

EXECUTIVE REPORT

Comprehensive citizen audit of reciprocal investment protection treaties and the investment arbitration system in Ecuador

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INTRODUCTION

The context in which Bilateral Investment Treaties are signed

The signing of Bilateral Investment Treaties (BITs) was a fairly widespread trend in Latin America and throughout the world in the 1980s and 1990s. It was influenced, and even induced, by a series of international factors, which were combined with internal factors in each country.

Latin America had achieved accelerated growth rates based on a domestic market-oriented model that sought industrialization based on import substitution and included strong protectionism and state intervention in the economy. In some countries, including Ecuador, little progress was made in industrialization and the economy continued to be based on extractivism. This strategy showed signs of exhaustion in terms of its capacity to sustain accelerated growth rates and low inflation. This, coupled with the external debt crisis of the 1980s, made a change necessary. However, no in-depth reflection and analysis of the merits, successes and limits of this strategy was ever carried out to determine which changes were advisable. Instead, the crisis was exploited by new emerging political elites who, in alliance with business sectors, came into power.

In the case of Ecuador, the foreign debt crisis, provoked by the rise in interest rates induced by U.S. monetary policy along with international oil prices, exploded in 1982. Politically, the rise to power of Febres Cordero (1984-1988) marked a shift towards neoliberalism, a trend that was continued and consolidated by subsequent governments.

These internal economic and political events in our countries were interwoven with external factors that were equally decisive in nature.

At the ideological level, neoliberal economic theory, promoted by the governments of the United States and England and supported by many of the major universities in developed countries, was becoming a quasi-unique way of thinking. This was summed up in the so-called Washington Consensus of 1989. In terms of foreign investment, the Washington Consensus posited the idea that there is no possibility of development without foreign capital, and that without investment protection, no foreign investment would be attracted.

Furthermore, the foreign debt crisis made possible the intervention of the International Monetary Fund (IMF), which conditioned its support for the renegotiation of such debts and the granting of bridge loans on the signing of letters of intent. Ecuador signed 16 letters and notes with the IMF between 1983 and 2003. The World Bank promotes what it called “structural adjustment” by

conditioning its loans to follow these guidelines. Both the letters of intent signed with the IMF and the World Bank policies imposed the guidelines of the Washington Consensus. These internal and external factors, which were both ideological and coercive, led to the consolidation of neoliberalism throughout Latin America by the mid-1980s.

However, it was only a matter of time before the social and environmental effects of neoliberalism began to spark growing opposition in our countries, which raised alarm bells in the power centers of global capital, particularly in the U.S. and Europe. Both governmental and corporate global power centers wondered whether it would be possible for the neoliberal model to be sustained and reproduced if this opposition translated into electoral victories that put governments critical of said model into power. In the absence of allied governments, the strategy of global capital and the neoliberal model would be in jeopardy. The promotion of Free Trade Agreements and Reciprocal Investment Promotion and Protection Treaties should be understood in this context. These Treaties are a cornerstone of the supranational legal framework that limits the regulatory power of governments and protects transnational capital. Governments that attempted changes outside the neoliberal framework would be sued in international arbitration courts.

Latin American governments have long argued that national laws and national courts are the best place to decide disputes between foreign investors and states. This resistance was expressed in the so-called Calvo Doctrine. However, during the 1990s, a process of change in domestic investment regulations and the signing of investment protection agreements began. This change was brought about by the external debt crisis, which led governments to seek international capital by attracting investment as opposed to incurring debt. This was coupled with the dominant neoliberal thinking on the need to offer legal certainty to investors, an idea promoted by trusted institutions in the countries of the Global South, such as the United Nations Conference on Trade and Development (UNCTAD).¹

Ecuador followed the same trend. During the 1990s, fundamental changes were made to domestic investment legislation and the majority of the BITs were signed:

- 1993: Executive Decree 415 published on January 13, 1993, issued by Sixto Durán Ballén, under the name of Regulatory Norms on Foreign Investment and on Contracts for the Transfer of Technologies, Trademarks,

Patents, Licenses and Royalties. This measure initiated a full opening to foreign direct investment, under similar conditions as national investment, with total freedom of location and financial flows, in addition to expressly prohibiting local entities from imposing requirements or granting any type of authorization.

- 1993: Law for the Modernization, Privatization and Provision of Public Services by the Private Sector, which made it possible to reduce the size of the State by transferring functions to the private sector, offering investment spaces in highly attractive areas such as mass-use public services.

- 1993: Reforms to the Hydrocarbons Law, which allowed ordinary and customary contracts under any of the contractual forms in force in the national legislation, with preference for private interests over those of the Republic. The share of operating revenues was increased in favor of private companies, with severe detrimental effects on the state's share. When the State attempted to suspend these burdensome concessions and recover its legitimate revenues, it was sued by these companies, as noted in the audit findings.

- Withdrawal from the Organization of Petroleum Exporting Countries (OPEC), and replacement of Decisions 24 and 220 of the Andean Community of Nations (CAN), which established limits on foreign investment to safeguard the interests of its nations and safeguards in areas of natural resource exploitation, with Decision 291 of 1991, which was adapted to the model of openness and liberalization.

- Following this, foreign direct investment did increase, but only in the oil sector, where the appeal and determining factor was the enormous profits guaranteed through these new types of contracts; and not precisely the signing of BITs, which were rarely taken into account in other economic areas.

- 1994: The General Law of Financial Institutions offered advantages and concessions to foreign investors, such as the opening of off-shore offices and the free flow of financial capital and money transfers abroad.

- 1997: The Foreign Trade and Investment Law (LEXI) embraced the principle of fiscal neutrality and guaranteed tax stability, whereby the State renounced the use of budgetary policy and social justice instruments.

- 1997: The Law for the Promotion and Guarantee of Investments established the free entry of capital to all economic sectors, without any authorization whatsoever, free monetary transfers abroad for any purpose and solid long term tax stability.

- Both the LEXI and the Law for the Promotion and

Guarantee of Investments were repealed during the current Government, in 2010, with the issuance of the Organic Code of Production, Foreign Trade and Investments

- 2006: Membership in the World Trade Organization, under a policy of openness, legal compatibility in foreign trade, tariff reduction mechanisms and the setting of ceilings. Elimination of all non-tariff restrictions, price bands, seasonal restrictions and other restrictions to protect domestic production from price variations. The country also committed not to apply any restrictions on international payments and transfers for routine transactions.

All these changes sought to accommodate domestic legislation to the BIT regulations. The amendments to national legislation and the rights established in the BITs not only ensured legal certainty for investors, but also granted them special rights and limited the sovereign authority of the State to regulate the economy and, in particular, foreign direct investment (FDI).

Why should we audit the Reciprocal Investment Protection Treaties and the International Investment Arbitration System?

During the 1990s, foreign investment volumes grew, not only in Ecuador but in the region as a whole. This seemed to confirm that the FDI protection strategy was the right strategy. Expectations also increased regarding the potential of foreign investment to contribute to the country's growth. However, in the decade that followed, FDI inflows stagnated. Highly profitable areas of exploitation had been surrendered, the State's capacities had been restricted, enormous privileges had been granted, and yet the country was still struggling to reach its potential. Meanwhile, a large number of million-dollar lawsuits from transnational corporations were filed. This litigation began to make use of the privileges of investment protection agreements to block any public policy effort that might diminish expected profits.

As time went by, the need to verify whether the signing of investment protection agreements had really achieved the desired objectives, not only in terms of attracting FDI, but also in terms of generating the expected benefits for the host country, began to gain traction.

At the international level, academia began to question whether there was truly a direct, causal relationship between the signing of BITs and the increase in FDI. Many arrived at the conclusion that no such relationship existed.² There is empirical evidence that the increase in FDI in the 1990s was driven by other factors, among them, capitalizing on the privatization processes that occurred during the first neoliberal governments.

Social movements in various parts of the world, which had for decades waged struggles against the excessive investor rights consecrated in Investment Agreements (for example, against the Multilateral Agreement on Investment, or MAI), once more emphasized the need for States to regain sovereignty and regulatory power. They likewise expressed the need for a new international foreign investment regime that would prioritize human rights, peoples' rights and the rights of nature over commercial law. These social movements in Ecuador, and at the Latin American level, expressed their support for the Ecuadorian initiative to carry out an audit of the BITs.

Not only academia and social movements, but also the international community as a whole, began to question whether the outcome of the signing of the BITs was ultimately positive. International organizations such as the United Nations Conference on Trade and Development (UNCTAD) and the Economic Commission for Latin America and the Caribbean (ECLAC), backed by a large body of empirical research on foreign investment flows and their effects on host economies, changed their positions and began to question the benefits of the existing investment protection system. These organizations called for changes in the investment protection model in order to achieve a balance between legal certainty and investment attractiveness, while preserving the State's regulatory capacity and directing FDI in accordance with national priorities.³

Of late, some governments in Latin America, as well as in other continents, have decided to withdraw from these treaties. Countries as diverse as South Africa and Australia, and more recently Indonesia and Pakistan, have carried out processes to review their investment protection policies. Both Australia and South Africa concluded that these policies were in need of radical changes.⁴ South Africa and Indonesia, along with Bolivia, Venezuela and Ecuador, have already begun to phase out Bilateral Investment Protection Treaties, and are in the process of developing alternative models that will guide the signing of similar agreements in the future.

In Ecuador, President Rafael Correa was highly critical of these treaties since his first election campaign and has launched international initiatives against this model, which he describes as perverse. The process of reviewing the Ecuadorian investment protection model began in the mid-2000s. This was particularly the case following the ratification of the 2008 Constitution, which reinforced and strengthened the mandate of a regulatory State, a move that was at odds with the commitments made in the BITs.

In Ecuador, concern continued to grow as the number of million-dollar investor lawsuits increased in response to

sovereign acts of recovery and defense of national assets that had previously been mortgaged in favor of external interests.

In 2013, amidst a scenario where the investment protection system and the international arbitration mechanisms were quickly losing national and international legitimacy, the President of the Republic decided to re-examine the conditions under which the BIT negotiations took place, the presumed errors of consent, the abusive clauses in the treaties and contracts, and the other indisputable signs of fraudulent practices. It was then decided that an audit should be carried out with citizen participation. This audit sought to provide information and transparency, along with indicating responsibilities and establishing precedents to ensure rigorous management, with a focus on national interests in the use of external resources.

The President of the Republic, economist Rafael Correa Delgado, issued Executive Decree No. 1506 of May 6, 2013, which created the Commission for the Integral Citizen Audit of Reciprocal Investment Protection Treaties and the Investment Arbitration System (CAITISA).

The comprehensive audit of public credit, which was carried out between 2007 and 2008, was used as a precedent. The objective of said audit was to lend greater transparency to the way in which public indebtedness had been incurred and the destination of the funds, as well as to establish the responsibilities of the creditors and other institutional and personal actors. Its valuable results provided a foundation for favorable solutions that led to a significant reduction in Ecuador's commercial debt.

The Decree by which CAITISA was created determined that the oversight action, accompanied by citizens, should address the process of treaties signed and negotiated by Ecuador, the consequences of the application of these treaties, their content and compatibility with national legislation, the validity and relevance of the procedures adopted, the awards and decisions issued in international arbitration processes against Ecuador, their legality, legitimacy and lawfulness, as well as inconveniences and irregularities that have caused or could cause impacts to the State and Ecuadorian peoples and nationalities in economic, social and environmental terms.

The Commission, by provision of the same Decree, was composed of: the heads or their delegates of four State institutions (the National Secretary of Planning and Development, the National Secretary of Policy, the Ministry of Foreign Affairs and Human Mobility and the General Legal Secretary of the Presidency of the Republic); and eight national and international experts, some from civil society and/or representatives of social

organizations, with experience in investment and/or international arbitration.

The international character of the Commission was ensured by the participation of experts from the following countries: Argentina, Colombia, Ecuador, Mexico, Paraguay, Uruguay and Singapore.

This audit process is just one of the Ecuadorian government's initiatives, and it forms part of a broader set of measures that seek to reaffirm national sovereignty in the regulation of foreign investment and the promotion of public policies that benefit the rights of peoples and nature over corporate profits. Other measures taken by Ecuador in this area include: the creation of a dispute settlement center as part of the Union of South American Nations (UNASUR), which provides for the application of alternative arbitration mechanisms such as mediation and conciliation;⁵ and the proposal to enact, at the United Nations, a code with binding human rights obligations for transnational corporations.⁶

1 M. Sornarajah (2011), Mutations of Neo-Liberalism International Investment Law, *Trade, Law and Development Journal*, 3(1): 203-232.

2 Poulsen, Lauge N. Skovgaard (2010). The Importance of BITs for Foreign Direct Investment and Political Risk Insurance: Revisiting the Evidence, *Yearbook on International Investment Law and Policy 2009/2010*, New York: Oxford University Press, pp. 539-574.

