Part II - How does the so-called "fork-in-the-road" provision in Article 26(3)(b)(i) of the Energy Charter Treaty work? Why did the United States decline to sign the Energy Charter Treaty?

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How does the so-called "fork-in-the-road" provision in Article 26(3)(b)(i) of the Energy Charter Treaty work?

Like many Bilateral Investment Treaties and investment chapters of Free Trade Agreements, the Energy Charter Treaty contains a so-called "fork-in-the-road" provision that requires a claimant to make an irrevocable choice of forum for its claim. Specifically, Article 26(3)(b)(i) bars an Investor from submitting its claim to arbitration if the following conditions can be cumulatively demonstrated: (i) "the Investor party to the dispute"[2] (ii) "concern[ing] an alleged breach of an obligation of the [Contracting Party to the dispute] under Part III" of the ECT[3]; (iii) has "previously submitted the dispute"[4] (iv) "to the courts or administrative tribunals of the Contracting Party to the dispute" or to "any applicable, previously agreed dispute settlement procedure."[5]

Article 26(3)(b)(i) merits several observations. *First,* unlike fork-in-the-road provisions in other treaties, Article 26(3)(b)(i) is not available to all Contracting Parties, but only to those that have made a declaration that they wish to be listed in Annex ID, which is entitled "List of Contracting Parties not allowing an Investor to resubmit the same dispute to international arbitration at a later stage under Article 26 (in accordance with Article 26(3)(b)(i))." Contracting Parties *not* listed in Annex ID have extended their unconditional consent to arbitrate a dispute under the Treaty,

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[2] ECT Art. 26(2).

[3] *Ibid.,* Art. 26(1).

[4] *Ibid.,* Art. 26(3)(b)(i).

[5] *Ibid.,* Arts. 26(2)(a)&(b).

even if the same dispute has already been submitted elsewhere.[6] Slightly less than half of the Energy Charter Treaty's signatories opted to retain their rights under Article 26(3)(b)(i) and are listed in Annex ID.[7]

Second, under Article 26(3)(b)(i), the mere "submission" of the dispute to the relevant forum results in a forfeiture of the arbitral claim. In contrast, under certain other treaties such as the North American Free Trade Agreement (NAFTA) and the Central American Free Trade Agreement (CAFTA), the prior submission of the dispute to the courts of the host State will not automatically bar the arbitral claim. Rather, the investor need only waive the right to "continue" any such proceeding at the time it submits its claim to arbitration.[8]

Third, Article 26(3)(b)(i) applies only with respect to "previously" submitted disputes. The Investor is, therefore, free to submit the same dispute to another forum any time *after* it submits its claim to arbitration under the Treaty. In contrast, the NAFTA and CAFTA require the claimant to waive for all time the right to initiate duplicative claims in the courts or administrative tribunals of the Respondent State.[9]

Fourth, the ECT's fork-in-the-road applies only to "[d]isputes between a Contracting Party and an Investor of another Contracting Party."[10] It has no effect on an arbitral claim, for

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[6] The Arbitral Tribunal in *Petrobart Ltd. v. The Kyrgyz Republic,* for example, confirmed that the claimant could not be barred from submitting a claim to arbitration under the ECT by virtue of the "fork-in-the-road" provision in Article 26(3)(b)(i) because "the Kyrgyz Republic chose not to be listed in Annex ID of the Treaty." *Petrobart Ltd. v. The Kyrgyz Republic,* Arbitration No. 126/2003, Stockholm Chamber of Commerce, Final Award of March 29, 2005, p. 56.

[7] Those signatories are: Australia, Azerbaijan, Bulgaria, Croatia, Cyprus, the Czech Republic, the European Communities, Finland, Greece, Hungary, Ireland, Italy, Japan, Kazakhstan, Mongolia, Norway, Poland, Portugal, Romania, the Russian Federation, Slovenia, Spain, Sweden, and Turkey.

[8] North American Free Trade Agreement, Art. 1121(1)(b); Central American Free Trade Agreement, Art. 10.18(2)(2)(b). These mechanisms are sometimes referred to as "no U-turn" provisions.

