotiated solution have proven futile.

61. The Claimants also dispute the Respondent's suggestion that the waiting period at issue is a jurisdictional requirement, as opposed to a procedural one. As for the Respondent's allegation that their claims are premature, the Claimants argue that this is not the case because, *inter alia*, they were required to make an irrevocable choice between the TCA and this Tribunal and that this issue, in any event, goes to the merits of the case, not to the issue of this Tribunal's jurisdiction.

## **V. THE TRIBUNAL'S ANALYSIS**

### ***1. The Respondent's First Jurisdictional Objection***

62. As gleaned from the overview of their respective arguments regarding the issue of jurisdiction, the parties fundamentally disagree on the interpretation of Clause 21.4 of the Participation Contract, in particular as to whether this provision operates to exclude the

Claimants' claims from the Tribunal's remit. The Tribunal must accordingly decide whether Clause 21.4 carves out an exception to the availability of ICSID arbitration in the context of a dispute resulting from a declaration of *caducidad* of the Participation Contract by the Respondent.

63. Before turning to its analysis of Clause 21.4 of the Participation Contract, the Tribunal observes that the parties also fundamentally disagree on the issue of whether Clause 22.2.1 of the Participation Contract, which is part of Section 22 entitled "Applicable Law, Domicile, Jurisdiction and Procedure", operates as a waiver to the adjudication of claims under ICSID. The language of this provision is highlighted again below for ease of reference:

**"TWENTY TWO: APPLICABLE LAW, DOMICILE, JURISDICTION AND PROCEDURE**

[...]

**22.2 Domicile, Jurisdiction and Competence.-** The Parties submit to Ecuadorian laws, and controversies shall be substantiated by the provisions of clauses 22.1.2 and 22.1.3 of this Participation Contract. This provision shall prevail even after the termination of this Participation Contract, up to the time when the operating permit of Contractor in Ecuador is legally canceled [*sic*], regardless of the causes for termination.

**22.2.1** In the event of controversies that may arise as a result of the performance of this Participation Contract, in accordance with Ecuadorian law, Contractor expressly waives its right to use diplomatic or consular channels, or to have recourse to any national or foreign jurisdictional body not provided for in this Participation Contract, or to arbitration not recognized by Ecuadorian law or provided for in this Participation Contract. Lack of compliance with this provision shall constitute grounds for the forfeiture of this Participation Contract.

**22.2.2** The parties agree to use the means set forth in this Participation Contract to settle questions or controversies that may arise during the term hereof, as well as to observe and comply with decisions issued by experts, arbiters, judges or competent tribunals in all applicable cases, according to the provisions of this Participation Contract.

[...]"

64. The Tribunal notes that whilst the Clause 22.2.1 waiver argument was not central to the Respondent's written submissions on jurisdiction, it was argued extensively by the Respondent at the Hearing. Indeed, it was the main focus of the Respondent's Opening Statement. For this reason, the Tribunal addresses the Respondent's waiver argument first.

65. At the Hearing, the Respondent submitted that Clause 22.2.1 of the Participation Contract is an "unequivocal waiver of arbitrability". The Respondent argued that "this is an agreement to waive some of the options in the BIT, but not all of them. So, you don't have a renunciation of the BIT, you have a narrowing of options". These options under the BIT, the Tribunal recalls, are set forth at Article VI thereof, which provides *inter alia* as follows:

"ARTICLE VI

[...]

2. In the event of an investment dispute, the parties to the dispute should initially seek a resolution through consultation and negotiation. If the dispute cannot be settled amicably, the national or company concerned may choose to submit the dispute, under one of the following alternatives, for resolution;

(a) to the courts or administrative tribunals of the Party that is a party to the dispute; or

(b) in accordance with any applicable, previously agreed dispute-settlement procedures; or

(c) in accordance with the terms of paragraph 3.

3. (a) Provided that the national or company concerned has not submitted the dispute for resolution under paragraph 2 (a) or (b) and that six months have elapsed from the date on which the dispute arose, the national or company concerned may choose to consent in writing to the submission of the dispute for settlement by binding arbitration:

(i) to the International Centre for the Settlement of Investment Disputes ('Centre') established by the Convention on the Settlement of Investment Disputes between States and Nationals of other States, done at Washington, March 18, 1965 ('ICSID Convention'), provided that Party is a party to such convention;

[...]

