School of International Arbitration, Queen Mary, University of London

International Arbitration Case Law

Academic Directors: Ignacio Torterola
*Loukas Mistelis**

BG GROUP PLC.
V.
REPUBLIC OF ARGENTINA
CASE NO. U.S. 12-138 (2014)
U.S. SUPREME COURT

Case Report by Laura Ghitti**
Edited by Loukas Mistelis***

In a decision rendered on March 5, 2014, the US Supreme Court ruled on a 7-to-2 majority that an UNCITRAL arbitral tribunal did not exceed its powers by waiving a treaty requirement that recourse to arbitration would be possible only where disputes had been submitted for 18 months to the host State competent courts.

Tribunal:	Supreme Court of the United States. Associate Justice Stephen G. Breyer delivered the opinion of the Court. Associate Justice Sonia Sotomayor concurred in part and Chief Justice John G. Roberts and Associate Justice Anthony M. Kennedy dissented.
Counsel to BG Group:	Before the US Supreme Court: Mr. Thomas Goldstein, Mr. Kevin Russel and Mr. Tejinder Singh, Goldstein & Russel; and, Mr. Alexander Yanos, Mr. Elliot Friedman and Ms. Julia Lisztwan, Freshfields Bruckhaus Deringer.
Counsel to Argentina:	Before the US Supreme Court: Mr. Matthew Slater, Ms. Teale Toweill, Ms. Veronica Yepez, Mr. Jonathan Blackman, Ms. Carmen Amalia Corrales and Mr. Carmine Boccuzzi, Cleary Gottlieb Steen & Hamilton.

* Directors can be reached by email at ignacio.torterola@internationalarbitrationcaselaw.com and loukas.mistelis@internationalarbitrationcaselaw.com

** Laura Ghitti is a Brazilian attorney and is currently doing a Postgraduate Degree in Private International Law at Université Panthéon-Assas.

*** Loukas Mistelis is co-Director of International Arbitration Case Law (IACL).

INDEX OF THE MATTERS DISCUSSED

Digest

1. Facts of the Case

In 1990, BG Group plc ("BG Group"), a British corporation, formed part to a consortium that had a majority interest in MetroGas, an Argentine gas distribution company that held a 35-year exclusive license to distribute natural gas in Buenos Aires. At that time, Argentina's regulatory framework provided that its regulators would calculate gas tariffs in U.S. dollars in a way sufficient to assure gas distribution firms a reasonable return.

In 2001, Argentina adopted a series of measures in order to contend an economic crisis that hit the country. Among these measures, gas tariffs started being calculated from U.S. dollars to Argentine pesos, at an exchange rate of one dollar per peso.

2. The Arbitral Award

In 2003, BG Group started arbitral proceedings under the UNCITRAL Arbitration Rules invoking Article 8 of the Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Republic of Argentina for the Promotion and Protection of Investments (the "Treaty" or the "BIT"). The seat of the arbitration was Washington, DC.

In brief, BG Group claimed that Argentina's new laws and regulatory practices had violated provisions of the BIT that amounted to an expropriation and that Argentina had breached the standards of treatment provided in Article 2.2 of the BIT (promotion and protection of the investment). Argentina not only denied these claims but also argued that the dispute was not within the jurisdiction of the arbitral tribunal. Among other jurisdictional objections, Argentina alleged that, as stipulated in Article 8 of the BIT, recourse to arbitration would be possible only where disputes had been submitted for 18 months to its competent courts and the tribunal had not issued a final decision or the parties were still in disagreement after the decision.

In a final award rendered in 2007, the arbitral tribunal decided that it had jurisdiction with respect to all BG Group's claims. Regarding Argentina's position that BG Group had not complied with Article's 8 requirement, the arbitral tribunal held that Argentina's conduct had waived (or excused) BG

Group's failure to litigate before its courts. The arbitral tribunal took into consideration a decree issued by the President of Argentina staying for 180 days the execution of its court's final judgments in suits resulting of the new economic measures. The impossibility faced by firms that were litigating against Argentina to renegotiate the impact of these measures was also stressed.