[9] NAFTA, Art. 1121(1)(b); CAFTA, Art. 10.18(2)(2)(b).

[10] ECT, Art. 26(1).

instance, where the prior dispute was submitted by a locally incorporated subsidiary of the Investor, but not the Investor itself. Nor would it bar a claim where the prior dispute involved, for example, a subnational authority or parastatal entity of the Contracting Party, but not the Contracting Party itself.

In contrast, some other treaties such as the NAFTA and the CAFTA expressly require *both* the claimant and any locally-incorporated enterprise that is owned or controlled by the claimant (where the claim is for loss or damage to the claimant's interest in such enterprise, or is brought by the claimant on behalf of the enterprise) to waive their rights to initiate or continue any duplicative proceeding in the courts or administrative tribunals of the Respondent Party.[11] The waiver requirement in those Treaties can also apply to a prior proceeding even if the Respondent Party was not named in that proceeding. In *Waste Management, Inc. v. United Mexican States,* for example, the NAFTA Tribunal dismissed the claim primarily on the basis that the claimant had failed to withdraw proceedings brought by its Mexican subsidiary – but not the claimant itself – against a Mexican State-owned bank and the city of Acapulco – but not the State of Mexico.[12]

Fifth, Article 26(3)(b)(i) specifically defines the "dispute" as one "concern[ing] an alleged breach of an obligation of the [Respondent] under Part III" of the ECT.[13] It therefore bars an arbitral claim only where the prior dispute alleged a breach of the Energy Charter Treaty itself, and not some other source of law. In contrast, the NAFTA and CAFTA require the claimant to waive the right to pursue a broader class of domestic proceedings:

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[11] NAFTA Art. 1121(1)(b) & 2(b); CAFTA, Art. 10.18(2)(b).

[12] *Waste Management, Inc. v. United Mexican States,* Case No. ARB(AF)/98/2, Award of June 2, 2000, at para. 27 ("[T]he domestic proceedings initiated by Acaverde fall within the prohibition of NAFTA Article 1121 in that they refer to measures that are also invoked in the present arbitral proceedings as breaches of NAFTA provisions, namely non-compliance with the obligations of guarantor assumed under a line of credit agreement requiring Banobras to defray invoices not paid by Acapulco city council, and non-compliance by Acapulco city council through its failure to pay said invoices.").

[13] *Ibid.,* Art. 26(1).

namely, any proceeding that merely refers to the same "measure" that is at issue in the Treaty arbitration.[14] The US-Chile Free Trade Agreement arguably contains an even broader waiver requirement, conditioning jurisdiction on the investor's forfeiture of its right to pursue any claim "with respect to the *events* alleged to give rise to the claimed breach" of the Treaty.[15]

Finally, a consistent line of case law interpreting fork-in-the-road provisions similar to that contained in Article 26(3)(b)(i) of the ECT have applied the so-called "triple identity" test, which

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[14] NAFTA Art. 1121(1)(b) & 2(b) (providing that a disputing party may submit a claim to arbitration only if it waives its right to pursue "any proceeding with respect to the measure of the disputing Party that is alleged to be a breach [of the NAFTA]."); CAFTA Art. 10.18(2)(b) (similarly requiring waiver of "any proceeding with respect to any measure alleged to constitute a breach [of the CAFTA]."). As the NAFTA Tribunal in *Waste Management* explained with respect to pending domestic proceedings, "when both legal actions have a legal basis derived from the same measures, they can no longer continue simultaneously." *Waste Management, Inc. v. United Mexican States*, Case No. ARB(AF)/98/2, Award of June 2, 2000, at para. 27.