[...]"

66. In essence, the Respondent argues that Clause 22.2.1 of the Participation Contract narrows the scope of the availability of ICSID arbitration under the BIT by creating a waiver applicable to any arbitration not recognized by Ecuadorian law. Arbitration of *caducidad* disputes, the Respondent contends, is "arbitration not recognized by Ecuadorian law".

67. In response to a question from the Chairman in this regard during the Hearing, counsel for the Respondent answered that:

"the BIT came first, and the contract came second, and I think that, you know, to the extent it is a factor, it is a situation where the parties knew there were the three options, and in the contract, they agreed to exercise just one of them. I think that is a perfectly rational, commercial, governmental decision [...]."

68. In other words, the Respondent maintains that the parties agreed that in the event of a *caducidad*-related dispute under the Participation Contract, the Ecuadorian administrative courts would have exclusive jurisdiction. This line of argument led to further questions from the Tribunal regarding Clause 22.2.1, and ultimately to the following exchange between Mr. Williams and Mr. von Mehren:

"ARBITRATOR WILLIAMS: If you have a decision where the parties are negotiating against the backdrop of this Treaty, why would it be a commercial and rational and sensible outcome for the Claimant to write in such a clause of

this -- as this -- which would compel them to go to the State courts for an argument about the forfeiture decree?

MR. VON MEHREN: Why would that be reasonable?

ARBITRATOR WILLIAMS: Yes. Why would they want to do that? You suggested that this would be a sensible, commercial and rational outcome.

MR. VON MEHREN: You know, my experience in negotiating arbitration provisions is that you don't always end up with what you would prefer to have in the best possible world, and what happens is you think about the commercial benefits that you hope to gain from the transaction, the business guys are there, and they are saying, 'You know, we are going to do this, we are going to make a lot of money', and, 'Let's pursue that', and you weigh those off against what is going to happen if there is a dispute, and where you are going to take that dispute and how that might affect your ability to win if you deserve to do so.

I think a very rationale [*sic*] decision -- I have seen it many times in my career -- is to accept perhaps not your perfect, your greatest desire as to how the dispute is resolved, in order to go forward with an economic transaction, and I would say, as the Attorney General did, that the courts of Ecuador are independent, the courts of Ecuador are fully equipped to handle this issue, the administrative courts, and there is absolutely no evidence before this Tribunal that they wouldn't do that in an entirely proper way.

So, I think it is reasonable in the context of the entire transaction and negotiations for Occi [*sic*] to have agreed to this, and once they do, once they do, I think it is reasonable to say, 'We have an agreement and it should be followed'. More than, 'Should be followed', I think it is necessary in any system of jurisprudence, whether that be a national system, or this international system; extremely important that agreements be followed rather than not."

69. The Claimants strenuously reject this argument which, they note, surfaced very late in the Respondent's jurisdictional challenge. At the Hearing, they argued:

"[E]ven the waiver argument rests not only on a misreading of those words, and I will get to that, but it rests on their use of 21.4, and as we pointed out in our answer, it was a little bit like one of these glossy brochures, they kept telling you that 21.4 was a clear carve-out, clear exception and so forth, they told you that for about what [*sic*] half a dozen pages, they repeated that several times before they actually showed you the text, and that is not surprising because if it was such a clear carve-out you would expect it to say something like, 'Notwithstanding the provisions of Clause 20 in the event of a forfeiture by Caducidad the contractors' only recourse shall be to the Ecuadorian courts or to the TCA [*Tribunal de lo Contencioso-Administrativo*]'". That would be a clear carve-out, instead of, as the President pointed out in his question to Mr. Von Mehren just now, it is in the forfeiture sections, and it is simply providing that if

a party wants to request forfeiture, one of the grounds in the contract, then it is to do so through the arbitration process and Article 20, except for declaring forfeiture by Caducidad which has its own provision immediately before that in 21.2. That is what the contract says. That disposes of their arguments.”