3 UNCTAD (2012) Investment Policy Framework for Sustainable Development http://unctad.org/en/PublicationChapters/wir2012ch4_en.pdf y World Investment Report 2015 - Reforming International Investment Governance <http://unctad.org/en/pages/PublicationWebflyer.aspx?publicationid=1245>

4 Republic of South Africa (2009), Bilateral Investment Treaty Policy Framework Review, Government Position Paper <http://www.pmg.org.za/files/docs/090626trade-bi-lateralpolicy.pdf>; Gobierno de Australia (2010) Bilateral and Regional Trade Agreements, Productivity Commission Research Report <http://www.pc.gov.au/inquiries/completed/trade-agreements/report/trade-agreements-report.pdf>

5 See <http://www.cancilleria.gob.ec/unasur-avanza-en-la-creacion-de-un-centro-de-solucion-de-controversias/>

6 See <http://business-humanrights.org/en/binding-treaty/un-human-rights-council-sessions>



AUDIT RESULTS

A. BILATERAL INVESTMENT TREATIES (BITs) IN ECUADOR

Negotiation and signing processes for BITs

Against the backdrop described in the previous section, and at the height of the implementation of policies aimed at facilitating capital flows, the country made the negotiation of investment protection treaties (BITs) one of the cornerstones of foreign policy during the 1990s. The State negotiated 30 of these treaties between 1968 and 2002, of which three did not enter into force: two of

them because, despite having been negotiated, they were not signed by the parties (in the case of Panama and Costa Rica) and one due to lack of ratification by the counterparty, as in the case of the BIT with Russia. Of the 27 BITs that did enter into force, the three-year BIT with Egypt expired on April 19, 1995, due to the non-renewal of the parties.

The following chart shows the presidency in which each of the 30 Bilateral Investment Treaties was signed:

President	Number of Treaties	Countries
José María Velasco Ibarra (1968-1972)	1	Switzerland (1969)
León Febres Cordero (1984-1988)	1	Uruguay (1985)
Rodrigo Borja (1988-1992)	1	Egypt (1992)
Sixto Durán Ballén (1992-1996)	16	United States, Chile and Venezuela (1993); Paraguay, Argentina, China, Great Britain, El Salvador and France (1994); Bolivia (1995); Panama ¹ , Germany, Romania, Russia, Canada and Spain (1996);
Fabián Alarcón (1997-1998)	2	Cuba (1997), Dominican Republic (1998)
Jamil Mahuad (1998-2000)	2	Netherlands and Peru (1999)
Gustavo Noboa (2000-2003)	7	Nicaragua and Honduras (2002); Sweden, Italy, Finland and Costa Rica (2001); Guatemala (2002)

Elaboration: CAITISA

On Ecuador's Negotiation of BITs

Following a thorough analysis of the files of various ministries, the audit process concluded that the BITs signed by Ecuador did not go through a negotiation process as such. There was no indication that there was any discussion about the form of BITs that Ecuador was signing, more specifically about the possible implications of the clauses contained in the treaties. This suggests that the government officials who signed the various BITs gave their approval and signature without having undertaken an analysis of the consequences of these international instruments, and without having attempted to negotiate terms that would preserve the state's regulatory capacity.

On the Ratification Process of BITs in Ecuador

The ratification process that BITs signed by Ecuador had to go through depends on the constitutional provisions and requirements in force at the time of their approval. Depending on the date on which the BITs were signed,

they had to follow the procedure of the 1968, 1979 (codified in 1984) or 1998 Constitutions (detailed information in the table below). The 1968 and 1979 Constitutions included legislative approval as a requirement. However, the 1998 Constitution excluded express legislative approval for some types of treaties; the interpretation of several government agencies during those dates was thus that BITs did not require legislative approval.

The process for the approval of these international treaties did not always comply with Ecuadorian legislation in force at the time of ratification. Other irregularities were also detected in the approval process due to circumstantial interpretations of laws or regulations and ad-hoc criteria of the authorities in office.

BIT/Date Signed	Under what Constitution was the BIT ratified?	Irregularities in the ratification procedure
Switzerland (1969)	Constitution of 1968	
Uruguay (1985)		The legislative branch was not consulted for approval, a requirement specified in Article 59.
Egypt (1992)		The legislative branch was not consulted for approval, a requirement specified in Article 59.
United States (1993)		Legislative approval was granted, but this approval was based on the report prepared by the Subcommittee on International Conventions and Treaties, instead of the Specialized Commission, as required by the Constitution of the time.
Chile (1993)		The legislative approval process took place without debate.
Venezuela (1993)		Approved by the National Congress
Paraguay (1994)		The legislative approval process took place without debate.
Argentina (1994)	Constitution of 1979	The legislative approval process took place without debate.
China (1994)		Approved by the National Congress
Great Britain (1994)		Approved by the National Congress
El Salvador (1994)		Approved by the National Congress
France (1994)		Approved by the National Congress
Bolivia (1995)		The legislative approval process took place without debate.
Germany (1996)		The legislative approval process took place without debate.
Rumania (1996)		The legislative approval process took place without debate.
Russia (1996)		The legislative approval process took place without debate. The BIT did not enter into force because Russia failed to ratify it.
Canada (1996)		The legislative approval process took place without debate.
Spain (1996)		The legislative approval process took place without debate.
Cuba (1997)		Approved by the National Congress
Dominican Republic (1998)		The legislative approval process was omitted.
Netherlands (1999)		The legislative approval process was omitted.
Peru (1999)		The legislative approval process was omitted.
Nicaragua (2002)	Constitution of 1998	The legislative approval process was omitted.
Honduras (2002)		The legislative approval process was omitted.
Sweden (2001)		The legislative approval process was omitted.
Italy (2001)		The legislative approval process was omitted.
Finland (2001)		The legislative approval process was omitted.
Guatemala (2002)		The legislative approval process was omitted.

Elaboration: CAITISA

Below is a breakdown of the special situations and irregularities that were found. These would give rise to legal and/or procedural questions:

- Eleven of the cases lack legislative approval records, according to the Deputy Secretary General of the National Assembly, in a letter dated October 17, 2014.

In the BIT cases with Egypt and Uruguay, the lack of legislative approval is an explicit omission of a requirement of the 1979 Constitution in force at the time. The lack of this requirement in the ratification process may lead to the interpretation that this Treaty never took effect; however, according to information provided by the Ministry of Foreign Affairs, it is in the list of treaties in force and its termination was requested by the executive branch to the National Assembly.

In the remaining nine cases, which refer to BITs signed since 1998, the omission of legislative approval seems to be due to a pro-investment interpretation of

Art. 161 of the 1998 Constitution. This article determined the types of international treaties and agreements requiring approval from the National Congress. Among them are mentioned: “Those that refer to the fundamental rights and duties of individuals and to collective rights.” It seems that, at the time, it was interpreted that the Investment Protection Treaties signed by Ecuador did not affect Ecuadorians' individual and collective rights.

This interpretation was maintained by government officials between the years 1998 and 2002. However, the analysis carried out by the audit determined that there are elements in the BITs signed that effectively compromise sovereignty and affect rights.

For example, the transfer of powers arising from the Constitution or the Law to an international or supranational body, (since the BITs state that disputes will be submitted directly to international arbitration) or the potential impact of the BITs on the fundamental rights and duties of individuals and collective rights, are reasons why the BITs merited the

Legislature's knowledge and approval.

The decision to exempt post-1998 BITs from legislative ratification was reinforced through negligent interpretations by State agencies. For example, Ministry of Foreign Affairs Order No. 8-AJ-DGAJ, dated January 12, 2001, determined the exclusion of the legislative approval, by the National Congress, of the BITs signed with Nicaragua, the Netherlands and the Dominican Republic and this was used as a basis for the ratification of these agreements by President Gustavo Noboa. It should be noted that an order of the Ministry of Foreign Affairs may under no circumstances be considered a binding document of constitutional interpretation.

- Seven treaties—those signed with Spain, Romania, Bolivia, Canada, China, Russia and Cuba—were approved in a single session (Act No. 16 of May 21, 1997), with two similar reports from the Special Permanent Committee on International Affairs, drafted succinctly for all the treaties and presented sequentially one after the other, also being voted on jointly and without debate. One legislator objected to the procedure because he believed that each treaty should have been debated and approved individually. It was decided that individual resolutions would be sent to the Ministry of Foreign Affairs.

The unusual procedure of multiple approvals, with reports that were likewise joint, shows the superficiality and lightness with which these proceedings took place. This violated the rule that a reasoned and substantiated pronouncement to be made for each agreement by both the Specialized Commission and the full Congress.

- The treaty with the United States, signed in 1993 and approved in 1994, was submitted for legislative approval with a report from the Subcommittee on International Agreements and Treaties, rather than with a report from the Special Permanent Commission, as required by constitutional provisions. By means of a request for reconsideration, one of the legislators, Diego Delgado, objected to the procedure inasmuch as there was no reading of the Treaty and as well as to the inappropriateness of the Subcommittee's report. Another request for reconsideration points to specific drawbacks and a serious impact on national sovereignty. Nonetheless, the Treaty was approved by a majority in the Plenary.
- The BITs entered into with Germany, France and Great Britain were approved by the National Congress with no reading of the text and with no debate.

The failure to read the Treaty and the Report is an irregularity that repeated in both cases of multiple approvals and in cases of individual processing.

The processes described above in essence show the level of persuasion and political commitment to the “need and convenience” of attracting foreign investment, along with the ready disregard for legal procedures despite the enormous magnitude of risk that the country assumed by granting rights, guarantees and ample concessions to foreign interests, without an inventory of benefits.

However, the analysis carried out by the audit determined that there are elements in the BITs signed that effectively compromise sovereignty and affect rights. These policies are complemented by the issuance of laws and legal reforms in the sense that they were issued at the same time, as mentioned in the preceding points.

Contents of the BITs signed by Ecuador

The Bilateral Treaties for the Reciprocal Protection of Investments, signed by Ecuador, are international instruments entered into with the purpose of offering investors a legal framework capable of protecting said investments from any governmental measure they could be affected by. An analysis of the 30 treaties signed by Ecuador (basic definitions, substantive clauses; clauses that regulate aspects such as the Treaty's duration and termination), allows us to conclude that most of the BITs follow a common model and structure. The only Ecuadorian BITs where certain differences can be found are those signed with Switzerland, Egypt and Uruguay; these BITs are shorter, do not include punitive precautions and do not include holdover requirements.

Preamble

Most treaties begin with a preamble defining the expectations and characteristics of the bilateral relationship and the objectives pursued by the parties through the treaty's implementation and enforcement; in practice, preambles are often taken to be merely declaratory in nature. However, arbitral tribunals use them with discretion, as an interpretative resource that may even be used to modify the scope of a treaty's substantive clauses.

Main clauses of BITs

Beyond the minor variations among the BITs Ecuador has signed with various countries, we can find standard clauses or common contents that mark a generic logic in the content of the substantive clauses. This set of clauses can be summarized in the following blocks:

The definition of investment: Describes what is meant by investment according to these agreements.

Following general parameters, Ecuadorian BITs protect both intangible and tangible assets. Intangible assets include all those associated with the movement of money and its derived rights (financial or speculative investments), as well as intellectual property rights. They also include administrative rights, such as concessions for the exploitation of natural resources.

The definition of investor: BITs are intended to protect foreign investors and to determine whether an investor is foreign, not only must nationality be identified, but also the origin of the investor's capital. If an investor seeks to benefit from a treaty, the investor must demonstrate that they hold the nationality of one of the States parties. All BITs, except for those signed with Uruguay and Egypt, have definitions of what is meant by "investor". In all cases, the concept includes both natural and legal persons who are nationals of one of the two state parties to the treaty, or who have their headquarters in the territory of one of these two states, respectively. Some treaties (such as the BITs with Venezuela, Chile, Argentina, El Salvador or Nicaragua), include an exception for persons who have resided in the country for more than two years at the time the investment was made; in such cases, they are not considered foreign investors. In the rest of the cases, and especially with developed countries, there is no such exception. This means that a natural person of French nationality can be based in Ecuadorian territory for ten years and yet, when making an investment, exercise the right to the protection of foreign investments based on the Ecuador-France BIT.

National treatment: Arises from commercial treaties and refers to the state's obligation to provide equal treatment to both foreign and domestic investments. This clause is found in most Ecuadorian BITs.

Fair and equitable treatment: Establishes that any procedure originating in the host country of the investment must not violate the minimum standards of international treatment of investments. It may include concepts such as the investor's "legitimate expectations". However, in and of itself, the expression "fair and equitable treatment" is indeterminate, ambiguous and may be subject to different interpretations. Several arbitral tribunals have extensively interpreted the concept of "fair and equitable" by incorporating ideas such as the investor's legitimate expectations, which are not provided for in the international legal systems. These interpretations thus go beyond the internationally-recognized standards of treatment of investment. In the case of Ecuador, the "fair and equitable treatment" clause is

found in almost all of the BITs that have been signed, except in the BITs with Egypt, the Dominican Republic and Honduras, where it is not explicitly mentioned.

Full Protection and Security: This clause usually indicates that the state is obliged to take appropriate measures to protect investments from adverse effects from the host state, any of its organs or third parties. Its nature is similar to that of "fair and equitable treatment" in that it is also general in its approach. This is why they are usually analyzed together, despite their differences. At the moment, consensus exists that the clause does not offer absolute protection against physical or legal infringements, and therefore the state is not responsible for preventing said infringements. In the case of Ecuador's BITs, the full protection and security clause is found in twenty-eight of the thirty BITs entered into. The exceptions are the BITs concluded with Egypt and Cuba.

Most Favored Nation (MFN): Used in trade agreements, it means that the most beneficial level of treatment granted to one country must be replicated and respected for the rest of the countries with which a state holds the same type of agreements. It is the amplification of legal relations, which are established in a restricted form and on a bilateral basis, to a generic network of relations with other treaties of the same nature. Together with other clauses, such as fair and equitable treatment and national treatment, it is one of the key clauses contained in the international protection scheme granted to investments through BITs. It has been included in the vast majority of BITs signed by Ecuador.