[15] US-Chile FTA, Art. 10.17(2)(b) (emphasis added). Likewise, the fork-in-the-road in Article 8 of the Argentina-France Bilateral Investment Treaty addresses disputes "relating to investments made under this Agreement between one Contracting Party and an investor of the other Contracting Party," and is therefore not limited to claims alleging a breach of the BIT itself. As the annulment committee in *Compagnia de Aguas del Aconquija S.A. v. Argentine Republic* explained with respect to that provision:

> Article 8 [of the Argentina-France BIT] deals generally with disputes "relating to investments made under this Agreement between one Contracting Party and an investor of the other Contracting Party." It is those disputes which may be submitted, at the investor's option, either to national or international adjudication. Article 8 does not use a narrower formulation, requiring that the investor's claim allege a breach of the BIT itself. Read literally, the requirements for arbitral jurisdiction in Article 8 do not necessitate that the Claimant allege a breach of the BIT itself: it is sufficient that the dispute relate to an investment made under the BIT. . . . In the Committee's view, a claim by CAA against the Province of Tucumàn for breach of the Concession Contract, brought before the contentious administrative courts of Tucumàn, would *prima facie* fall within Article 8(2) and constitute a "final" choice of forum and jurisdiction, if that claim was coextensive with a dispute relating to investments made under the BIT.

Compagnia de Aguas del Aconquija S.A. v. Argentine Republic, Case No. ARB/97/3, Decision on Annulment of July 3, 2002, at para. 55.

requires the Respondent Party to show: (i) identity of parties; (ii) identity of cause of action; and (iii) identity of the object of the dispute.

That test was applied, for example, in *Occidental Exploration and Production Company v. Ecuador.*[16] In 1999, Occidental Exploration and Production Company (OEPC) entered into a participation contract with Petroecuador, a State-owned Ecuadorian corporation, to undertake exploration for and production of oil in Ecuador. In 2001, the Ecuadorian tax administration (*Servicio de Rentas Internas* (SRI)) issued resolutions denying OEPC the refund of value added tax paid on purchases required for its exploration and exploitation activities under the contract. OEPC challenged those resolutions before the Ecuadorian courts on the ground of inconsistency with the Ecuador's legislation. OEPC subsequently initiated arbitration proceedings for breach of the US-Ecuador BIT. Ecuador raised a fork-in-the-road objection, arguing that OEPC was precluded from submitting the dispute to arbitration as it has made an irrevocable choice to submit that dispute to the Ecuadorian courts. The Tribunal, interpreting the Treaty's fork-in-the-road provision, observed that: "To the extent that a dispute might involve the *same parties, object and cause of action* it might be considered as the same dispute and the 'fork in the road' mechanism would preclude its submission to concurrent tribunals."[17] The Tribunal held that the BIT's fork-in-the-road was not triggered, however, because the arbitral claim was "treaty-based," whereas the court proceedings were based on domestic law.[18]

Likewise, in *CMS Gas Transmission Co. v. The Republic of Argentina,* the Respondent argued that CMS was barred from submitting its claim to arbitration under the Argentina-US BIT by virtue of the fork-in-the-road provision because Transportadora de Gas del Norte (TGN), an Argentine company in which CMS held a minority stake, had appealed a judicial decision to the

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[16] *Occidental Exploration and Production Company v. Ecuador,* LCIA Case No. UN3467, Final Award of July 1, 2004.

[17] *Ibid.,* para. 52 (emphasis added).

[18] *Ibid.,* para. 57.

Federal Supreme Court of Argentina and had sought other administrative remedies that Argentina alleged were redundant with CMS's arbitral claim.[19] The Tribunal rejected that argument. Referring to the decisions of other ICSID tribunals, the Tribunal held that:

> [A]s contractual claims are different from treaty claims, even if there had been or there currently was a recourse to the local courts for breach of contract, this would not have prevented submission of the treaty claims to arbitration. This Tribunal is persuaded that with even more reason this view applies to the instant dispute, since no submission has been made by CMS to local courts and since, even if TGN had done so—which is not the case—this would not result in triggering the "fork-in-the-road" provision against CMS. Both the parties and the causes of action under separate instruments are different.[20]

Similarly, in *Azurix v. The Argentine Republic,* the Tribunal rejected the Respondent's fork-in-the-road objection because the causes of action in the two proceedings were different, and because "[n]either of the parties [Azurix and Argentina] is a party to the proceedings before the local courts. Even if Azurix had joined ABA as a plaintiff in those courts, there would not be party identity since Argentina is not party to any of those proceedings."[21] This reasoning was reiterated as well in *Enron Corporation and Ponderosa Asset, LP v. The Argentine Republic.*[22]

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[19] *CMS Gas Transmission Company v. The Republic of Argentina,* ICSID Case No. ARB/01/8, Decision on Objections to Jurisdiction of July 17, 2003, 42 ILM 788 (2003), para. 77.