70. The Tribunal agrees with the Claimants regarding the interpretation of Clause 22.2.1 of the Participation Contract. The Tribunal does not accept that, by virtue of this provision, the parties agreed that *caducidad*-related disputes under the Participation Contract would solely be resolved by submission to the Ecuadorian administrative courts, *i.e.* the TCA. This is simply not what the clause says.

71. Based on elementary principles of contract interpretation, any exception to the availability of ICSID arbitration for the resolution of disputes arising under the Participation Contract, in this case *caducidad*-related disputes, requires clear language to this effect. The requirement of clear and unequivocal language in such circumstances was confirmed by the ICSID tribunal in the case of *Aguas del Tunari v. The Republic of Bolivia*<sup>8</sup> which recalled a tribunal’s duty to the parties in this regard (at paragraph 119):

“[I]t is the Tribunal’s view that an ICSID tribunal has a duty to exercise its jurisdiction in such instances absent any indication that the parties specifically intended that the conflicting clause act as a waiver or modification of an otherwise existing grant of jurisdiction to ICSID. A separate conflicting document should be held to affect the jurisdiction of an ICSID tribunal only if it clearly is intended to modify the jurisdiction otherwise granted to ICSID. As stated above, an explicit waiver by an investor of its rights to invoke the jurisdiction of ICSID pursuant to a BIT could affect the jurisdiction of an ICSID tribunal. However, the Tribunal will not imply a waiver or modification of ICSID jurisdiction without specific indications of the common intention of the Parties.” (emphasis added)

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<sup>8</sup> ICSID Case No. ARB/02/3, Decision on Respondent’s Objections to Jurisdiction, dated 21 October 2005.



72. The tribunal in that case further cautioned (at paragraph 122): “The Tribunal will not read an ambiguous clause as an implicit waiver of ICSID jurisdiction; silence as to the question is not sufficient.” That caution is apposite in the present case and this Tribunal adopts it.

73. Clause 22.2.1 cannot, on its terms, be construed as an exception or waiver to ICSID jurisdiction over *caducidad*-related disputes. The Participation Contract is fraught with express and extensive references to *caducidad* under the very preceding section to the one in which Clause 22.2.1 is found. The parties fully understood the significance of *caducidad* in terms of the Participation Contract’s potential forfeiture and resulting disputes. Had the parties wished to exclude such disputes from ICSID jurisdiction and confer exclusive jurisdiction to the Ecuadorian administrative courts in this regard, they could have done so. They did not and the Tribunal will not imply such wording in the clause.

74. By virtue of the Treaty, the Respondent expressly consented to the submission of investment disputes for settlement by binding ICSID arbitration under the Washington Convention. The Respondent acknowledged at the Hearing that this Treaty, upon ratification, became part of Ecuadorian law. Therefore, whilst Clause 22.2.1 refers to “arbitration not recognized by Ecuadorian law”, nothing in the Participation Contract supports or even suggests that this language, when read in context, reveals a common intention to waive ICSID jurisdiction over *caducidad*-related disputes, and the Tribunal so finds.

75. The Tribunal now comes to the provision which, at least initially, was central to the Respondent's jurisdictional challenge, *i.e.* Clause 21.4. This provision, as indicated previously, is part of a Section of the Participation Contract entitled "Termination and *Caducidad* of this Participation Contract". Clause 21.4 is in fact the penultimate provision of this Section which is reproduced *in extenso* for purposes of fully appreciating the contractual context at issue:

**"TWENTY ONE: TERMINATION AND CADUCIDAD OF THIS PARTICIPATION CONTRACT.-**

**21.1 Termination:** This Contract shall terminate:

**21.1.1** By a declaration of *caducidad* issued by the Corresponding Ministry for the causes and following the procedure established in Articles seventy four (74), seventy five (75) and seventy six (76) of the Hydrocarbons Law, insofar as applicable.

**21.1.2** Due to a transfer of rights and obligations of the Participation Contract without prior authorization from the Corresponding Ministry.

**21.1.3** By executed judicial sentence of Contractor's bankruptcy.

**21.1.4** By modification of the legal status of Contractor without a prior authorization from the Corresponding Ministry.