The MFN clause carries with it the risk of multilateralizing the same level of treatment to any investor, since the contracting parties, the states that sign the BIT, lose control of the benefits granted to foreign investments. Depending on the type of investment in question, this makes it difficult for them to exercise their power to issue differentiated policies. They also lose the ability to differentiate according to the investment's country of origin. This makes it impossible to privilege those countries with which integration, complementation or mutual support is sought, beyond the strictly commercial context.

In addition, it is very complicated and difficult to maintain the knowledge of the radial legal relations established by the MFN clause on the part of any subject that enters into this type of clause. This is because it allows a universe of investors from third states to sue the territorial state via a BIT between states of which it is not a national. Thanks to the

inclusion of legal standing for those with indirect control of a company, via the MFN clause, one must hold merely a single share of a foreign company listed on the stock exchange in order to sue the state whose BIT offers the most guarantees. As a result, the control and actual knowledge of legal obligations and the risks of lawsuits are transformed into an impossible-to-measure universe, with the result that the State must increasingly surrender its regulatory capacity. This “regulatory cooling” results in a new version of the state's withdrawal from its spheres of action in favor of the private sphere.

Prohibition of direct and indirect expropriation:

This is a prohibition on any direct or indirect measure that could affect a foreign investor. It is found in all of Ecuador's BITs. The prohibition of a direct expropriation clause refers to the forced dispossession of an investor's property by the state. Unless it is by sanction of law, BITs include this prohibition, by declaration of public utility and with the payment of a prompt and fair compensation to the private party. But BITs also include the prohibition of indirect expropriation; that is, any other measure that would have effects similar to an expropriation. This clause broadly opens the state to the possibility of claims; it is an open clause whose scope is not limited or restricted to specific acts; it restricts the state's ability to regulate certain areas considered central to the exercise of state functions. If the state decides to implement new regulations in an area of the economy, and these regulations negatively affect the foreign investor—who may interpret them to have an expropriatory effect on profits or investment within the national territory—this could cause the state (so as not to affect the business of foreign investors) to reduce its ability to set, modify or apply a regulation.

Free currency transfer: These are guarantees for investors to freely transfer their profits—or even the investment itself—abroad, without any type of requirements. All the BITs (with the exceptions of Uruguay and Egypt) contain this clause.

Dispute resolution mechanisms: These are the procedures for the settlement of disputes related to BITs between the state parties or between a foreign investor and the host state of the investment; it enables a natural or legal person to resort to international arbitration against a state. It includes the legal standing to sue, as well as the choice of forum (special arbitration, ICSID, UNCITRAL rules, international chambers of commerce, etc.).

Applicable law: determines what legal rules are applicable for the arbitral tribunal to issue its awards.

Fourteen of the 30 treaties include the option of resolving the dispute based on the state's domestic law; however, this is just one more possibility regarding the law to be applied in each case presented. Sixteen of the Ecuadorian BITs provide that the law governing dispute resolution is the BIT itself.

Survival or ultra-activity: Determines how long the treaty remains in force after a state party has denounced it. It allows for a period of activity following the formal entry into force of the treaty and permits the obligations and the possibility to sue to remain active for up to 20 years. Survival clauses in Ecuador's BITs cover a range of possibilities. The only BIT that provided for a 1-year survival clause was the first BIT with Germany in 1965. This was replaced by the BIT entered into in 1996, which currently has a 15-year survival clause. Only the BITs with the Dominican Republic (already withdrawn and with an extinct survival clause) and Italy have an ultra-activity of five years. In the rest of the treaties, the survival clauses are 10 or 15 years after the termination of these agreements has been pronounced. Only in the BIT with Great Britain is the survival period still longer than 20 years, after having been terminated.

Another anomaly is that BITs are usually tacitly renewable, meaning that if they are not terminated, they are automatically renewed for an additional period. Consequently, in the case of Ecuador, the renewal periods are 10 years.

Umbrella clause: By means of this clause, the state agrees to comply with any other investment commitments it may have assumed through other international agreements, the national legal system and contracts entered into by the state with foreign investors. The umbrella clause is not found in all BITs, nor does it emerge clearly when reading them. It is most commonly applied based on an interpretation by investment arbitration tribunals of various clauses in the BIT; in particular, the clauses the state's obligation to any other investment commitments it may have assumed from other sources, whose violation would imply a breach of the BIT. In the case of Ecuador's BITs, the presence of the umbrella clause is clearly evident in seven cases (USA, Paraguay, Great Britain, Canada, the Netherlands, Sweden and Italy), although there are also seven more cases in which it may arise through interpretation.

Fork in the Road Clause: The fork in the road clause is a clause whereby a foreign investor must opt for a domestic recourse or international arbitration and is unable to choose the recourse of the other option at a later time. In essence, it prevents the same case from

being presented simultaneously in several forums. This clause is found in half of the BITs signed by Ecuador. The BITs that do not include this clause are those signed with the USA, Great Britain, China, Russia, Canada, Spain, Finland, Sweden and Italy. On the other hand, this clause preventing the multiplication of claims is found in the BITs with Romania, Germany and France. This means that, since most investors come from large economies, they are able to replicate claims in different forums simultaneously, which constitutes an additional risk for the Ecuadorian state.

Compatibility of the BITs' substantive clauses with national and international regulations

In the face of internal policies and regulations and the state's regulatory capacity

Ecuador's BITs adhere to a traditional model that is followed by most of the world's nations, which include the same investment protection standards without considering each country's specific economic and social conditions.

A simple reading of the fundamental contents of the BITs, synthesized in the clauses referred to in the previous point, allows us to deduce the limitations on and interference in a state's power to manage and guide the foreign investment entering its territory based on its legitimate and sovereign interests. They do, however, ensure the possibility of states being subject to lawsuits and arbitration awards in the International Arbitration System that impose heavy economic sanctions for alleged breaches of treaty clauses.

There are several cases where conflicts and distortions between the clauses in BITs and the public commitments acquired and the legal structure of the Ecuadorian state have been identified.

In tax matters, the governments in office have issued laws and legal reforms according to public requirements and the national interest in applying tax justice and ensuring budget financing. However, under the BIT, the investor may challenge a tax measure, particularly when the investor claims that the measure is directly tantamount to indirect expropriation. The very presumption of the lawfulness and validity of the state's action is called into question and it will be the prerogative of the arbitral tribunal to rule on these issues.

The free flow of foreign currency to and from the exterior, which is guaranteed to a foreign investor, alters a state's power to regulate its currency (when Ecuador had national currency) and international reserves by controlling the flow of transfers to protect the balance in

its foreign accounts. Capital flight can be devastating for a State, creating instability in the economy and the financial sector. If these controls are exercised to prevent a crisis, the state could be sued internationally by the foreign investor for breaching a BIT under which it is bound to allow the free transfer of foreign exchange.

In the Constitutions in force in the Republic of Ecuador since 1978, the concept of indirect expropriation is not addressed or enshrined in any of the aforementioned norms. Nor was this figure explicitly recognized as an integral part of the domestic legislation, by which the state consents to a substantial limitation of its legislative, jurisdictional or other powers.

The 2008 Constitution reaffirms the state's right to expropriate and nationalize in accordance with customary international law. This power is exercised by the state for purposes of public utility or social and national interest. As in the preceding constitutional texts, we can see that there is no classification of the notion of expropriation under different categories; rather, there is an explicit mention of expropriation and nationalization. And this, without any doubt, is in accordance with the rule of international law. Expropriation or nationalization is, first and foremost, a state right arising from its character as a sovereign entity.

Firstly, the "national treatment" clause is contrary to the constitutional requirement that priority be given to domestic investment and that foreign investment shall be complementary to domestic investment. Secondly, it constitutes preferential treatment and gives supremacy to the foreign investor, since the national investor does not have the right of direct recourse to international arbitration.

In the face of the development objectives

The majority of the country's population has had to endure periods of injustice, inequity and poverty, while the stockpiling and concentration of profits in the hands of a few powerful domestic and foreign beneficiaries has grown at the expense of the exploitation of vast patrimonial resources. This reality led to several efforts to overcome such shortcomings and promote a genuine national development guided by fundamental objectives; these have remained in place since the emergence of appropriate planning mechanisms.

Naturally, these legitimate efforts to reduce marginality, unjust external economic dependence, to redistribute wealth, to promote equal opportunities and productive growth were relegated to the sidelines as private interests—such as those of the demands of foreign investors—were allowed to prevail over the public interest.

To cite specific ways in which provisions of the BITs are in conflict with development objectives, we turn to the proposals of the National Plan for Good Living (in Spanish, the Plan Nacional para el Buen Vivir, or PNBV) adopted by the current government.

With respect to investments, the current Constitution provides that both domestic and foreign investments must be oriented towards fulfilling the objectives of the National Development Plan, which implies state guidance, or at least supervision, for their effective realization. This is at odds with the liberality guaranteed in the BITs.

One of the objectives of the National Development Plan is state transformation and the recovery of regulatory and planning capacities aimed at satisfying the population's needs, which enables the adoption of legal measures and provisions in the exercise of national sovereignty. However, intolerably, the internal acts of the state, particularly those of a regulatory nature, are subject to international control where arbitrators are responsible for deciding whether such acts are in compliance with investment protection standards.

On the other hand, the privileged role granted to transnational corporations in the ownership of and access to the means of production, in accordance with their best interests, cannot be compromised even when state seeks to modify the productive matrix and the schemes of accumulation, distribution and the redistribution of wealth in society.

In the face of regional legislation defined in integration processes

Regional integration bodies have issued common procedures for the handling of foreign direct investment and the foreign capital flows that this entails. The most assiduous group that Ecuador is a member of is the Andean Community of Nations (CAN), established in 1969.

Among the first CAN Decisions was Decision No. 024 (December 1970), which established the Common Regime for the handling of foreign capital and for trademarks, patents, licenses and royalties, under the consideration that foreign investment “can make a considerable contribution to the economic development of Latin America, provided that it stimulates the capitalization of the country where it is based, facilitates the broad participation of national capital in this process and does not create obstacles to regional integration”.

These provisions established that the treatment of foreign capital may not discriminate against national investors; the widest possible access to modern technology and to the managerial innovations of the contemporary world; the

gradual transformation of foreign companies into national or mixed companies; the need for authorization of foreign investment by the corresponding authority, which will determine whether it will be admitted into sectors reserved for national public or private companies; restrictions on concessions in basic product sectors (including exploration and exploitation of hydrocarbons and forestry) with preference to contractual forms of association; prohibition of the establishment of foreign companies in the public services sector, as well as in financial activities (insurance, commercial banking and other financial institutions); no new direct foreign investment in domestic transportation companies, advertising, commercial radio stations, television stations, newspapers, magazines or in those dedicated to the domestic sale of products of any kind.

This Decision was amended in May 1987 by Decision 220, which retained its essential content. In particular, it reiterates that Member Countries shall not grant foreign investors any treatment more favorable than that granted to domestic investors and that for the settlement of disputes or conflicts arising from foreign direct investments or the transfer of foreign technology, Member Countries shall apply the provisions of their domestic legislation.

Furthermore, under this framework, the foreign credit operations of transnational companies were to be analyzed and authorized, with limits on interest rates. Had this policy been maintained, the country would not have undergone decades of harm due to the fraudulent practice of undercapitalization, highlighted later in this audit.

In March 1991, the pressures for a total reform of policies and systems in favor of maximum openness and liberalization of foreign investment took effect, leading the Andean Community of Nations to issue Decision 291, which is still in force today. It justifies the regional shift through the “implementation of an economic rationality based on private initiative, fiscal discipline and a resized and efficient state”.

The new norms embraced the model of liberality, incentives for private intervention and self-regulation. Examples include the establishment of equal rights and obligations for foreign and domestic investors, the free circulation of foreign currency and transfers abroad, and the extension to any foreign investor of the benefits of the Cartagena Agreement's Liberalization Program.

Regarding technology transfer contracts, Decree 415, issued by Sixto Durán, claims to comply with CAN Decision 291; however, it establishes only registration procedures and does not include the precautions and conditions for evaluation that are included in the Community standard to ensure effectiveness and

transparency in the execution of such contracts.

The trend in regional legislation regarding the system for the handling of foreign capital has not changed, although objections and questions have gradually spread among the governments of the Member Countries, often spurred by social movements demanding an end to the indolent exploitation by transnational corporations.

With the emergence of new organizations in the Latin American region (such as UNASUR and CELAC) proposals are gaining strength for a new international financial architecture that offers alternatives for the financing of national projects, and that organizes reliable bodies for the exercise of justice and the sovereign rights of the peoples.

In this context, the creation of the UNASUR Investment Dispute Settlement Center has been proposed, and the Southern Observatory on Investment and Transnationals—born out of the initiative approved at the First Ministerial Conference of Latin American States Affected by Transnational Interests, held on April 22, 2013 in the city of Guayaquil—is in operation.