[20] *Ibid.,* para. 80.

[21] *Azurix Corp. v. The Argentine Republic,* ICSID Case No. ARB/01/12, Decision on Objections to Jurisdiction of December 8, 2003, 43 ILM 262 (2004), at para. 89.

[22] *Enron Corporation and Ponderosa Asset, LP v. The Argentine Republic,* Decision on Jurisdiction of January 14, 2004, ICSID Case No. ARB/01/3, at para. 98; *see also* C. Schreuer, "Traveling the BIT route: Of waiting Periods, Umbrella

The implication of the above is that the conditions for invoking the Energy Charter Treaty's fork-in-the-road provision will not often be met. Only a minority of Contracting Parties reserved the right to bar claims on that basis to begin with. Even with respect to those States that did reserve that right, however, the path that leads to the Investor's forfeiture of its Treaty claims is exceedingly narrow, and can easily be sidestepped by the alert investor.

Because many domestic legal systems do not even provide a private right of action to enforce treaty rights, it is not possible in many cases for the investor to bring a claim in a domestic court or administrative tribunal based on alleged breaches of the obligations in Part III of the Treaty.[23] Even where such a cause of action is provided for, however, the investor could easily circumvent the ECT's fork-in-the-road simply by construing its claims as arising only under domestic law, or some other applicable law, but not the Treaty. Moreover, Tribunals are wont to find that a fork-in-the-road has been triggered unless the claimant has made a deliberate *choice* to bring the domestic proceeding, as opposed to having been compelled by circumstances to protect its rights.[24]

Clauses and Forks in the Road", J. World Inv. & Trade, Vol. 5, No. 2, April 2004, pp. 247-248 ("The picture emerging from this consistent case-law is reasonably clear. The fork in the road provisions and the consequent loss of access to international arbitration applies *only if the same dispute between the same parties has been submitted to domestic courts or administrative tribunals* of the host State before the resort to international arbitration.") (emphasis added).

[23] Where the Treaty claims are based in whole or in part on an alleged breach of a contract or "any other obligations entered into with [the] Investor or [its] Investment" pursuant to Article 10(1), however, and the prior proceeding involved the same contract or other obligations, the Investor could conceivably forfeit the right to submit some or all of its claims to arbitration under the Treaty, assuming the other conditions of Article 26(3)(b)(i) are met.

[24] *See, e.g., Occidental Exploration and Production Company v. Ecuador,* LCIA Case No. UN3467, Final Award of July 1, 2004, at para. 60 ("The 'fork-in-the-road' mechanism by its very definition assumes that the investor has made a choice between alternative avenues. This in turn requires that the choice be made entirely free and not under any form of duress.").

Finally, as demonstrated by all of the cases above that address fork-in-the-road provisions, domestic judicial or administrative proceedings are more often commenced by a locally incorporated company instead of by its foreign shareholders, and they are often brought against a local authority or State-owned company, instead of the State itself. Accordingly, the identity-of-the-parties requirement will likewise not be satisfied in many cases, either as a matter of course or by design.

Why did the United States decline to sign the Energy Charter Treaty?

More than a dozen years after the Treaty was opened for signature in Lisbon on December 17, 1994, debate still lingers on this question, as well as related questions concerning the impact of the United States' decision. Unsurprisingly, no single, straightforward answer is to be found. Rather, the complexity of factors requires some understanding of the historical context in which the Treaty negotiations took place.

In 1990, when Netherlands Prime Minister Ruud Lubbers first proposed the concept of the "Energy Charter," the Soviet Union's energy sector appeared to be in serious turmoil. Western European countries feared a precipitous decline in oil and gas imports in the absence of an immediate injection of capital and know-how into the Soviet Union and its Republics.