In the merits, the arbitral tribunal denied the claim of expropriation, but found that Argentina had breached Article 2.2 of the BIT and therefore was ordered to pay US $185,285,485.85 for damages to BG Group's investment.

3. Procedural History

In March 2008, both parties filed petitions in the District Court for the District of Columbia. While BG Group sought to confirm the award under the New York Convention and the Federal Arbitration Act, Argentina sought to partially vacate it alleging that arbitrators lacked jurisdiction. In 2011, the District Court confirmed the award and rejected Argentina's claims.

In 2012 and after a petition was filed by Argentina, the Court of Appeals for the District of Columbia Circuit reversed this decision. In accordance with the appeals court, the interpretation and application of the local litigation requirement in the Treaty was a matter for courts to decide *de novo*.

BG Group filed a writ of certiorari before the Supreme Court of the United States that, in a 7-to-2 majority opinion, reversed the decision of the appeals court. This opinion, the opinion concurring in part and the dissent are reported below.

4. Legal Issues Before the US Supreme Court

In the words of the Supreme Court, "*the question before us is who – court or arbitrator – bears primary responsibility for interpreting and applying Article's 8 local court litigation provision. Put in terms of standards of judicial review, should a United States court review the arbitrators' interpretation and application of the provision* de novo, *or with the deference that courts ordinarily show arbitral decisions on matters the parties have committed to arbitrators?*" (*Opinion of the Court,* p. 6).

To answer this question, the majority initially treated the "document" before it (the Treaty) as if it were an ordinary contract between private parties (a). Then, the majority verified whether the fact that this document is a treaty would impact on its conclusion (b).

(a) If the document before the Supreme Court were an ordinary contract, who should interpret and apply the local litigation provision: judges or arbitrators?

The majority opened its analysis by saying that "*where ordinary contracts are at issue, it is up to the parties do determine whether a particular matter is primarily for arbitrators or for courts to decide*" (*Opinion of the Court*, p. 7). In the absence of such determination, presumptions will guide courts in order to find the parties' real intent.

Regarding these presumptions and based on US case law[1], the majority stated that "*[o]n the one hand, courts presume that the parties intend courts, not arbitrators, to decide what we have called disputes about 'arbitrability'. […] On the other hand, courts presume that the parties intend arbitrators, not courts, to decide disputes about the meaning and application of particular procedural preconditions for the use of arbitration*" (*Opinion of the Court*, pp. 7-8).

Bearing this distinction in mind, the majority analyzed the structure contained in the BIT and held that the litigation provision pertained to the second variety and therefore was a purely procedural requirement: "*The text and structure of the provision make clear that it operates a procedural condition precedent to arbitration. It says that a dispute 'shall be submitted to international arbitration' if 'one of the Parties so requests,' as long as 'a period of eighteen months has elapsed' since the dispute was 'submitted' to a local tribunal and the tribunal 'has not given its final decision.' Art. 8(2). It determines* when *the contractual duty to arbitrate arises, not* whether *there is a contractual duty to arbitrate at all. […].*" (*Opinion of the Court*, p. 8).

The Court concluded that, were the document an ordinary contract, arbitrators and not courts should interpret and apply the procedural local litigation provision (*Opinion of the Court*, p. 9).

(b) The fact that the document is question is a treaty makes a crucial difference?

Leaving the ordinary contract assumption aside, the majority asked whether the fact that the document in question is a treaty would make a difference in its analysis.

---

[1] *Howsan v. Dean Witter Reynolds, Inc.*, 537 U.S. 79, 84 (2002).

Besides the Solicitor General view that this fact would amount into a contrasting conclusion, the majority took a contrary approach. Firstly, it considered whether the litigation requirement was a condition on the State's consent (i). Secondly, the majority analyzed whether there was any evidence in the Treaty about who should rule on the litigation provision (ii).