In the face of international law and human rights

Ecuador, like most countries in the world, has adhered to international regulations protecting human rights. This includes not only the Universal Declaration of Human Rights, but also legally binding instruments such as the International Covenant on Civil and Political Rights and the International Covenant on Economic, Social and Cultural Rights.⁷ In fact, in 2000, Ecuador became the first Latin American country to sign all international human rights treaties adopted at the level of the United Nations and the Organization of American States. In 2006, the Ecuadorian government presented its candidacy to the United Nations Human Rights Council and in doing so, reaffirmed its commitment to the evolution of human rights.⁸

The BITs signed by Ecuador contain numerous legal obligations, but none of them consider human rights obligations; to the contrary, the BITs create a parallel legal framework, with its own set of obligations and its own system of application, and lacking any consideration of other international obligations. Even matters of an erga omnes nature, such as the legal framework of human rights, are left out. The ICSID arbitral tribunals that have rendered awards to date have not taken human rights into account in their decisions, even in their erga omnes recognition at the international level. However, in some cases, they have explicitly acknowledged that their decisions may involve self-interest.

Not only do the BITs and arbitral tribunals not consider human rights, but the rights of investors enshrined in the BITs and the possibilities granted to them to sue states directly violate the states' obligation to respect and ensure respect for human rights in state territory.

Recently, the United Nations Independent Expert on the promotion of a democratic and equitable international order, Alfred de Zayas, warned that “States enter into bilateral and multilateral free trade and investment treaties, which hinder the fulfillment of human rights treaty obligations and result in the violation of civil, cultural, economic, political and social rights”. As early as 2003, the UN Human Rights Council had expressed a similar view on the incompatibilities between BITs and the proper enforcement of human rights.¹⁰

In this debate, we should stress the hierarchy of norms. The valuation and hierarchy of international standards or obligations is referred to in Article 103 of the Charter of the United Nations, where it states: “Art. 103: In the event of a conflict between the obligations of the Members of the United Nations under this Charter and their obligations under any other international agreement, their obligations under this Charter shall prevail”. Such is the case of jus cogens norms and the erga omnes obligations of international law.

Notwithstanding these express commitments, the BITs signed by Ecuador negatively interfere with and affect the state's ability to respect, protect and fulfill its human rights obligations.

On the lack of binding obligations for international investors

The international standard for determining personal responsibility in human rights matters is found in the Statute of the International Criminal Court (ICC), established by the Rome Statute in 1998. However, the types of crimes established by this international instrument are framed in direct acts of violence such as genocide, crimes against humanity, crimes of aggression or crimes against international humanitarian law.

Nonetheless, human rights violations can be much more extensive and prolonged when, in order to defend its own, sometimes antagonistic, interests, a public (the state) or private (a transnational corporation) legal entity interferes with the enjoyment and exercise of social rights.

Transnational corporations can be drivers of progress and modernization, but, simultaneously, they can be strong constraints on states' economic, social and political sovereignty, resulting in major impacts that should not be exempted from guarantees for local populations. However, there is a lack of regulations at the global level to provide

communities with the same certainty about the rights and obligations that such companies demand from governments.

Responsibility for violation of the international human rights framework has been defined in normative terms in United Nations General Assembly resolutions, adopted in 2001, insofar as it concerns states in respect to internationally wrongful acts.

However, there is little legal reference to the responsibility of international organizations that have promoted policies of privatization and the unrestricted liberalization of markets—policies that have had an impact on the full enjoyment of individual and collective human rights. These organizations, which are the International Monetary Fund (IMF), the World Bank (WB), the Inter-American Development Bank (IDB), the World Trade Organization (WTO), the Organization for Economic Cooperation and Development (OECD), in addition to policies and conditions imposed, by different means, on peripheral states, have endeavored to grant guarantees to private capital, such as the adoption of mechanisms for the protection of foreign investment.

With the backing of influential actors and a legal framework that limits investor liability, it becomes clear that investors are entitled to all rights without any *quid pro quo*. This is why investment treaties, encouraged by international organizations and the governments of the countries in which the capital originates, do not stipulate binding international obligations for transnational corporations that would oblige them to respect and ensure respect for the rights of peoples, the environment, labor and cultural rights.

In the aforementioned circumstances, the most coherent option would seem to be the establishment of a worldwide legal framework for organizations that, due to their characteristics, act globally in the corporate field. The Ecuadorian initiative to create internationally binding codes that hold transnational corporations accountable for human rights violations fills this legal void. These codes could establish complementary jurisdictions in which the international human rights regime would be applicable worldwide, whether at the level of countries, individuals or legal entities.¹¹

Political decision on BIT termination

As regards the withdrawal from treaties, the general principle of international law determines that the procedure established in the instrument to be terminated must be followed. All of Ecuador's BITs include a termination clause that enables any of the signatory parties to unilaterally terminate the Treaty. The disadvantage inherent in the termination process is the

ultra-activity of these agreements, which is generally for periods of 10 or 15 years. Withdrawal from these treaties does not require the concurrent will of the parties that entered into the agreement, since it is a state's right to decide to withdraw and this act does not entail any conflict or incompatibility with any provision of international law.

Ecuador initiated the process of withdrawal from its BITs in 2008, simply by invoking the legal authority that the BITs themselves conferred for such purpose; these objective clauses were incorporated into each treaty at the time. As indicated, termination does not require prior consents that could condition or, in fact, “veto” the right to withdraw established in a clause.

The decision was based on the understanding that several commitments taken on through BITs constituted an erosion of state powers and were obstacles to the adoption and implementation of national development policies.

The first phase of the withdrawal process began in 2008, under the provisions of the 1998 Constitution. Nine TBIs were terminated in this process: Cuba, Honduras, Guatemala, Nicaragua, Paraguay, Dominican Republic, Romania, El Salvador, and Uruguay. According to the said Constitution, the termination process could be complied with solely by sending reversal notes to the embassies of the other subscribing party, notifying them of the Ecuadorian government's decision to terminate the respective BIT. The termination of these BITs was therefore concluded upon notification to the respective states. However, only the BITs signed with Uruguay, the Dominican Republic and Guatemala—a country that expressly declared the agreement terminated once Ecuador notified its withdrawal—have ceased to be in force; the others remain in force due to the application of the corresponding survival clause.

The second phase was completed with the initiation of the termination process for the remaining 17 of the 26 BITs in force, which began in 2010, subject to the provisions of the Montecristi Constitution, passed in 2008.

Ecuador established new rules in the 2008 Constitution regarding investment and submission to international arbitration, based upon which it was necessary to readjust Ecuador's political and institutional relations in this area. The new constitutional mandate that made the reorganization process initiated by the Ecuadorian State viable is an instrument that is directly inscribed in theergaomnes rule of self-determination and the right of each state and people to choose their own economic, social, political and cultural system. As a legal result, there was a fundamental change of circumstances, enshrined in the new Constitution of the Republic, in force since

September 2008.

The procedure for the withdrawal from international treaties was substantially modified in the 2008 Constitution, with the incorporation of steps such as: the resolution of termination from the National Assembly, the binding opinion of the Constitutional Court and the confirmation by the Presidency of the Republic.

Although the termination process has been initiated for all BITs, only a few have been completed. Most of them are

still in the process of going through the administrative, legislative and judicial acts required to complete the withdrawal. The following table identifies the status of each TBI with respect to the reporting process.

BIT	Executive Branch initiates complaint process	Binding opinion of the Constitutional Court	Assembly approves the termination	Confirmation from the Executive Branch	Current (yes/no)	Survival Clause
Egypt (ended in 1995 due to non-renewal)					No	N/A
Dominican Republic	2008			X	No	5 years
El Salvador	2008			X	Yes	10 years
Cuba	2008			X	Yes	10 years
Nicaragua	2008			X	Yes	10 years
Guatemala	2008			X	No	10 years
Honduras	2008			X	Yes	10 years
Uruguay	2008			X	No	N/A
Paraguay	2008			X	Yes	10 years
Rumania	2008			X	Yes	10 years
Finland	2010	X	X	X	Yes	10 years
Germany	2010	X	X		Yes	15 years
Great Britain	2010	X	X		Yes	20 years
France	2010	X	X		Yes	15 years
Sweden	2010	X	X		Yes	15 years
Netherlands	2010	X			Yes	15 years
Venezuela	2010	X			Yes	10 years
China	2010	X			Yes	10 years
Chile	2010	X			Yes	10 years
Switzerland	2010	X			Yes	10 years
Canada	2010	X			Yes	15 years
United States	2010	X			Yes	10 years
Argentina	2010	X			Yes	15 years
Bolivia	2010	X			Yes	10 years
Peru	2010	X			Yes	15 years
Spain	2010	X			Yes	10 years
Italy	2010	X			Yes	5 years

Elaboration: CATTISA.

On the ruling of the Constitutional Court

All of the BITs, for which the withdrawal process began in 2010 (under the 2008 Constitution), have Constitutional Court rulings. The Court declared that the BITs in force were wholly or partially incompatible with the new paradigms legally formulated in the Constitution of the Republic; among others, the recovery of national sovereignty, in general, and jurisdictional sovereignty, in particular, can be mentioned.

After analyzing the various BITs signed, the Court considered three arguments for their termination: First, the normative-social reorganization of the State, which set forth a new constitutional framework in relation to international obligations.¹² Second, in several opinions it explicitly referred to and invoked the termination clause contained in the investment treaties analyzed,¹³ and third, it revealed a series of incompatibilities between certain treaty rules, especially with regard to the transfer of powers, and constitutional provisions.

On the pending steps in the termination process

- a. The BIT with Finland is the only one that has completed the termination process;
- b. The files of the BITs with Germany, France, Great Britain and Sweden have favorable reports from the Specialized Commission and have been approved by the National Assembly; they are therefore awaiting notification to the corresponding countries and remain in force;
- c. The BIT signed with Italy does not have a favorable report from the Specialized Commission and therefore has not been submitted to the plenary of the Assembly;
- d. The proceedings for the termination of the BITs with China, Chile, Venezuela, and the Netherlands were debated in the plenary session of the National Assembly, but were not terminated; and,
- e. The BITs with Argentina, Bolivia, Canada, Spain, the United States, Peru and Switzerland are still waiting to be heard by the plenary of the National Assembly.

On objections to termination made by counterpart states

Of the ten BITs challenged, in only two cases has there been an objection by the other State to Ecuador's challenge. These are the cases of Uruguay and Romania,

both of which have raised disputes on a point of law, albeit on different issues.

In the case of Uruguay, said country raises not an explicit objection to the withdrawal of Ecuador, but a kind of counter-offer to said act which was made in a diplomatic note dated February 12, 2008: to open a "transition period" between the date of withdrawal and "until a new legal framework regulating investments between both states can be defined". In this transition period, Uruguay requested that the rights and guarantees to Uruguayan investors in Ecuador be maintained, with identical protection and treatment no less favorable than that provided to nationals of other states. What Uruguay is proposing is to agree on an ultra-activity of the rights established in the BIT, a permanence that the Ecuador-Uruguay BIT does not possess. Ecuador could therefore expressly consent to this request to maintain the effects of the BIT post-withdrawal, implying the survival of the denounced treaty "until a new legal framework is defined".

Romania was the only country to object to the Ecuadorian act of termination. In its note of March 3, 2008, with which it objects to the aforementioned act, it states that the BIT can be terminated only twelve months before the end of its term, since the sole legal possibility for termination before the BIT's finalization date is through mutual agreement of the parties, and it clarifies that the receipt and confirmation of the notice of termination does not constitute an expression of consent to such act.

First, Romania has every right to object to Ecuador's complaint. This poses a case of international controversy on a point of law, specifically on the interpretation of the final provisions of the BIT.

Since no *jus cogens* norms are involved, the appropriate way to resolve this dispute would have been for both States to decide, within a period of twelve months, on a method of peaceful settlement of disputes referred to in Article 33 of the UN Charter. However, this does not seem to have happened, as neither Ecuador nor Romania have held talks on how to resolve their dispute regarding the obligations of the BIT. The treaty is therefore in a legal "limbo", not addressed by any of the experts in the field.

On the survival or remanence clause

The survival or holdover clause is a treaty provision that determines the continuation, for a certain period of time, of the obligations of the states parties to a BIT, regarding the investments made in the territory of these countries prior to the BIT's termination. The purpose of this clause is to extend the protection afforded to foreign investment under a BIT, notwithstanding its termination, for a period of time conventionally determined by the countries that

signed the agreement.

Its particularity lies in the fact that it comes into play as an autonomous clause—as a source of conventional international obligations that persist in the burden of the state, even when the treaty has been terminated. This is undoubtedly a legal mechanism that substantially relativizes the rule “*Pacta Tertius nec nocent nec prosunt*”. Because of the holdover clause, the state that is no longer a party to the treaty would maintain any and all obligations. However, the survival clause would not apply to any investments made after the treaty has been terminated. In this case, the State is fully entitled under international law not to execute any of the conventional obligations, but rather, to fully apply its own domestic law.

Regarding the survival clause in the BITs signed by Ecuador, there are different periods for ultractivity, with the exception of Egypt and Uruguay, which do not include this clause. The TBIs with the Dominican Republic and Italy indicate five years. In the rest of the treaties, the survival clauses indicate ten or 15 years following termination. Only the BIT with Great Britain establishes a longer period, 20 years after termination.

It could be understandable that, in the context in which the BITs were signed, and in an effort to provide an acceptable level of legal certainty to investments made prior to a treaty's termination, the parties stipulate protection measures during the transition to an investment protection framework different from that of the BIT. What is incomprehensible is, together with the broadness of the BIT conditions, the number of years of most of the holdover clauses. During this time, they could contravene both the national legal system and the public policies implemented by the government, limiting the state's ability to determine its economic, financial and tax policies. Because of the remanence clauses in the BITs, Ecuador has been forced to substantiate disputes before international forums, despite the fact that this is expressly forbidden by the Ecuadorian Constitution.