The initial offspring of Prime Minister Lubbers' vision was the European Energy Charter, a non-binding declaration of intent signed at The Hague on December 17, 1991 by nearly fifty States and the European Community. The Charter sought to maintain open markets for former Soviet Union (FSU) energy exports through GATT-type non-discrimination policies and to promote energy transit and encourage foreign direct investment into the FSU energy sector. Originally a European initiative, the United States and other non-European members of the Organization for Economic Cooperation and Development (OECD) joined the negotiating process and signed the Charter.

The Conference subsequently began the process of translating the Charter principles into a legally-binding international trade and investment agreement. The United States was deeply involved in those negotiations from the start. As one participant to the negotiations has observed, the United States' imprint on the Treaty was "profound," particularly in the areas of investment protections and dispute resolution.[25]

One goal espoused by the United States that was not adopted, however, was the extension of national treatment to "making investments" – also referred to as the "pre-establishment" phase, when for example, foreign firms bid on leases for oil reserves or apply for government permits. As originally conceived, the ECT allowed Contracting Parties to list exceptions to national treatment for making investments. Many of the FSU States, however, lacked a legal structure for trade and investment, and could not list exceptions to national treatment because they could not determine what those exceptions might be. The Russian Federation demanded a three-year grace period following the Treaty's signature to pass legislation that would not be subject to the Treaty's obligations. In response, the European Community proposed a "two treaty" approach whereby "pre-establishment" rights would be deferred to a second treaty.

The United States at first strongly resisted that approach, indicating that it was unwilling to sign the first treaty without seeing the content of the second treaty. In December 1993, the United States reluctantly agreed to accept the "two-treaty" model, considering its change in position to be a major concession by the United States toward its negotiating partners.

In June 1994, the Conference Chairman, Dutch Ambassador Charles Rutten, gavelled through approval of the treaty text, and on September 14, issued a "final text for adoption" over the

[25] Presentation of Craig Bamberger, Investment Protection and the Energy Charter Treaty Conference, Washington, D.C., May 18, 2007; see also William Fox, *The United States and the Energy Charter Treaty: Misgivings and Misperceptions*, in The Energy Charter Treaty: an East-West Gateway for Investment & Trade (ed. T. Wälde 1996).

United States' objection that further negotiations were needed to resolve outstanding issues. The signature ceremony took place on December 17, 1994, the third anniversary of the Charter's signing. At the ceremony, the United States announced that it would not sign the Treaty, stating that the international investment standards in the ECT were "unacceptably low," and fell short of the "standards that the US has obtained in its bilateral investment instruments and in multilateral investment agreements".[26]

General and specific factors contributed the United States' decision not to sign the Treaty. One underlying factor was the United States' ambivalence from the start towards the largely European-driven process.

In its BIT negotiations, the United States was not accustomed to deviating significantly from its Model BIT – which was the product of much inter-agency development. Agreeing to protections different from its BITs, the United States feared, would set a harmful precedent in the context of its ongoing BIT negotiations, as well as in the context of the investment policy negotiations taking place at the OECD. The United States felt that its investors would be sufficiently protected by the many bilateral investment treaties that had been signed or were in the process of being negotiated with many of the FSU States.[27]

The Energy Charter Treaty also lacked the support of U.S. industry, which generally favoured securing Russia's ratification of the U.S.-Russia BIT, which had been signed by the United States and Russia in 1992, and ratified by the U.S. Congress that

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[26] Speculation that the United States actually decided not to sign the Energy Charter Treaty much earlier seems unfounded. The National Economic Council Deputies Committee made the decision not to sign the Treaty on December 15, 1994, two days before the signature ceremony, and communicated that decision to the Energy Charter Secretariat on the same day.

[27] Between March 1990 and March 1994, the United States had signed bilateral investment treaties with Armenia, Belarus, Bulgaria, the Czech Republic, Estonia, Georgia, Kazakhstan, Kyrgyzstan, Moldova, Poland, Romania, the Russian Federation, Slovakia and the Ukraine, and was in negotiations with Albania, Hungary, Lithuania, Turkmenistan and Uzbekistan.

same year. Finally, the United States raised concerns about what it viewed as a significant loophole in Russia's obligations to guarantee the right of capital transfer for foreign enterprises that had been negotiated in late 1994 by the Russian Central Bank.

