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# Client Alert

International Arbitration Practice Group

November 12, 2015

## Establishing the Application of The Foreign Sovereign Immunities Act's Arbitration Exception

On October 7, 2015, the United States Court of Appeals for the District of Columbia Circuit issued the mandate on its opinion affirming the judgment of the United States District Court for the District of Columbia confirming Chevron's $96 million arbitral award against Ecuador. In so doing, the Court held that, under the Foreign Sovereign Immunities Act (FSIA), it is sufficient for the plaintiff to show that there is an arbitration agreement and an arbitral award to invoke the arbitration exception to sovereign immunity. This decision also brings the D.C. Circuit in line with the growing consensus of federal circuits that afford substantial deference to an arbitral tribunal's jurisdictional determinations where a state has agreed in a treaty to arbitrate disputes under arbitral rules empowering a tribunal with "competence-competence," or the competence to decide its own jurisdiction.

The D.C. Circuit issued its opinion on August 4, 2015. On September 3, 2015, Ecuador filed petitions for panel and *en banc* rehearing of the case. The D.C. Circuit denied the petitions on September 28, 2015, and issued its mandate on October 7, 2015, finally terminating the appellate court's jurisdiction over the matter.

### The Dispute

In 2006, Chevron and TexPet (Chevron) filed an arbitration against the Republic of Ecuador alleging that the failure of the Ecuadorian courts to adjudicate seven breach-of-contract claims brought by Chevron in Ecuador amounted to a breach of the U.S.-Ecuador Bilateral Investment Treaty (BIT). The BIT provided any investor with a right to arbitrate disputes under the BIT "in accordance with the Arbitration Rules of the United Nations Commission on International Trade Law (UNCITRAL)." The Tribunal ultimately awarded Chevron $96 million along with post-award compound interest. Ecuador unsuccessfully sought to set aside the award at the seat of the arbitration in the Netherlands, while Chevron sought to confirm the award in the U.S. On June 6, 2013, the U.S. District Court for the District of Columbia confirmed the award, entering judgment in favor of Chevron.

Ecuador appealed to the Court of Appeals, arguing that the district court erred in refusing to determine, on a *de novo* basis, whether Ecuador had agreed to arbitrate Chevron's dispute under the BIT, and by affording substantial deference to the Tribunal's determinations on that matter. Specifically,

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Ecuador argued that because Chevron had based its suit upon Section 1605(a)(6) of the FSIA (abrogating a foreign state's presumptive immunity from suits that seek "to confirm an award made pursuant to … an agreement to arbitrate … governed by a treaty or other international agreement in force for the United States calling for the recognition and enforcement of arbitral awards"), the FSIA required the district court to determine, on a *de novo* basis, whether an arbitration agreement existed between Chevron and Ecuador. Ecuador further argued that the award should not have been recognized under, *inter alia*, Article V(1)(c) of the New York Convention, which permits enforcing courts to deny recognition to an arbitral award that "deals with a difference not contemplated by or not falling within the terms of the submission to arbitration."[1]

**The D.C. Circuit's Decision**

The D.C. Circuit rejected Ecuador's argument that the FSIA requires a court to determine questions of arbitrability on a *de novo* basis when jurisdiction is premised upon Section 1605(a)(6). The Court of Appeals first noted that the FSIA requires the plaintiff to satisfy its burden of production that an exception to sovereign immunity exists, but that the foreign state defendant ultimately bears the burden of persuasion that it is entitled to sovereign immunity. The Court then found that Chevron had met its burden of production by producing the U.S.-Ecuador BIT and the arbitration award, the existence of neither of which Ecuador disputed. Rather, Ecuador argued that the scope of its consent to arbitrate under the BIT did not encompass Chevron's breach of contract claims, and that this issue was an issue of arbitrability that should presumptively be decided by the courts, not the arbitrators. The D.C. Circuit disagreed, holding that "Ecuador conflates the jurisdictional standard of the FSIA with the standard for review under the New York Convention." In the Court's view, the FSIA "allows federal courts to exercise jurisdiction over Ecuador in order to consider an action to confirm or enforce the award," and any dispute over whether Chevron's Ecuadorian lawsuits were "investments" for purposes of the treaty was "properly considered as part of review under the New York Convention."

With respect to Ecuador's New York Convention-based arguments, the Court of Appeals first rejected Ecuador's argument that the district court erred in deferring to the Tribunal's determination that Chevron's breach of contract claims constituted "investments" within the scope of the U.S.-Ecuador BIT. The Court affirmed that Ecuador had agreed to delegate such questions to the Tribunal under the BIT, which was "not silent on who decides arbitrability." Specifically, the BIT permitted an investor to bring its claims against Ecuador in arbitration under the UNCITRAL Rules, which provide in Article 21 that "[t]he arbitral tribunal shall have the power to rule on objections that it has no jurisdiction, including any objections with respect to the existence or validity of the arbitration clause," and "shall have the power to determine the existence or the validity of the contract of which an arbitration clause forms a part."