Different doctrinal positions on the validity of the survival clause

Regarding the survival clause, it should be mentioned that there is no consensus in the doctrine on its implementation.

One school of thought holds that even if a country has terminated investment treaties and renounced the Washington Convention, the remanence clause still applies because of its specific nature in the various BITs. With its continued validity, international obligations remain intact and continue to be upheld, including those relating to international arbitration, in particular, before ICSID. The remanence clause is thus governed by the principle of *lex*

specialis between treaties.

Another school of thought, which originated in the 1969 Vienna Convention, holds that when a state denounces a treaty, it denounces the totality, i.e. the entirety of its provisions. Another school of thought, which originated in the 1969 Vienna Convention, holds that when a state terminates a treaty, it terminates the totality, i.e. the entirety of its provisions. In this perspective, the remanence clause does not acquire autonomy outside the treaty, since it is simply another provision.

In addition, it is argued that the direct effect of Ecuador's withdrawal from the Washington Convention is the inapplicability of any particular clause contained in the BITs, referring to the investor's discretionary right to settle a dispute with the state before the ICSID, against a non-Party state. The consent of both States Parties to the investment treaty is required for such a mechanism to be triggered.¹⁴ That is to say, a double requirement, or in its case, a consent for the specific case on the part of the state. According to this thesis, the Washington Convention's Article 72 does not give rise to a kind of consent *ad perpetuum* that would result in an obligation for the state.

On the interpretation of the Constitutional Court regarding the remanence clause

In some opinions concerning the constitutionality of BITs, the Constitutional Court referred to the survival clause. Without entering into a qualitative analysis of the clause, the Court holds that there is a direct relationship between the withdrawal from the treaty in question, the withdrawal from the Washington Convention and the remanence clause. This is more of an assertion than an analysis of the legal relationship based on conventional rules. Consequently, the thorny issue of the scope and content of the withdrawal from the 1965 Washington Convention, the exercise of ICSID jurisdiction and the clause in question were not addressed.

In most of the rulings, the Court affirmed that the international obligations to investors contained in the BITs would be applicable during the “transition period” between termination and the remanence period determined in each investment treaty. The Court's opinions accept that once the treaty has been terminated in its entirety, including the so-called holdover clause, with the exception of the article referring to the termination, each and every one of the treaty obligations continue to be directly applicable. Under this hypothesis, the new social, political and economic organization embodied in the 2008 Constitution would not be enforceable or applicable.

Since the rulings of the Constitutional Court may

correspond to acts of a state organ, the Constitutional Court's reasoning could be invoked by another state to claim the applicability and autonomy of the survival clause.

Ecuador and the Centre for Settlement of Investment Disputes (ICSID)

A key milestone in the establishment of the investment dispute settlement system was the enactment of the Washington Convention, signed in 1966, which created the Centre for the Settlement of Investment Disputes (ICSID). This Center is a supra-national institution established by the World Bank to hear and resolve disputes that may arise between an investor and the state receiving the investment.

Over time, it has become one of the main centers for the resolution of foreign investment disputes and the main tribunal in which the Ecuadorian State has been sued.

As a historical benchmark, it is worth mentioning that in 1964, during an annual meeting of the World Bank in Tokyo, together with 20 other developing countries, the government of Ecuador voted against the establishment of an investor-state dispute settlement center, what today is known as ICSID.¹⁵

Irregularities in the ICSID accession process

The documents that implement Ecuador's accession to the ICSID contain a series of irregularities that should be taken into account to verify the effective validity of submission to this arbitration tribunal. The ICSID Accession Agreement was signed in Washington on January 15, 1986, by the then Foreign Minister Edgar Terán Terán, during a visit to the city by former President León Febres Cordero. On the same day, Chancellor Terán addressed a communication to the World Bank, stating that the Agreement “is in full force and effect in accordance with the country's legal norms”.

Chancellor Terán's statement, contained in the aforementioned document, was clearly inaccurate: the approval of the National Congress and the ratification of the President of the Republic were necessary for the effective entry into force of the Agreement, as provided for in the 1979 Constitution, codified in 1984.

The responsible agencies of the World Bank announced that Ecuador had filed the instrument of acceptance of the Convention and communicated its effectiveness as of February 14, 1986 (30 days after the deposit), and this was in turn communicated to the member states of the Washington Convention.

Internally, actions arising from the Accession Agreement were carried out, such as the appointment of four

arbitrators and four conciliators for a renewable six-year term. The signing of BITs allowing ICSID to intervene in the settlement of disputes was also encouraged, with the assurance that Ecuador was a party to the Washington Convention.

The irregularity of the Agreement's validity, due to non-compliance with constitutional provisions, was observed by the Attorney General's Office (in Spanish, the Procuraduría General del Estado or PGE) through a first official letter addressed to the Minister of Foreign Affairs, dated February 19, 1987; a second official letter, with similar content, was addressed by the same entity to the Minister of Energy and Mines, on September 19, 1994.

Thereafter, the National Congress took steps for the approval of the ICSID Accession Agreement through requests made by the Executive Branch. There are communications to this effect in June 1995, in January 1996, in June and July 1997 and in the year 2000; in turn, the Congress requested that complementary documents be submitted to the Plenary for approval. At the same time, institutions interested in signing foreign investment contracts intervened and requested—in some cases at the demand of the investing companies—that the legal conditions for Ecuador's participation in the ICSID be fulfilled, since it was clear that the Convention did not comply with the fundamental requirements established under the Constitution.

A report dated November 24, 1994, presented by the Legal Advisor of the Ministry of Foreign Affairs, Teodoro Bustamante Muñoz in response to inquiries made by the Attorney General of the State and the Minister of Energy and Mines, highlighted the flagrant irregularities in the signing of the ICSID Accession Agreement, which this Audit summarizes in the following facts and implications:

Foreign Minister Edgar Teran made a false statement when he affirmed that the Agreement was in full force and effect in accordance with the country's legal norms, since it lacked legislative approval (as required by the Constitution) and, in the absence of presidential ratification, it was impossible for it to be in force in Ecuador. Such an assertion is cause for criminal liability due to the violation of the state's public faith.

The Ministry of Foreign Affairs did not carry out the necessary administrative inquiries with the Attorney General's Office, the Supreme Court of Justice, the National Development Council, the Monetary Board and the Central Bank, all institutions that could have issued an opinion on the advisability of signing the Agreement.

We know that it became commonplace for the former

President of the Republic, Leon Febres Cordero, to ratify international treaties without prior approval from the National Congress, in spite of the constitutional provision to do so; or he would decide on a case-by-case basis which treaty would or would not pass through the National Congress.

The interest and persistence of the actions of the then chancellor, Edgar Terán, in addition to the violation of the country's legal system at the time, can be explained by his personal interests. His law firm, Terán & Terán, represented—and continues to represent—the companies IBM and Merck, which sued Ecuador before the ICSID.

Lastly, the Convention of Accession to ICSID was approved by the National Congress on February 7, 2001, after a favorable report from the Constitutional Court, because the Convention “attributes the exercise of powers derived from the Constitution or the law to a supranational organization”. The Tribunal's criterion was that it “is in conformity with the constitutional text insofar as it conditions submission to the jurisdiction of the Centre to the existence of written consent by the parties”.

By means of Executive Decree 1417-B, published in the Official Gazette 309 of April 19, 2001, the President of the Republic at the time, Gustavo Noboa Bejarano, ratified the Agreement, declaring it a Law of the Republic. He stated that he “commits the National Honor to its observance”. It is clear that only thereafter would Ecuador have been bound to ICSID. Six months later, the first arbitration request was filed against the country by Repsol.

Given these circumstances, it could be argued that BITs signed before 2001, which accept ICSID's jurisdiction for dispute resolution, are invalid on that point and, therefore, disputes submitted for arbitration to the Centre would lack the Centre's jurisdiction requirement. Other internal regulations and norms issued before 2001 and referring to an International Convention to which Ecuador was not bound and a Centre to which it did not belong, would also have no legal value and would have to be examined.

Challenge to the ICSID Convention

The President of the Republic, Rafael Correa, by Executive Decree 1823, of July 2, 2009, challenges and declares the Agreement terminated. The then Foreign Minister, Fander Falconí, notified the President of the World Bank, whose response indicated that the termination would take effect six months after notification, that is, starting on January 7, 2010.

The denouncement of the ICSID Convention presupposes the existence of substantial changes with respect to the actions taken in the 1980s, 1990s and the first decade of the new century. Indeed, with the 2008

Constitution, Ecuador modified the rules by which the state functioned according to a legal system based on the neoliberal model. The new state organization represents a substantial change in its nature. The recovery of overall sovereignty, of the State's powers and its regulatory capacity, the enforcement of rights over natural and energy resources, and participatory democracy are all called for.

7 See http://tbinternet.ohchr.org/_layouts/TreatyBodyExternal/Treaty.aspx?CountryID=53&Lang=SP

8 See <http://www.un.org/ga/60/elect/hrc/ecuador.pdf>

9 Report of the independent expert on the promotion of a democratic and equitable international order on investor–state dispute arbitration (A/70/285). http://www.ohchr.org/Documents/Issues/IntOrder/A-70-285_en.doc

10 UN, Report of the UN High Commissioner for Human Rights “Human rights, Trade and Investment”.

11 The new binding codes on human rights for transnational corporations would be the instrument that includes jurisdiction over non-state legal entities in this area.

12 See, Opinion of the Constitutional Court, Ecuador-Chile treaty, 2010, p. 16.

13 See, Opinion of the Constitutional Court, Ecuador-Germany treaty, 2010, p. 36-37.

14 F. M. Lavopa, L.E. Barreiros, M. V. B. (2013). “How to Kill a BIT and not Die Trying: Legal and Political Challenges of Denouncing or Renegotiating Bilateral Investment Treaties”. *Journal of International Economic Law*, December: 874. These authors advocate the renegotiation of the clauses of the BITs relating to disputes.

15 See <http://triplecrisis.com/remembering-the-tokyo-no-fifty-years-later>

16 Annex 3 ICSID. Ministry of Foreign Affairs. Letter dated January 15, 1986 and signed by Dr. Edgar Terán.

B. ECUADOR BEFORE THE INTERNATIONAL INVESTMENT ARBITRATION SYSTEM

All investment protection treaties signed by Ecuador, except for the investment protection and promotion agreement signed with Switzerland, include an investor-state dispute settlement clause. This provides investors with different arbitration forum options and different arbitration rules for dispute resolution.

Foreign investors have the discretionary power to sue the State before the ICSID, or another international arbitration forum, for violation of international law and for calling into question their own liabilities, with all the consequences entailed by an internationally wrongful act. Domestic investors are deprived of this discretionary power.

The investor-State dispute settlement clause in BITs breaks with the Latin American tradition, also defended in Ecuador, of the Calvo Doctrine. This legal-political doctrine, written by the Argentine jurist Carlos Calvo, established the principle by which disputes with foreign citizens must necessarily be resolved by the local courts, thereby avoiding diplomatic intervention by the country of origin. The basis of this doctrine is found in the principles and rules of national sovereignty, the sovereign equality of states, and equality before the law between national and foreign citizens. The full exercise of one of the cornerstones of sovereignty is the territorial application of the law.

Status of investor-state litigation against Ecuador

Recent years have seen an exponential increase in multi-million dollar investor claims against states based on BITs. According to data from the United Nations Conference on Trade and Development (UNCTAD), in the 1987-1999 period only 38 cases existed globally; by the end of 2014, a total of 608 investor-state claims had been filed.¹⁷

Latin America is the region that has been hit the hardest by investment arbitration. Foreign investors had sued governments in Latin America and the Caribbean (LAC) at least 183 times by the end of 2013, representing 32.2% of the total number of known cases. According to UNCTAD, Ecuador is sixth worldwide in the countries that have received the most lawsuits.¹⁸

As of April 2017,¹⁹ the Ecuadorian State has been sued on 26 occasions by foreign investors before international tribunals on the basis of BITs; of that total, 12 claims have been filed before ICSID, while eight proceedings

have been filed before the Permanent Court of Arbitration in The Hague. On three occasions the claims have been submitted to the London Court of International Arbitration and, finally, in three cases, no court has been chosen to hear the case.

Most of the plaintiff companies operate in the oil exploration sector (13 cases, or 50%). Other areas where the majority of plaintiff companies operate include: electricity supply (5 cases, 19%), mining (3 cases, 12%) and five other sectors (one case each, 19%).

In the 26 arbitration proceedings, 6 BITs signed by Ecuador have been invoked. The treaty signed with the United States is the most used (16 occasions), followed by the BIT with Canada on four occasions, as indicated in the table below:

Arbitration proceedings that have invoked BITs signed by Ecuador

BITs invoked by investors (6)	Number of cases in which a BIT was invoked
United States-Ecuador BIT	16
Canada-Ecuador BIT	4
Spain- Ecuador BIT	3
France-Ecuador BIT	1
Bolivia-Ecuador BIT	1
Argentina-Ecuador BIT	1

Source: PGE.

Elaboration: CAITISA.

As can be concluded, of the 26 cases, only two cases were filed by investors from Latin American countries (Bolivia and Argentina); the investors in the other 24 cases correspond to countries owning large amounts of capital. Some investors have sued Ecuador repeatedly: Murphy Exploration and Production Company International (3 times for the same dispute), Chevron (3 times, for different reasons) and Occidental –Oxy– (2 times).