**21.1.5** By extinction of the legal status of Contractor.

**21.1.6** By mutual agreement between the Parties.

**21.1.7** By executed judicial judgment that declares the termination of this Participation Contract.

**21.1.8** At any time during the existence of this Contract, at Contractor's opinion, and once it has complied with its contractual and legal obligations enforceable to date, with prior authorization from the Corresponding Ministry.

**21.1.9** Because the term of this Participation Contract has lapsed.

**21.1.10** At the sole discretion of Contractor and without any right to be indemnified by the other Party, when Force Majeure or Acts of God last for a period of more than twelve continuous or discontinuous months within a period of twenty four months.

**21.2 *Caducidad.***- In cases of default that may constitute a cause for *caducidad*, in accordance with the provisions of the Hydrocarbons Law, the procedure described below shall be followed:

**21.2.1** The legal representative of PETROECUADOR shall serve notice with claim of non-compliance to Contractor, to be answered within ten (10) days, rejecting or accepting said claim and in this latter case, offering to remedy the situation within a period of thirty days from the date of receiving notice of same. Within this period Contractor shall take all necessary measures, according to circumstances, to remedy, correct or rectify the failure or non-compliance that brought about that claim.

**21.2.2** If within the terms determined in the clause 21.2.1 above, Contractor does not solve such failures or noncompliance or does not justify such failures or non-compliance to PETROECUADOR's satisfaction, the legal representative of PETROECUADOR shall request from the Corresponding Minister of a declaration of *caducidad* for this Participation Contract.

**21.2.3** Prior to said declaration of *caducidad*, the Corresponding Minister shall serve notice to Contractor so that, in a period of no less than thirty days and no more than sixty days from the date of the notice, Contractor shall comply with all obligations that have not been performed, or clears the claims formulated. If, having taken such actions, the term is insufficient for the Contractor to remedy, correct or rectify such failure or lack of compliance, and Contractor is able to prove this, then upon Contractor's request, the Corresponding Ministry can provide an additional term to that granted.

**21.2.4** Once *caducidad* has been declared, the provisions of Art. 75 of the Hydrocarbons Law shall be applied, and Contractor shall transfer to PETROECUADOR the originals of all antecedents and all geological, geophysical, drilling or any other type of records, relative to the Area, unless evidence is provided that such documents have already been delivered.

**21.3** For the purposes of *caducidad* and penalties, the provisions of Chapter IX of the Hydrocarbons Law shall be applicable.

**21.4** Termination of this Participation Contract for any reason other than those that result in *caducidad* may be requested by either of the Parties, subject to the procedures stipulated in Clause Twenty in the event that they fail to reach an agreement.

**21.5** Breaches of this Contract or violations of the Hydrocarbons Law or its regulations that do not result in *caducidad* shall be punished in accordance with the Law and its Regulations." (emphasis added)

76. Resorting to arguments not dissimilar to its Clause 22.2.1 waiver argument, the Respondent contends that Clause 21.4 operates to carve-out *caducidad* disputes from

being resolved by way of arbitration in general and by ICSID arbitration in particular. In the words of counsel for the Respondent, “21.4 and 22.2.1 are specific provisions that appl[y] to specific situations, and therefore they are the exceptions to the general rules in Clause 20”. For reasons not dissimilar to those which led the Tribunal to reject the Respondent’s Clause 22.2.1 waiver argument, the Tribunal finds that the Respondent’s Clause 21.4 carve-out argument fails as well.

77. To state the obvious, Section 21 addresses termination and *caducidad* of the Participation Contract. Clause 21.4 in particular provides that either party may request termination of the Participation Contract for any reason other than those that result in *caducidad* and also addresses the manner in which this is to be done (“... subject to the procedures stipulated in Clause Twenty ...”). There is simply no indication in this clearly-worded clause of a common intention of the parties to carve-out *caducidad* disputes from being resolved by way of arbitration in general or ICSID arbitration in particular.