The two "deal-breaker" issues for the Clinton administration that were not resolved in time by the negotiating parties, however, were the following:

(1) The ECT did not contain an exemption for U.S. sub-federal entities (*i.e.*, states). The United States felt that without such an exception, such as that contained in the investment chapter of the North American Free Trade Agreement (NAFTA),[28] the Treaty would infringe on certain powers and responsibilities of the states (*e.g.*, to levy taxes, issue licenses, and register businesses). The United States Senate, which represents the interests of the states in the U.S. Federal legislature, must give its "advice and consent" to all treaties. According to the United States, without an exemption for sub-federal entities, U.S. ratification of the Energy Charter Treaty would not have been feasible. Other negotiating parties understandably were not willing to accede to Russia's demand that any sub-federal exemptions be extended reciprocally to the Russian Federation, which would have offset many of the Treaty's benefits by removing Russia's numerous regional authorities from the Treaty's obligations.

(2) The Treaty's unconditional provision of most-favoured-nation treatment also conflicted with Title IV of the 1974

[28] Article 1108 of the NAFTA provides that "Articles 1102 [National Treatment], 1103 [Most-Favored-Nation Treatment], 1106 [Performance Requirements] and 1107 [Senior Management and Boards of Directors] do not apply to: "a state or province, for two years after the date of entry into force of [the NAFTA], and thereafter as set out by a Party in its Schedule to Annex I . . . or [to] a local government." Each Party may "set out in its Schedule to Annex I, within two years of the date of entry into force of [the NAFTA], any existing non-conforming measure maintained by a state or province, not including a local government."

> Trade Act, commonly referred to as the "Jackson-Vanik Amendment." Jackson-Vanik was enacted in response to U.S. concerns over the emigration policies of certain countries, particularly those of the Soviet Union. In November 1994, the United States believed that it had reached a solution through the ongoing energy cooperation negotiations in the Gore-Chernomyrdin Commission. The United States had declared Russia to be in full compliance with Jackson-Vanik, and had communicated to Russia the expectation that Russia would fully graduate from the purview of Jackson-Vanik, but that such a step could only be taken in consultation with Congress, a process that could not be completed before signing the Treaty. The negotiating parties, however, did not agree to a Treaty exception to accommodate the Jackson-Vanik Amendment.

The urgency with which the Treaty was concluded—arising in part from the realization that earlier concerns over FSU energy markets had been overblown, allowing negotiating parties more leeway to push their national interests—left little room to resolve these two issues that were important for the United States. It is not possible to say whether, given more time, those two issues could have been resolved, or whether their resolution would have led the United States to sign the Energy Charter Treaty.

In any event, the passage of time has proven the United States' rejection of the Energy Charter Treaty to have been extremely short-sighted. As the world's largest energy investing country, the United States' participation could have contributed significantly to achieving the Treaty's goals for promoting Western investment in the energy sector in Russia and the other FSU States. And with a tightening global oil market, the United States' commercial and strategic interests in Eurasian energy affairs have only increased since the time the Treaty was signed.[29]

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[29] As the Secretary General of the Energy Charter Secretariat, Andre Mernier, noted an April 4, 2006 speech before the United States Energy Association, "American companies are prominent participants in some world-

Moreover, the United States did not end up concluding bilateral investment treaties with many of the FSU States that have ratified the ECT, including Uzbekistan, Tajikistan, Turkmenistan, Slovenia, Hungary, and Bosnia-Herzegovina. Nor did Russia ever ratify the U.S.-Russia Bilateral Investment Treaty.[30] As a result, U.S. energy investors in those FSU States are arguably at a significant commercial disadvantage to their European competitors. The US investors who purchased Yukos American Depositary Receipts, for example, might have benefited had the United States signed the Energy Charter Treaty.

The avenue is still open, of course, for the United States to accede to the Energy Charter Treaty pursuant to Article 41 "on terms to be approved by the Charter Conference." It remains to be seen whether the United States will find it in its interest to do so.

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class Eurasian energy projects, for example the development of the Tengiz oil field in Kazakhstan."

[30] Although Russia has not ratified the Energy Charter Treaty, it applies the Treaty on a provisional basis pursuant to Article 45(1).