(i) Is the local litigation requirement a condition on the State's consent?

In the majority's opinion, the fact that the litigation provision was inserted in a treaty did not change its previous conclusion. The majority considered that this provision was not a condition on the State's consent to enter into an arbitration agreement. In its view, "*a treaty is a contract, though between nations. Its interpretation normally is, like a contract's interpretation, a matter of determining the parties' intent*" (*Opinion of the Court*, p. 10).

It was pointed out that presumptions supplied by American law should be taken into consideration to interpret the intent of the parties in a motion to vacate or confirm an award made in the United States under the Federal Arbitration Act (*Opinion of the Court*, pp. 10-11).

The majority stressed that while it was possible to read the litigation provision as a consent to arbitration and thus on the contract's formation, "*doing so is not consistent with our case law interpreting similar provisions appearing in ordinary arbitration contracts*" (*Opinion of the Court*, p. 15).

Regarding the Solicitor General's view about the proper interpretation of treaties and the case *Abbott v. Abbott*[2], the majority explained that it had been "*unable to find any other authority or precedent suggesting that the use of the 'consent' label in a treaty should make a critical difference in discerning the parties' intent about whether courts or arbitrators should interpret and apply the relevant provision*" (*Opinion of the Court*, p. 11).

While the majority left opened the question of express reference to a condition of consent, it stated that "*[w]e are willing to assume with the Solicitor General that the appearance of this label [consent] in a treaty can show that the parties, or one of them, thought the designated matter quite important. But that is unlikely to be conclusive*" (*Opinion of the Court*, p. 11).

Additionally, the majority also observed that the Treaty does not define the local litigation requirement as a condition of consent to arbitration and left "*for another*

[2] *Abbott v. Abbott*, 560 U.S. 1, 15 (2010).

day the question of interpreting treaties that refers to 'conditions of consent' explicitly" (*Opinion of the Court*, pp. 12-13).

Associate Justice Sonia Sotomayor joined the opinion of Court and agreed that the local litigation requirement in this case was a procedural precondition to arbitration. However, she disagreed with the majority's statement that the express use of the term "consent" in a treaty would not be conclusive. She noted that this suggestion was unnecessary and incorrect. In her judgement, in the absence of the reserve to leave to "another day" treaties that refer to conditions of consent explicitly, the Court's opinion might be construed otherwise (*Opinion Concurring in Part*, pp.1-2).

Justice Sotomayor concluded that "*[...] if the local litigation requirement at issue here were labelled a condition on the treaty parties' 'consent' to arbitrate, that would in my view change the analysis as to whether the parties intended the requirement to be interpreted by a court or arbitrator*" (*Opinion Concurring in Part*, p. 3).

(ii) Is there any evidence in the Treaty about who should rule on this issue?

The Supreme Court also held that the Treaty contained no evidence that could show a different intent of the parties about who should decide threshold issues related to arbitration (*Opinion of the Court*, p. 13).

The majority highlighted its previous statement that the text and structure set forth in Article 8 was a procedural condition precedent to arbitration: "*The Treaty nowhere says that the provision is to operate as a substantive condition on the formation of the arbitration contract [...]. And the Treaty itself authorizes the use of international arbitration associations, the rules of which provide that arbitrators shall have the authority to interpret provisions of this kind*" (*Opinion of the Court*, p. 14)[3].

5. Decision

The Supreme Court reversed the decision of the Court of Appeals for the District of Columbia Circuit. It held that arbitrators, not courts, should interpret and apply the local litigation provision of the Treaty. Consequently, arbitrators' jurisdictional determinations were lawful.

[3] The majority mentioned Article 23(1) of the 2010 UNCITRAL Arbitration Rules and Article 41(1) of the 2006 ICSID Convention, Regulation and Rules.