78. Plainly, Section 21 as a whole, including *a fortiori* Clause 21.4, is not about the resolution of disputes arising under the Participation Contract, be they *caducidad*-related or not. Rather, it deals with the causes and the manner in which the Participation Contract may come to an end, including by a declaration of *caducidad*. More particularly, it provides that the Participation Contract can be lawfully terminated for the reasons listed in Clause 21.1. In the event of termination resulting from *caducidad*, the Respondent is required to follow the procedure set forth in Clause 21.2. And prior to termination resulting from causes other than *caducidad*, the parties are to seek an agreement to terminate, failing which the procedures set out in Section 20 are to be

followed. The Tribunal agrees with the Claimants that Section 21 is a “very logical” section. It consists of no more (and no less) than procedures to be followed in order to proceed to the lawful termination of the Participation Contract.

79. The Tribunal thus finds that Clause 21.4 does not consist of a carve-out of *caducidad* disputes from ICSID jurisdiction. The Tribunal observes that certain jurisdictional carve-outs are found elsewhere in the Participation Contract, such as under Clause 22.1.2, which is reproduced again as follows:

**“22.1.2.** In any claims resulting from actions or resolutions of the National Direction for Hydrocarbons, the Corresponding Minister shall be the highest administrative instance. However, Contractor shall have the right to go directly before the District Tribunal No. 1 of Administrative Law, the competent legal body to hear direct claims or to resolve appeals against the decisions of the Corresponding Ministry. In claims arising from acts or resolutions issued by the General Direction of the Internal Revenue Service, said organization shall be the higher administrative instance. After this, Contractor have the right to appeal before the Fiscal District Tribunal No. 1, the competent jurisdictional body for hearing review direct claims or resolving appeals regarding decisions made by the Minister of Finance.” (emphasis added)

80. Clause 20.2.1 is yet another example of clear and unequivocal waiver language in the Participation Contract:

**“20.2.1.** Controversies that may arise from the interpretation, application and performance of this Participation Contract shall be submitted to arbitration under the law, administered by the Arbitration Centre of the Chamber of Commerce of Quito, or an international Arbitration Centre that shall be regulated by Treaties, Conventions, protocols and other actions of international Law signed and ratified by Ecuador, in accordance with the Law.

In the event of disputes between the Parties involving interpretation, application and performance in the execution of this Participation Contract, PETROECUADOR expressly waives the right to ordinary jurisdiction.” (emphasis added)

81. Had it been the parties' intention to exclude *caducidad* disputes from ICSID arbitration in favour of the exclusive jurisdiction of the Ecuadorian administrative courts, they could have very easily done so with language akin to that found in the above-quoted provisions.

82. Finally, the Tribunal also recalls that in alleging that Clause 21.4 excludes *caducidad* from submission to arbitration, the Respondent has maintained that this is the inevitable consequence of the Ecuadorian law principle according to which *caducidad* decrees such as the one at issue in this arbitration carry a presumption of legality and may only be challenged before the Ecuadorian administrative courts. More particularly, the Respondent refers to Article 4 of the Ecuadorian law on Mediation and Arbitration as establishing the non-arbitrability of *caducidad*-related disputes. The Respondent's position in this regard was confirmed at the Hearing in response to questions from the Tribunal:

“ARBITRATOR STERN: If I summarise what you have just said, your position, and what you have said, is that under Ecuadorian law, in your view, an administrative act is not arbitrable?”

MR. SILVA: I confirm that especially in relation to Caducidad. That would be my answer.”

83. In its closing argument, counsel for the Respondent added the following:

“It is my submission, distinguished members of the Tribunal, that it goes to the fundamental organization of the Ecuadorian State, it goes to the policies that the Ecuadorian State has adopted in relation to how the different branches of power should be organized. It goes to that very fundamental premise to say that Ecuador has decided to entrust questions in relation to administrative acts to its courts. This is important for Ecuador, because Ecuador, as I said, could eventually ask cassation against those administrative acts. Ecuador couldn't do it in arbitration.”