At present, 16 cases have come to an end, while 10 cases remain open in different stages of arbitration or collection proceedings. In 14 cases, some type of payment or financial compensation, payable by the Ecuadorian state, has been awarded; in 8 cases by virtue of a condemnatory award; in 6 cases as a result of an agreement between the parties. It was only in five cases that the tribunal ruled that the state had not violated the BIT or declined to admit jurisdiction to hear the case.

	Investor Plaintiff	Investment Sector	Amount Demanded by the Investor	State of the Conflict	Amount Paid by the State	
O P E N C A S E S	Chevron (III)	Hydrocarbons	\$9,500,000,000	The Court has yet to rule.	N/A	
	Merck Sharpe & Dohme	Sale of a Pharmaceutical Plant	\$41,966,571		N/A	
	RSM Production Corporation,	Mining	To be determined according to PGE		N/A	
	Zamora Gold	Mining	To be determined according to PGE		N/A	
	Perenco	Hydrocarbons	\$1,572,000,000		N/A	
	GLP	Hydrocarbons	\$50,000,000		N/A	
	Albacora	Fishing Company	\$25,000,000			
	Burlington	Hydrocarbons	\$1,515,000,000	The tribunal ruled in favor of the investor. Ecuador has requested annulment or is in the stage of quantifying damages	N/A	
	Murphy (III)	Hydrocarbons	\$636,000,000		N/A	
	Copper Mesa	Mining	\$69,700,000		N/A	
C L O S E D C A S E S	Ecuador FTA/Petrobras Argentina (PESA)	Hydrocarbons	An agreement was reached before establishing the amount	Agreement between the parties. There was no award	An agreement could not be reached	
	GLOBALNET – Únete Telecomunicaciones	Telecommunications	\$32,500,000		No values are detailed in the agreement	
	IBM	IT Services	\$4,680,508		\$3,500,000	
	Noble Energy and Machala	Electricity Supply	\$371,000,000		\$56,000,000	
	Quiport Corporation	Airport	An agreement was reached before establishing the amount		No values are detailed in the agreement	
	Técnicas Reunidas	Oil Refinery	\$120,000,000		An agreement could not be reached	
	Empresa Eléctrica del Ecuador (Emelec)	Electricity Supply	\$1,700,000,000	Ruling in favor of the State	N/A	
	Encana	Hydrocarbons	\$80,000,000		N/A	
	M.C.I. Power Group	Electricity Supply	\$75,000,000		N/A	
	Ulysseas	Electricity Supply	\$56,100,000		N/A	
	Murphy Exploration (I)	Hydrocarbons	\$185,400,000 ²⁰		Jurisdiction award in favor of the State	N/A
	Duke Energy	Electricity Supply	\$25,000,000		Ruling in favor of the investor	\$10,776,178
	Occidental (Oxy) I	Hydrocarbons	\$375,000,000			\$100,000,000
	Chevron (II)	Hydrocarbons	\$1,605,000,000			\$112,839,791
	Oxy (II)	Hydrocarbons	\$3,370,000,000			\$1,061,000,000
Murphy Exploration (II)	Hydrocarbons	\$185,400,000 ²¹	Investor withdrew demand	N/A		

Source: PGE. Elaboration: CAITISA.

Apart from the cases against Ecuador submitted to arbitration tribunals, at least 29 BIT-based dispute notifications were filed, of which 13 are active and 16 have been closed.

Such claims may fail if the parties reach an agreement before the conflict escalates. This leads to the presumption that the mere threat of a lawsuit may be sufficient for the state to grant monetary compensation or make changes in its policy (the chilling effect) to satisfy the investor and avoid the arbitration process.

	BIT	Investor
13	UNITED STATES (4)	Carlos Nicolas Perez Lapentti
		N. Perez Holdings LLC
		N. Pérez investments, LLC
		Pfizer Ireland Pharmaceuticals
	ARGENTINA (1)	Petrobras Argentinat S.A. (PESA)
	VENEZUELA (1)	Suelopetrol
	SPAIN (3)	Solarig
		Promocaledonian
		Cirsa International Gaming Corporation
	CANADA (1)	Doug W. Cannaday
	PERU (1)	Internexa Peru
	NETHERLANDS (1)	Antillean Finance Company
	ITALY (1)	Casinos Boulevard

NOTIFICATION OF EXISTENCE OF WITHDRAWN DISPUTES			
	BIT	Investor	Result
16	SPAIN (10)	Pontia Asset Management I	Amicable Solution Reached
		Pontia Asset Management II	Amicable Solution Reached
		TEC Group Advanced Services I	Amicable Solution Reached
		TEC Group Advanced Services II	Amicable Solution Reached
		GESPATCO S.L. I	Amicable Solution Reached
		GESPATCO S.L. II	Amicable Solution Reached
		Ecuador Energético S.A. I	Amicable Solution Reached
		Ecuador Energético S.A. II	Amicable Solution Reached
		Ausabi LLC I	Amicable Solution Reached
		Ausabi LLC II	Amicable Solution Reached
	ARGENTINA (1)	CGC	Amicable Solution Reached
	UNITED STATES (1)	Noble Energy & EDC	Amicable Solution Reached
	CHINA (2)	China Oil Corp	Amicable Solution Reached
		Petroriental	Amicable Solution Reached
	NETHERLANDS (1)	Schlumberger	Amicable Solution Reached
	GREAT BRITAIN (1)	Development Delivery International Limited	Amicable Solution Reached

Elaboration: PGE

Jurisdiction and merits standards invoked by investors to file suit against Ecuador

International conventions regulating dispute procedures between private investors and states stipulate that certain requirements must be met in order for an arbitral tribunal to hear the content of alleged violations of international law. This means that the arbitral tribunal must first decide whether it has jurisdiction to intervene in the dispute on the basis of “jurisdictional requirements”.²² On the other hand, violations of international law are judged on the basis of what is known as “standards of merit.” In this stage, state infringements of company investments under the BIT clauses are analyzed.

An analysis of 24 cases against Ecuador²³ shows that, in most of these cases, the arbitrators interpreted the applicable rules in a broad fashion. This resulted in decisions favorable to the investors, both in the jurisdiction stage and in the resolution of the claim's merits.

Jurisdiction Stage

Ordinary courts, at the national and international level, also decide on their own jurisdiction. The same applies to arbitral tribunals in commercial arbitration—a practice that is the source of most international investment arbitration rules—under the famous *Kompetenz-Kompetenz* principle: the tribunal is vested with the power to determine its jurisdiction. However, what is particular to commercial or investment arbitration, in comparison to all other judicial dispute resolution systems, is that the

economic compensation to go to the arbitrators is in the hands of the arbitrators themselves. In other words, if the arbitrators, who are always appointed on an ad-hoc, case-by-case basis, decide that they have no jurisdiction to resolve the dispute brought before them, their fees may be dramatically reduced. On the other hand, if they decide that they do have jurisdiction and see the dispute through to the end, their fees may reach the maximum amount they could be entitled to.

This does not occur in an ordinary judicial system, where the content of the decision (rejection or acceptance of jurisdiction, rejection or acceptance of the merits, determination of the amount of damages, etc.) has no impact on the judges' remuneration, which is a fixed amount. The current international investment arbitration system has a very clear economic incentive for arbitrators to accept jurisdiction, and discourages refusal. This is one of the reasons, though not the only one, for the adoption of very broad jurisdiction criteria by many arbitral tribunals; criteria that are questionable from a legal point of view.

The Ecuadorian State has argued, in all cases, that the tribunal does not have jurisdiction to resolve the dispute. The reasons given are specified in the following table:

Reasons invoked by the state to claim that the tribunal lacks jurisdiction	How many times?
Lack of consent to arbitration proceedings	15
Non-existence of Protected Investment	8
Investor's Nationality not Protected under the Invoked BIT	7
Fork in the Road	6
Concept of Investor	6
Material Incompetence: exclusion of tax matters	6
Non-retroactivity of the BIT	3

Elaboration: CAITISA.

Despite the strong grounds employed by the Ecuadorian State to allege that the individual tribunals lack jurisdiction in the cases against Ecuador, we find that in 13 disputes the tribunal accepted jurisdiction (using, to a large extent, broad interpretations of the rules) to decide the case; while there were only two cases in which the Tribunal did not accept jurisdiction. In the remaining 9 cases, the tribunal did not rule on jurisdiction for different reasons: the case is still open without a ruling on jurisdiction, there was an agreement of the parties, or the investor withdrew the claim before the decision on jurisdiction. The other two recently initiated cases are in the process of forming arbitration panels.

The cases against the Republic of Ecuador clearly exemplify the tendency of most arbitral tribunals to interpret jurisdiction requirements broadly (rather than restrictively) when deciding on their own jurisdiction.

Below is an analysis of selected cases in regards to the jurisdictional requirements presented by Ecuador:

The Temporal Validity of the Invoked BIT

One of the jurisdictional requirements is tied to the term of the BIT being invoked. The most prominent precedent for cases against Ecuador is the Chevron II case. The challenge referred to whether the BIT could be applicable to facts and acts prior to its entry into force.

Ecuador argued that the tribunal lacked jurisdiction to adjudicate the legitimacy of events of this type, which took place before the BIT entered into force.

This position was supported by Article 28 of the Vienna Convention on the Law of Treaties, which establishes: “Non-retro-activity of treaties. Unless a different intention appears from the treaty or is otherwise established, its provisions do not bind a party in relation to any act or fact which took place or any situation which ceased to exist before the date of the entry into force of the treaty with respect to that party.” Likewise, in Article 13 of the International Law Commission's Draft, according to which “an act of a State does not constitute a breach of an international obligation unless the State is bound by the obligation in question at the time the act occurs.”

For its part, Chevron argued that it was wrong to interpret the non-retroactivity principle as requiring that a claim be based only on acts and omissions subsequent to the BIT's entry into force. In its own words: “The principle according by which a treaty does not apply to acts prior to its entry into force does not mean that it may not apply to events subsequent to its entry into force, but relating to

investments prior to that date.”

Chevron also emphasized that the principle of non-retroactivity “is not infringed on by the application of the treaty to continuing violations and composite breaches that took place during the treaty's term, even if such acts began before its entry into force”. These two concepts are significant developments that have become references when considering the issue of retroactive BIT application: the continuous and composite nature of the state behaviors in dispute.

The tribunal assumed that the standards of conduct prescribed by the BIT were not in force prior to its date of entry into force and agreed with the Mondev precedent that “[t]he mere fact that prior conduct has not been remedied or redressed when a treaty enters into force” does not justify a tribunal applying the treaty retrospectively to that conduct. However, it agreed with Chevron that this did not mean that a violation had to be based only on acts taking place after the BIT had entered into force. The Tribunal understood that “the meaning attributed to post-entry into force acts or facts may be supplemented by pre-BIT acts or facts; this conduct may be considered for purposes of determining whether a breach of the BIT standards occurred after the date of entry into force.”

Fork in the Road

With respect to the jurisdictional requirement, included in numerous BITs, related to the claimant investor's inability to opt for all the jurisdictions provided for in the BIT to settle its claims, known as “fork in the road”; the most pertinent case is that of Occidental Petroleum (Oxy I).

Ecuador objected that the “fork in the road” provision, included in Article VI(2) and (3) of the U.S.-Ecuador BIT, precluded jurisdiction for Occidental in the case. By filing separate lawsuits before the Ecuadorian courts, Occidental made use of its irrevocable election to submit the dispute to the defendant's courts or administrative tribunals in accordance with Article VI(2)(a) of the Treaty. This choice precluded, in and of itself, the submission of the dispute to arbitration under the terms of Article VI (3) (a) of the Treaty.

Occidental filed two lawsuits before District Tax Court No. 1 in Quito. It then filed other lawsuits on March 10, 2003 and April 14, 2003, in connection with the issuance of IRS Resolutions 406 and 026, which again rejected other VAT reimbursement claims filed by Occidental. The claims argued that the IRS Refusal Resolutions violated the provisions of Ecuadorian law, with specific reference to Articles 65 and 69A of the Ecuadorian Tax Law, and on which the international arbitration claim would also be based.

This prevented Occidental from submitting the same dispute to arbitration. To make this argument, the Ecuadorian defense correctly emphasized that there is objective similarity between the litigation in question: they all involve the same disallowance resolutions and therefore the same refusal to refund tax contributions. The fundamental dispute is the same in both national and international forums. Based on the choice made, the Ecuadorian government deemed Occidental to have waived its right to proceed to international arbitration.

Occidental, on the other hand, argued the opposite. In its view, the claim brought before Ecuador's domestic courts was not related, in any substantive sense, to the investment; indeed, it had made no assertion or claim in those courts regarding its rights under the BIT. Occidental thus contended that its ongoing litigation before the Ecuadorian courts was brought solely to safeguard its rights to a tax refund under Ecuadorian law. If we look at the terms under which an investment dispute is defined under Article VI (1) of the BIT, we see that it is linked to the investor's rights under the Treaty. It lacks any connection with the claims pending before the Ecuadorian courts, which exclusively involve the consistency of refusal rulings with Ecuadorian tax law. This is Occidental's point.

Contrary to Ecuador's contention, Occidental asserts that there is no objective similarity between the disputes pursued through the two channels: the "cause of action" submitted to arbitration is different from the cause of action asserted before the Ecuadorian courts. The first relates to BIT rights; the second to questions of domestic law.