**Judicial Deference to Arbitrators' Determinations Concerning Arbitrability**

The D.C. Circuit's decision contributes to a growing consensus among the federal circuits that the parties' agreement to arbitrate under arbitration rules that empower the arbitrators to determine issues concerning their own jurisdiction constitutes "clear and unmistakable evidence" of the intent to delegate questions of arbitrability to the arbitrators, and to limit judicial review of such matters. The rule, which grew out of the Supreme Court's seminal holding in *First Options v. Kaplan*,[2] first gained traction in the Eighth and Second Circuits, which provided some of the earliest precedent holding that deference would be shown to the arbitrators' determination of issues of arbitrability where the parties agreed to rules of arbitration that grant arbitrators the power to determine their own jurisdiction. *See FSC Securities Corp. v. Freel*, 14 F.3d 1310, 1312–13 (8th Cir. 1994) (NASD Rules); *PaineWebber Inc. v. Bybyk*, 81 F.3d 1193, 1199 (2d Cir. 1996) (same). Although both of these cases involved the NASD Rules, subsequent circuit precedents applied the principle to arbitrations conducted under the AAA Rules. *See Terminix Int'l Co. v. Palmer Ranch L.P.*, 432 F.3d 1327, 1332 (11th Cir. 2005) (AAA Commercial Rules); *Qualcomm Inc. v. Nokia Corp.*, 466 F.3d 1366, 1373 (Fed. Cir. 2006) (AAA Rules); *Fallo v. High-Tech Inst.*, 559 F.3d 874, 878 (8th Cir. 2009) (AAA Rules); *Petrofac, Inc. v. DynMcDermott Petroleum Operations Co.*, 687 F.3d 671, 675 (5th Cir. 2012) (AAA Rules). The Second Circuit

subsequently applied the rule in the context of international arbitration, holding that agreements to arbitrate under the UNCITRAL Rules sufficed as clear and unmistakable evidence of the intent to arbitrate arbitrability issues. *See Schneider v. Kingdom of Thailand*, 688 F.3d 68, 72-73 (2d Cir. 2012) (UNCITRAL Rules); *Rep. of Ecuador v. Chevron Corp.*, 638 F.3d 384, 394 (2d Cir. 2011) (same). The Ninth Circuit joined the Second Circuit in *Oracle Am., Inc. v. Myriad Grp. A.G.*, 724 F.3d 1069, 1076-75 (9th Cir. 2013), finding "no reason to deviate from the prevailing view that incorporation of the UNCITRAL arbitration rules is clear and unmistakable evidence that the parties agreed the arbitrator would decide arbitrability." While the majority of courts applying this rule have done so in the context of compelling arbitration or declining to stay arbitration (*i.e.* before the tribunal has reached a decision on jurisdiction), the D.C. Circuit joins the Second,[3] Fifth,[4] and Eighth[5] Circuits in applying the rule in confirmation of an arbitral award, sharply limiting the possibility of judicial review after a tribunal empowered to decide arbitrability has made its decision.

The D.C. Circuit had ruled in *Rep. of Argentina v. BG Group PLC*, 655 F.3d 1363, 1371 (D.C. Cir. 2012), that the United Kingdom-Argentina Bilateral Investment Treaty's (BIT) incorporation of the UNCITRAL Rules constituted clear and unmistakable evidence of an agreement to arbitrate arbitrability. However, that decision was ultimately vacated upon the Supreme Court's ruling that the Court of Appeals had not afforded due deference to the arbitral tribunal's determinations concerning compliance with the BIT's waiting period. *See BG Grp., PLC v. Rep. of Argentina*, 134 S.Ct. 1198, 1207 (2014). By echoing its previous holding in *BG Group* that a bilateral investment treaty's incorporation of the UNCITRAL Rules evidences the parties' intent to arbitrate arbitrability – which holding was not addressed, let alone overruled, by the Supreme Court's decision in that case – the D.C. Circuit thus confirmed that principle as prevailing law in the D.C. Circuit through its decision in *Chevron v. Rep. of Ecuador*.



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1 Ecuador also objected to confirmation of the award under Article V(2)(b), which permits non-recognition of an award if "the recognition or enforcement of the award would be contrary to the public policy" of the country in which enforcement is sought. These arguments were similarly rejected by the Court of Appeals.

2 514 U.S. 938 (1995).

3 *Schneider v. Kingdom of Thailand*, 688 F.3d 68 (2d Cir. 2012).

4 *Petrofac, Inc. v. DynMcDermott Petroleum Operations Co.*, 687 F.3d 671 (5th Cir. 2012).

5 *FSC Securities Corp. v. Freel*, 14 F.3d 1310 (8th Cir. 1994).