84. The Tribunal notes that, as part of its closing argument at the Hearing, counsel for the Respondent admitted that Clause 21.4 does not address the resolution of *caducidad*-related disputes *per se*. According to the Respondent, this is a “purposeful” omission:

“Clause 21 deals with termination in general, and it states that with respect to a non-Caducidad termination, arbitration is available. It does not, however, speak to a Caducidad determination, and we believe that the omission is purposeful, and that it reflects the point of Ecuadorian law, that one cannot have arbitration with respect to Caducidad. In the entire section dealing with termination, the only right to arbitration that is recognized is the one with respect to a non-Caducidad situation. If this is not an exclusion then we point out that that reference is, in fact, redundant, because it is entirely unnecessary. Clause 20 would certainly deal with arbitration in the non-Caducidad situation.” (emphasis added)

85. The Tribunal does not accept the Respondent’s argument. The words of the tribunal in *Aguas del Tunari v. The Republic of Bolivia* (at paragraph 122) will be recalled again: “The Tribunal will not read an ambiguous clause as an implicit waiver of ICSID jurisdiction; silence as to the question is not sufficient.” The exception urged by the Respondent simply cannot operate by way of omission, purposeful or not.

86. More fundamentally, the Respondent cannot invoke its domestic law for the purpose of avoiding ICSID jurisdiction under the Treaty. As noted earlier, by virtue of the Treaty, the Respondent expressly consented to the submission of disputes for settlement by binding arbitration under the Washington Convention, thereby establishing the basis for this Tribunal’s jurisdiction in the present circumstances. The Respondent’s Constitution, at Article 163, recognizes that international treaties duly ratified by the Republic of Ecuador shall prevail over any laws in Ecuador. This was confirmed at the

Hearing by the Respondent's own legal expert on Ecuadorian law when he answered questions posed to him by counsel for the Claimants:

“Q. You agree with me that pursuant to Article 163 of the constitution, in case of conflict between those duly-ratified international Treaties, on the one hand, and the arbitration law on the other hand, the provisions of the duly-ratified international Treaties shall prevail; correct?”

A. Yes. That is so.

[...]

Q. Fair enough. A very simple assumption; if there was a duly-ratified Treaty that affirmatively granted jurisdiction to an Arbitral Tribunal, and the Ecuadorian arbitration law did not grant such jurisdiction because of a failure to meet certain requirements in that law, the Tribunal would still have jurisdiction pursuant to that Treaty; correct?

A. In such a situation, if Ecuadorian law, as you referred to, is a law or a lower level regulation, that would be the case.”

87. This is in fact a fulsome answer to the Respondent's allegation regarding non-arbitrability of *caducidad*-related disputes. Indeed, the Respondent acknowledged at the Hearing that it cannot invoke its domestic law for the purpose of avoiding ICSID jurisdiction under the Treaty. In its closing argument, counsel for the Respondent also argued that the “exclusive jurisdiction principle” according to which *caducidad* decrees may only be challenged before the Ecuadorian administrative courts is enshrined in the Ecuadorian Constitution, and that the Constitution prevails over the Treaty:

“[W]e certainly agree that where the Claimant has not executed a waiver of any sort, the state cannot use its own law to try to circumvent, or impede, the International Tribunal. We believe this case is a very different type of case because there was an explicit waiver, and that explicit waiver was that in the circumstances governed under this contract, the contractor, the investor, agreed that it could only have access to an International Tribunal under the BIT as long as that arbitration was recognized by Ecuadorian law, and one would imagine that in many, indeed most instances, there would be no conflict, since the Treaty is part of Ecuadorian law. The only instance is [sic] where it is a problem is



where the constitution itself conflicts with the Treaty, and in that instance, the constitution has to take priority.” (emphasis added)

88. The premise to this line of argument is based on a finding that the Participation Contract, be it Clause 22.2.1 or Clause 21.4, contains a clear and unequivocal waiver to ICSID jurisdiction. The Tribunal has found earlier in this Decision that no such waiver has been made under the Participation Contract. For all of these reasons, the Respondent’s first jurisdictional objection is accordingly denied.

89. It follows that the Tribunal has jurisdiction over the Claimants’ claims under both the Participation Contract and the Treaty. For this reason, the Respondent’s submission that Claimant OPC, the “ultimate parent” of OEPC, lacks standing to assert claims as an investor in the circumstances because it is not a signatory to the Participation Contract is moot and need not be addressed as part of this Decision on Jurisdiction.