The Tribunal agreed with Occidental regarding the best interpretation of Article II(3)(b) of the Treaty. The second sentence of this article allows for referral to arbitration of unfair or discriminatory measures even if the claimant has resorted to the defendant's courts or administrative tribunals to seek review of such measures. This is a decisive normative point for the case (revealing the seriousness of including such a clause in a BIT).

Interestingly, the Tribunal took care to clarify that this understanding could not be interpreted as rendering meaningless the "fork in the road" provisions that might be contained in a bilateral investment treaty: the roles of domestic mechanisms and international arbitration are different. To uphold this, the Tribunal then unpacked what it called "the triple Identity test", whereby insofar as a dispute could involve the same parties, the same subject matter and the same cause of action, it could be considered the same dispute and the "fork in the road" mechanism would preclude its submission to concurrent tribunals.

The Tribunal found that the crucial point, ultimately, was

that any solution should respond to the specific circumstances and nature of the dispute, to the extent that the nature of the dispute submitted to arbitration was primarily—although not exclusively—treaty-based; the jurisdiction of the arbitral tribunal was thus properly invoked.

For the Tribunal that was precisely the case in Oxy I: treaty-based issues were submitted to arbitration in the local Ecuadorian courts, issues related to domestic, non-contractual law. Here, the Tribunal implemented the doctrine of cumulative effect, or the doctrine of complementarity in terms of the procedural avenues available to the investor. In its own words: "Far from creating a situation of incompatibility, the decisions adopted to date by the Ecuadorian courts on questions of interpretation of the Ecuadorian Tax Law have been of great assistance to this Tribunal in its own interpretation, both of the treaty and of the relevant provisions of the Ecuadorian laws, as will be further demonstrated below. It follows that the causes of action could be separate and the nature of the disputes different, but they could have cumulative effects, as well as interacting with each other."

Exclusion by Subject Matter (taxation)

Regarding the jurisdictional provision contained in numerous BITs related to the exclusion of certain matters (particularly tax matters, in whole or in part) from ICSID jurisdiction, the Oxy I case is likewise pivotal.

As a jurisdictional objection, Ecuador raised exclusion in the dispute of taxation issues under Article X of the U.S.-Ecuador BIT.

In order to understand the case, it is essential that we refer to the text of the aforementioned Article, which we transcribe below:

“1. Regarding its tax policies, each party should strive to accord fairness and equity in the handling of investments made by the other party's nationals and companies.

2. However, the provisions of this treaty, in particular Articles VI and VII, shall apply to matters of taxation only in respect to the following:

(a) expropriation, in accordance with Article III;

(b) transfers, in accordance with Article IV; or,

(c) enforcement and oversight of compliance with the terms of an investment agreement or authorization as referred to in Article VI(1)(a) or (b), insofar as they are not subject to the dispute resolution provisions of a treaty for the avoidance of double taxation between the two parties, or are brought in accordance with said

dispute resolution provisions and are not settled within a reasonable period of time.”

According to Ecuador, matters related to Value Added Tax (VAT) and the non-refund of VAT were clearly “matters of taxation”, which were excluded from dispute resolution under the treaty by the aforementioned article. Indeed, none of Occidental's Fair and Equitable Treatment or Full Protection and Security claims could be applied to taxation issues.

Occidental contradicted Ecuador on this point. From its perspective, this was not the best interpretation of BIT article X. The true meaning of the exclusion provided for in this article, and the history of the negotiations behind its drafting, would indicate that the exclusion applied only to direct taxation issues, since these are the issues addressed by the treaties in order to avoid the double taxation problem. According to Occidental, there was never any double taxation treaty between the United States and Ecuador. Indirect taxation would therefore be subject to the treaty's dispute settlement provisions, with no exceptions whatsoever. For Occidental, this was the proper interpretation of Article X, in accordance with the rules of interpretation of Articles 31 and 32 of the Vienna Convention on the Law of Treaties.

We should also note that Occidental based its interpretation on the fact that the article in question was drafted based on the U.S. Model Bilateral Investment Treaty, and that the interpretation given by U.S. officials, as well as their statements, ought to be decisive in construing its meaning. From this perspective, the sole purpose of the Article was to avoid conflicts with dispute resolution bodies in compliance with double taxation conventions; if all types of taxation were included in the exception to the Article, it would be rendered meaningless.

The Tribunal rejected Ecuador's interpretation that all taxation matters were exempt from dispute settlement as provided for in the Treaty, with the exception of the specific categories mentioned in Article X. According to the Tribunal, “even if certain issues could still be covered by this article and consequently not render it meaningless, as argued by the defendant, such interpretation would nevertheless restrict it to a fairly marginal application. This is clearly not what the parties intended by putting an Article of such importance in such a relatively short Treaty.”

The Tribunal proceeded to examine whether the dispute involved any of the three issues specifically listed in Article X, whereby the dispute settlement provisions of Article XI would be affirmatively applied. If it indeed involved any of the above elements, the dispute would in any case fall under the provisions of the treaty and dispute resolution. The question of transfers obviously did not

arise in the case, and the question of expropriation was analyzed separately. On the other hand, the determining issue was “whether the enforcement and monitoring of compliance with the terms of an investment agreement, concerning taxation issues, is at issue in this dispute.”

The Tribunal concluded that it had been presented with a tax issue related to an investment agreement. The dispute was therefore clearly subject to the treaty's dispute resolution provisions. This automatically includes Article II treatment standards, as well as fair and equitable treatment, unlike the exclusion sought by Ecuador. Article X(1) thus acquired its full significance in the Tribunal's view, and the Tribunal therefore upheld its jurisdiction and overruled Ecuador's objection.

This case demonstrates how including specific exceptions does not ensure that regulatory space will be safeguarded in these matters: investors can still file claims, and, using a broad interpretation of the rules, arbitrators may accept jurisdiction to settle the dispute.

Non-existence of Foreign Investor (investor nationality)

As for the jurisdiction requirement which is tied to the existence of a foreign investor to claim the protection of a BIT, in our view, Noble Energy is a particularly noteworthy case.

In this case, Ecuador argued that Noble Energy could not bring a claim under the BIT, since it did not make the investment itself, but was merely pursuing claims on behalf of its co-plaintiff, Machala Power.

Ecuador emphasized that Noble Energy was not the direct owner of Machala Power and invoked the decision taken by the International Court of Justice, in the famous Barcelona Traction precedent, as well as the Amco precedent, on the nationality of the plaintiff investor.

In a very important point of its argument, Ecuador contended that Noble Energy had too distant a relationship with Machala Power to qualify as an investor in its own right. The problem raised by this objection is extremely complex: the connection that must exist between the (indirect) shareholder and their (indirect) investment. To buttress its point, Ecuador cited a passage from the Enron decision: “it is indeed necessary to establish a limit beyond which it would no longer be permissible to file lawsuits on the grounds that they have only a distant connection with the affected company.”

For its part, Noble Energy argued that it, based on an independent cause of action, was not invoking Machala Power's rights, but rather its own. Noble Energy objected to the relevance of the precedents invoked by Ecuador for the case (Barcelona Traction and Amco), suggesting instead that the applicable precedent was CMS v.

Argentina, where the issue was analyzed in the context of the Argentina-United States BIT. This BIT in terms very similar to those of the BIT applicable to the Ecuadorian case, which read that no “[...] obstacle could be found in international law to the idea of allowing shareholder claims independently of the relevant company,” adding that this assertion did not lose validity “even [when] said shareholders [are] minority or non-controlling shareholders.”

The Tribunal agreed with Noble Energy: an indirect shareholder may pursue a claim under the ICSID Convention and a BIT in regards to a direct investment. In its own words: “in the absence of a provision to the contrary, the BIT and the ICSID Convention admit claims for damages brought by indirect shareholders.” It thus established a presumption supporting the possibility of an indirect investment claim.

The decision's central point was how close or how distant the relationship between the investors could be, according to the Tribunal, in order to allow for their respective autonomous claims: “how indirect can a shareholder be while still qualifying as an investor for treaty purposes? Is there a limit? If so, was it reached in this case? In other words, how many layers or companies can stand between the direct shareholders and the indirect investor?”

Machala Power was wholly and directly owned by Noble Energy International Ltd. (registered in the Cayman Islands), wholly and directly owned by Samedan of North Africa, Inc. (registered in Delaware), which in turn was wholly and directly owned by Noble Energy. This meant that there were two layers between Machala Power and Noble Energy. The Court referred to the famous passage of the Enron precedent, where it was stated that a cut-off point must exist in the chain of companies. Given the facts presented, the tribunal found that said degree had not been reached. Argentina had specifically invited the shareholders to invest and the investors had decision-making power in the management of the local company.

The Noble Energy Tribunal did not disagree with the Enron court's statement. In a crucial passage, it stated that: “there may well be a cut-off point somewhere, and future courts may be called upon to define it. In this case, there is no need for such a definition. In fact, whatever the cut-off point may be, it has not been reached, due to the fact that there are two intermediate layers. The relationship between the investment and the direct shareholder, on the one hand, and the indirect shareholder, on the other, is not that distant. [...] The Tribunal notes that, for all relevant periods, Noble Energy has been the ultimate parent company of all of subsidiary companies involved in the arbitration, and that these subsidiaries are wholly owned, directly or indirectly, by

Noble Energy.” Ecuador's jurisdictional objection was thus dismissed.

Stage of Merit

The BITs signed by the Republic of Ecuador contain the usual investor protection standards for this type of instruments. They thus protect investors against unlawful expropriation of assets, against unfair and inequitable treatment by the state, against lack of full protection and security, and against arbitrary or discriminatory treatment. Also, like the rest of the known BITs, the obligations established in these instruments are unidirectional, i.e., states-to-investor; no obligations are stipulated in the investor-to-state direction.

Another aspect generally characteristic of BITs (which is repeated in BITs signed by the Republic of Ecuador), is their brief wording; the aforementioned standards are defined in a few words and in general terms. It is quite difficult to know in advance what these standards imply in concrete terms for the parties. This has therefore given arbitral tribunals a considerable amount of room to establish broad interpretations, leading to the numerous multimillion-dollar awards that now hang over Ecuador.

In the six cases in which the Tribunal has ruled in favor of the investor,²⁴ according to the Tribunals, the clauses infringed on by the Ecuadorian State were the following:

- Fair and Equitable Treatment: Oxy I, Duke Energy, Oxy II and Perenco.
- Direct/Indirect Expropriation: Oxy II, Burlington and Perenco.
- Denial of Justice: Chevron III.
- Umbrella Clause: Duke Energy.
- Non-discriminatory or arbitrary treatment: Oxy I.
- Full Protection and Security: Oxy I.
- National Treatment: Oxy I.

Fair and equitable treatment

This standard has been applied in a significant number of cases and is considered one of the most ambiguous and imprecise. It is thus almost always possible to argue its violation and obtain a favorable result for investors. In this regard, UNCTAD stated that this has become “the most widely and successfully-used basis for investor claims under International Investment Agreements.” UNCTAD also noted that the arbitrators interpreted the fair and equitable treatment concept quite broadly, and concluded that this can result in an undefined and unbalanced approach that unduly favors the investor's interests, while ignoring legitimate regulation in the public interest.”²⁵

Perhaps the most relevant example of the fair and equitable treatment standard in ICSID jurisprudence can be found in OXY II, one of the cases faced by the Republic of Ecuador.

In May 2006, Ecuador declared the expiration of an agreement with US oil company Occidental, after the latter transferred the rights to 40% of its shares to Encana Corporation (Canadian), without the permission of the Ministry of Energy, and in violation of Ecuadorian law.

Oxy argued that the expiration proceedings implemented by the Ecuadorian State in regard to existing contracts violated Ecuador's legal, constitutional and administrative principles, including the principles of proportionality, equality, good faith, and legitimate aspirations. The company argued that this action constitutes, among others, a flagrant violation of Ecuador's obligations on fair and equitable treatment as determined in Article II of the Reciprocal Investment Protection Treaty between the Republic of Ecuador and the United States of America.

The Tribunal found in favor of the investor and the award was the largest damage award in ICSID history: USD \$1,769.6 million, plus interest. The sentence was based on a violation of the standards of “fair and equitable treatment” and lawful expropriation under the U.S.-Ecuador BIT.

Ultimately, without further refinement of its legal approach, the Tribunal found that the termination of the contract had been a clearly “disproportionate” response by Ecuador to Oxy's prior breach of contract. The principle of proportionality was considered by the Tribunal to be part of the “fair and equitable treatment” standard under the BIT. This was therefore the source of the legal liability on which Ecuador was sentenced.

Another very striking example of the operation of the fair and equitable treatment standard is the case brought by Perenco, a French company whose main activity is the exploitation and refining of oil in blocks 7 and 21 in the Amazon region.

Starting in 2006, the Ecuadorian State introduced reforms to the Hydrocarbons Law (Law No. 2006-42) as a result of the increase in international oil barrel prices, stipulating that the surplus on the oil price would be shared in the state's favor (Art. 44) at 50% and, later, at 99% (Decree 662).

In Perenco's view, these measures violated the fundamental terms of the participation contracts signed between Perenco and the state, since its legitimate expectations were denied and its investments were discriminated against and expropriated without compensation.