6. Dissent

Chief Justice John G. Roberts dissented and was joined by Associate Justice Anthony M. Kennedy. The first remark made in the dissent was that the document before the Court was not an ordinary contract between private parties, but a treaty between two sovereign nations. Therefore, "*it should come as no surprise that, after starting down the wrong road, the majority ends up at the wrong place*" (*Dissent*, p. 1).

Giving particular importance to the nature of the document before the Supreme Court, the dissent asserted that the local court litigation requirement constituted a condition on the formation of the arbitration agreement and that Argentina never consented to arbitrate (a). Then, domestic courts should decide *de novo* (b).

(a) Argentina has never consented to arbitration

In accordance with the dissent, the majority did not explain "*when and how Argentina agreed with BG Group to submit to arbitration*" (*Dissent*, p. 3). By interpreting the structure of the Treaty (i) and the nature of the obligations assumed by a State (ii), the dissent found that Argentina had never consented to arbitrate.

(i) Interpretation of the Treaty

The dissent argued that the majority focused on the "arbitration clause" rather than in the structure contained in Article 8 and its paragraphs. It was noted that this article submits any dispute of an investor with a contracting party to the contracting party own courts (Article 8.1). Then, Article 8(2)(a) provides two different routes that lead to arbitration, both of them passing through the contracting party's domestic courts. The first one allows a party to request arbitration "*after a period of eighteen months has elapsed from the moment when the dispute was submitted to the competent tribunal of the Contracting Party in whose territory the investment was made*" (Article 8(2)(a)(i)). The second route to arbitration is stated by Article 8(2)(a)(ii): "*where the final decision of the aforementioned tribunal has been made but the Parties are still in dispute*" (*Dissent*, pp. 4-5).

In addition to this mechanism, paragraph 8(2)(b) provides a third route to arbitration in cases where the contracting party and the investor have so agreed, without passing through the local litigation provision . According to the dissent, this omission is significant, as "*[i]t makes clear that an investor can bypass local*

litigation only by obtaining the Contracting Party's explicit agreement to proceed directly to arbitration" (*Dissent*, p. 5).

Therefore, the structure contained in Article 8 would confirm that both routes to arbitration set forth in paragraph (2)(a) are a matter of consent and would constitute an offer to arbitrate conditioned to a period of litigation before Argentine courts. In the words of the dissent, "*[u]nless the investor does so [...], it has not accepted the terms of Argentina's offer to arbitrate, and thus has not formed an arbitration agreement with Argentina*" (*Dissent*, p. 6).

The dissent also contended that there was no reason to require an express label of "consent" to a have a condition of consent to arbitrate. Instead of a condition precedent to the performance of the contract, the dissent considered the provision set forth in article 8(2)(a) a condition to the formation of the arbitration agreement (*Dissent*, pp. 6-9).

Thus, it was held that there was no completed arbitration agreement between Argentina and the British investor given that Argentina conditioned its consent to the 18-month litigation requirement that BG Group failed to comply with.

(ii) Nature of the obligations incurred by a State in a BIT

In order to determine whether there was a procedural precondition or a condition of consent, the dissent also took into consideration the nature of the obligations a State incurs in agreeing to arbitrate: "*Substantively, by acquiescing to arbitration, a state permits private adjudicators to review its public policies and effectively annul the authoritative acts of its legislature, executive and judiciary*" (*Dissent*, p. 10).

By giving to private adjudicators a power of its own courts, States would specify "limited circumstances in which foreign investors can trigger the Treaty's arbitration process" (*Dissent*, p .11).

(b) Domestic courts must decide de novo

According to the dissent, "*[g]iven that the Treaty's local litigation requirement is a condition on consent to arbitrate, it follows that whether an investor has complied with that requirement is a question a court must decide de novo*"(*Dissent*, p. 12). It would be a logical consequence on the fact that an arbitrator's authority depends on the consent of the parties (*Dissent*, pp. 12-16).