## ***2. The Respondent’s Second Jurisdictional Objection***

90. The Tribunal will now consider the Respondent’s second jurisdictional objection, *i.e.* that the Claimants failed to respect the six-month waiting period for submission of the dispute to arbitration. This waiting period is imposed by Article VI.3 of the Treaty, which states:

“Provided that the national or company concerned has not submitted the dispute for resolution under paragraph 2 (a) or (b) and that six months have elapsed from the date on which the dispute arose, the national or company concerned may choose to consent in writing to the submission of the dispute for settlement by binding arbitration.”

91. The Tribunal notes the Respondent's acknowledgment at the Hearing that "this is not an objection to jurisdiction that has fared extremely well in many cases. We all know that, but here we have the extreme." This "extreme" was summarized by counsel for the Respondent as follows:

"I would submit to you that they did not initiate this arbitration two days later because they had said, "Oh, this cannot be resolved in any way, shape or form with Ecuador", they did it for strategic purposes, they did it so they could get to a motion for provisional relief, they did it because they thought that that was the way to force themselves back into Block 15. That is what was going on, not any fair and legitimate decision that trying to discuss this and resolve this for six months was futile."

92. In response, the Claimants have emphasized that the very purpose of the waiting period requirement is to allow parties to enter into good faith negotiations before initiating arbitration. This requirement need not be respected if attempts at a negotiated solution have proven futile, which the Claimants contend was the case in the present circumstances.

93. In this regard, the Tribunal recalls that the *caducidad* procedure at issue in this arbitration was in fact initiated in 2004. As noted earlier, for some 18 months or so prior to the issuance of the actual *Caducidad* Decree on 15 May 2006, OEPC made a number of submissions seeking to rebut the allegations on the basis of which the *caducidad* procedure was initiated, but to no avail.<sup>9</sup>

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<sup>9</sup> See *supra* at paragraph 19.

94. Furthermore, the Tribunal accepts, albeit without prejudging the merits, that attempts at reaching a negotiated solution were indeed futile in the circumstances.<sup>10</sup>

95. The Respondent's second jurisdictional objection is accordingly denied.

96. Finally, it is recalled that the Respondent has requested, as part of its second jurisdictional objection, "an order that this arbitration be stayed until OEPC challenges the *Caducidad* Decree in the competent Ecuadorian administrative court and that court issues a final ruling on such challenge". This request is made on the basis of the allegation that the Claimants' claims are premature because the Claimants have made no attempt to challenge the *Caducidad* Decree before the Ecuadorian administrative courts. For the reasons set forth in this Decision on Jurisdiction, the Claimants were not required to do so, and this request is accordingly denied.

## **VI. DECISION**

97. For the foregoing reasons, the Tribunal decides and declares as follows:

- (i) the Respondent's first jurisdictional objection is denied;
- (ii) the Respondent's second jurisdictional objection is denied;

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<sup>10</sup> A number of tribunals have confirmed that where negotiations are bound to be futile, there is no need for the waiting period to have fully lapsed: *see e.g. Lauder v. The Czech Republic*, Award dated 3 September 2001 at paragraphs 187-191. *See also Consorzio Groupement L.E.S.I. DIPENTA v. People's Democratic Republic of Algeria*, ICSID Case No. ARB/03708, Award dated 10 January 2005 at paragraph 32(iv); *SGS Société Générale de Surveillance S.A. v. Islamic Republic of Pakistan*, ICSID Case No. ARB/10/13, Decision on Jurisdiction dated 6 August 2003 at paragraph 184; and *Ethyl Corporation v. The Government of Canada*, Award on Jurisdiction dated 24 June 1998 at paragraph 84.

(iii) the Respondent's alternative request for "an order that this arbitration be stayed until OEPC challenges the *Caducidad* Decree in the competent Ecuadorian administrative court and that court issues a final ruling on such challenge" is denied; and

(iv) the Tribunal has jurisdiction over both OEPC's and OPC's claims in this proceeding and the arbitral proceedings will continue to the merits phase in accordance with the calendar established in the Tribunal's Procedural Order N°. 1 as modified by Procedural Order N°. 2.

98. The costs are reserved for consideration at the conclusion of another phase of the arbitration and there shall accordingly be no order as to costs at this time.

*[signed]*

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Professor Brigitte Stern

*[signed]*

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David A.R. Williams, Q.C.

*[signed]*

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L. Yves Fortier, C.C., Q.C.

President