The case was conducted under the fair and equitable treatment standard in terms of international investment law. The Tribunal found that the 50% state appropriation of the extraordinary oil revenue established in Law 42 did not in itself imply a violation of the fair and equitable treatment standard. The Tribunal found that the standard of fair and equitable treatment was self-contained within the treaty, and not equivalent to the minimum standard of treatment under general international law. According to the Tribunal, application of the fair and equitable treatment standard required a balanced consideration between the investor's reasonable expectations and the state's regulatory powers. Here, the Tribunal found that a company experienced in the oil extraction and sales business, like Perenco, would be unable to anticipate the state's revision of its legal framework for the regulation of its natural resources. The Tribunal placed importance on the fact that Ecuador was not the only state to revise its natural resources legislation in terms similar to those of Law 42 during the period in question.

However, the change—through Decree 662—of the regulation to scale up to 99% of the extraordinary income, did constitute a violation of fair and equitable treatment.

As can be seen, the violations of fair and equitable treatment ultimately depended on the increase of the Ecuadorian State's rights over the extraordinary oil revenues from 50% to 99%, and on the details of that escalation.

Inconsistency in awards

Five cases against Ecuador have arisen as a result of the Hydrocarbons Law 42. In three of the five, the Tribunal has issued an award ruling on the violation of fair and equitable treatment standards. It is worth noting that, while the circumstances are nearly identical in all cases and the grounds for the claim are the same, the arbitrators' decisions have been different.

In the Perenco case, the Tribunal found that there was a violation of the investor's fair and equitable treatment when the state increased the treasury's to the treasury on oil revenues up to 99%. In the Occidental case, however, the Tribunal found that the breach had occurred when the state increased windfall profits received from the participation contracts to 50%. On the other hand, the Tribunal in the Burlington case—analyzed below—found that neither the 50% increase, nor the 99% increase, constituted a violation of the fair and equitable treatment standard.

Protection against direct and indirect expropriation

The protection against unlawful expropriation afforded by BITs to investors cannot involve removal of a state's

power to expropriate property in its territory (which is a sovereign right); rather, it is a regulation of the form in which this expropriation should take place. Under the protection of most BITs, expropriation must be carried out in furtherance of a public purpose, in a non-arbitrary and non-discriminatory manner that guarantees due process and lacks prompt financial compensation.

Arbitral tribunals have admitted the possibility of applying the standard of protection against unlawful expropriation in cases in which States have not openly ordered an expropriation, but have—in the opinion of the respective tribunal—adopted an administrative measure equivalent to expropriation based on its effects, in the sense of severely limiting the possibility of the investor to exercise property rights over its assets in the country. This is referred to as “indirect expropriation.”

An example of how tribunals have applied the indirect expropriation standard in cases against the Republic of Ecuador can be found in the Burlington case.

Burlington (a U.S. company) and its wholly-owned subsidiaries are primarily engaged in oil exploitation and refining. In 2009, Burlington suspended its operations in Blocks 7 and 21, and three days later Ecuador took over the exploitation of both blocks. For the company, Hydrocarbons Law 42-2006 and Decree No. 662 constituted, among other violations, an expropriation of its investments.

Taking into account ICSID rules, on December 14, 2012, the Tribunal determined that Ecuador expropriated Burlington's assets in Blocks 7 and 21. This decision on expropriation was based on the government's physical takeover of two of Burlington's oil fields. As regards the indirect expropriation claim, the majority of the tribunal considered that the recovery rate on the extraordinary oil revenue imposed by Law 42 (and its escalation as imposed by Decree 662) did not constitute expropriation, despite the fact that it reached a staggering 99%. The investment remained profitable, even if profits were limited, something that can never be equivalent to expropriation. This physical seizure of the investment (in the Tribunal's terms, “of the means of production itself”) was considered an expropriation, as opposed to measures that merely limited the investor's profit, because it entailed a complete deprivation of the investor's ability to earn any return on their investment. Insofar as this expropriation was not compensated, the Tribunal found that it was unlawful under the BIT.

Arbitrator Orrego Vicuña disagreed with the majority decision, finding that Ecuador should have been condemned for further violations of international law, as international law required that Ecuador's tax measures be considered as part of the illegitimate expropriation. The

most significant difference resided in Orrego Vicuña's assertion that not only should physical expropriation be considered expropriatory, but also the tax measures imposed by Law 42 and Decree 662.

Denial of Justice

Denial of justice includes the inability to exercise the right of access to justice for conflict resolution, either due to non-compliance with due process, or due to an unnecessary delay that results in the plaintiff giving up hope on reaching an effective resolution of the case.

In the lawsuits against Ecuador, three investor companies have alleged that they have been denied justice: Duke Energy, Chevron II and Merck Sharpe & Dohme.

In the Duke Energy case, the plaintiffs accuse Ecuador of denial of justice by failing to submit their claims to local arbitration proceedings and failing to process their tax claims in a timely manner. They argue that Ecuador has failed to establish effective means to enforce the claims and respect the plaintiffs' investment rights, in violation of Article II (7) of the BIT, which amounts to a denial of justice. However, in this case, the Tribunal decided that Ecuador “has not failed to comply with Article II (7) of the Treaty”.

Meanwhile, the investor Merck Sharpe & Dohme has sued the government of Ecuador, arguing that local Ecuadorian courts have ruled unfairly in a private dispute between Merck and another local company (Nueva IndustriaFarmacéuticaAsociada). The local generic drug company, NIFA, sued Merck in the national courts after Merck failed to fulfill a commitment to sell a drug production plant based in Ecuador. Merck argued that the damages awarded by the local courts against it are unreasonable. Not only did it ask the international tribunal that Ecuador indemnify and hold the company harmless against any loss caused by execution of the ruling against it, but it requested that the government prevent the execution of a judicial decision reached during a private litigation, while the case was still being evaluated by the National Court of Justice of Ecuador. The arbitral tribunal has not yet rendered an award, but the mere existence of the claim reflects how investors can take advantage of BITs to try to curtail the power of domestic courts, and influence or modify their decisions.

The best-known case of denial of justice in international arbitration is the lawsuit filed by Chevron against Ecuador. In the early nineties, TexPet (now Chevron) filed seven lawsuits against the Ecuadorian State; a decade later, in light of the lack of any response from the Ecuadorian courts, it resorted to international arbitration. Chevron alleged that Ecuador obstructed its access to the administration of justice and breached the BIT with the

United States. Ultimately, the arbitration tribunal ruled in favor of Chevron. In reaching this conclusion, it interpreted the standard expansively, indicating that investor law, included in the BIT, constitutes *lex specialis*, which is distinct from customary international law in relation to the denial of justice. For this reason, the high threshold for establishing denial of justice, as determined in customary international law, may be far less demanding.

Non-discriminatory or arbitrary treatment

This standard establishes that investors, both domestic and foreign, should be afforded a level playing field as regards the management, operation, expansion and transfer of their investments. Therefore, they cannot be subject to arbitrary or discriminatory measures. This ensures equality in the application of regulations and that the state does not legislate to the detriment of the rights of certain investors only.

Foreign investors have argued the violation of the non-discriminatory or arbitrary treatment standard in 14 of the 24 cases. The Oxy I case is an example in which the investor disagrees with the Internal Revenue Service's decision to deny VAT refunds due to tax reforms in Ecuador, which it considers arbitrary and discriminatory. The company argued that the measures are discriminatory, since they only apply to the industry's oil exploration and production companies and not systematically to other Ecuadorian exporters.

However, the tax refund law was designed only for exporters of manufactured goods; it was never intended to apply to the hydrocarbons sector. Ecuador argued that the measures were not discriminatory, because they were applied equally to all foreign or domestic oil companies.

In the end, the Tribunal ruled in favor of Oxy I, accusing the Ecuadorian Government of having acted, in part, in a discriminatory manner.

Full Protection and Security

Today, the concept extends beyond physical protection to include protection against violations of investor rights through host state laws and regulations. At the moment, there is consensus that the clause does not offer absolute protection against physical or legal affectations, and therefore the State is not responsible for preventing such violations; however, the Ecuadorian State has been sued for violations of this clause when it has tried to recover its essential attributes or when balancing profits in the hydrocarbons sector.

National Treatment

The national treatment clause obliges the state hosting the investment not to discriminate between domestic and

foreign investors when creating and applying its regulations and, therefore, to equalize the position of the foreign investor to that offered to the domestic investor. One criticism of this clause is that the national investor does not receive the same benefits and protection as the foreign investor, nor the possibility of resorting to international arbitration mechanisms, which is discriminatory to the Ecuadorian investor. In eight cases, investors have argued that the state treated them differently than its own nationals: Oxy, Encana, Perenco, Murphy, GLOBALNET-ÚneteTelecomunicaciones and Copper Mesa.

In the cases of Oxy I and II and Encana, the argument is similar. The companies argued that the denial of value added tax (VAT) refunds did not apply to investors in the area of goods production for export. However, the Government made it clear that Encana and Oxy were not treated less favorably than all investors, i.e. oil companies in the same position, whether Ecuadorian or foreign. We should note that investors in other non-oil industries are in different circumstances, and therefore, it is not possible to claim discrimination based on the Investor's nationality.

In the cases of Perenco and Murphy, the basis of the argument is that Law 42 created a disproportionate benefit for nationals in comparison to foreign investments in the oil production sector, since there is almost no Ecuadorian investment in said sector. Perenco, for example, alleges that by deliberately causing harm to non-Ecuadorian companies, including Perenco, Ecuador has given more favorable treatment to investments by domestic companies. However, Perenco has failed to demonstrate that in the enactment or application of Law 42, Ecuador intended to "favor domestic investors by discriminating against foreign investors". As Perenco itself admits, Law 42 was applied equally to all participants in the sector, regardless of their nationality, and thus clearly did not have the effect of discriminating against companies on the basis of nationality. To say that Law 42 is discriminatory because in a sector dominated by foreign entities the law numerically affected non-nationals more than nationals makes no sense.

Finally, two other cases where the violation of the national treatment clause was invoked are GLOBALNET-ÚneteTelecomunicaciones and Copper Mesa. In the first case, the company argued that the delay in assigning the interconnection provisions meant that, while the plaintiff company was prevented from operating and exploiting its concession, the other state and private operators in Ecuador were in possession of the aforementioned interconnections and were in a position to provide their services.

For its part, Copper Mesa claimed that the state had

granted more favorable treatment to the state mining company ENAMI by granting it a right of first refusal on mining projects. The state responded that such preference to the state-owned mining company is a legitimate public policy right and not a nationality-based discrimination, as no private Ecuadorian investor enjoys the same privilege.

Situation of the enforcement of arbitration awards in Ecuador

Enforcement of arbitration awards under the ICSID Convention and UNCITRAL rules

Awards rendered by arbitration tribunals are enforceable by investors once they have become final, i.e., when the award is no longer subject to appeal. However, for awards to become final, they must go through the administrative procedures indicated in the arbitral rules governing the Tribunal (those of the ICSID Convention or UNCITRAL) and, if applicable, the procedure established in the domestic legislation of those states where the investor seeks enforcement of arbitral awards.

Currently, the open cases that Ecuador faces are arbitrations before the ICSID and the Permanent Court of Arbitration (PCA), under the UNCITRAL rules. The following is thus an analysis of the enforcement processes of the resulting awards governed by these rules.

Enforcement of awards under the ICSID rules

Pursuant to Articles 53, 54 and 55 of the ICSID Convention, an award is enforceable once it has become final, i.e., the appeals filed against it have been resolved, or the time limit for filing appeals has elapsed without the parties having filed them. Final awards have the same binding force for the sentenced state as a judicial decision rendered in national territory.

On the other hand, an award may be enforced despite being under review or annulment proceedings, provided that its enforcement has not been suspended (a decision that depends on the Annulment Committee or the Tribunal itself, in the case of an appeal for review). In any case, in these cases, the award remains provisional and not definitive. For its part, Article 54 (2) of ICSID stipulates that the enforcement of awards must be carried out through the procedure and administrative agencies or bodies designated for that purpose, in accordance with the state's domestic law.

Enforcement of awards under UNCITRAL rules

The UNCITRAL rules, in Article 34 (2), provide that “the parties commit themselves to comply with the award without delay”, which implies that enforcement should be carried out with minimum difficulty. This could imply bypassing a recognition procedure, as it would mean

delaying the award's enforcement.

However, in investment arbitration cases to which UNCITRAL rules apply, enforcement rules ratified by Ecuador, such as the Convention on the Recognition and Enforcement of Foreign Arbitral Awards of 1958 (New York Convention), and the Inter-American Convention on International Commercial Arbitration of 1975 (Panama Convention), could be used on a subsidiary basis. These instruments establish that awards handed down by arbitral tribunals must be examined to ensure that their content is not contrary to the principles of the state's legal system and that they do not affect the rights of the party against whom the award is to be enforced.

Current situation for the enforcement of foreign awards

Currently, the General Organic Code of Proceedings (COGEP) establishes the jurisdictional competencies and the necessary procedures for the approval and enforcement of judgments, awards and mediation acts issued abroad, which have the characteristics or effects of a ruling according to their legislation of origin.

COGEP establishes the Provincial Court of Justice, through one of its specialized chambers, as the authority empowered to recognize and approve judicial decisions. Likewise, it is established that the judge of first instance of the defendant's place of residence will be responsible for the ruling's enforcement.

In accordance with this regulation, the process of homologation of a foreign judgment or award will be initiated by the requesting party before the specialized chamber of the Provincial Court, which will summon the person against whom enforcement of the judgment is sought so that, within a period of 5 days, the person may present and demonstrate their rejection of said enforcement. If the refusal of execution is found to be duly grounded, the Court will call for a hearing within a maximum period of 20 days, in which it will substantiate and resolve the claims presented by the parties.

In turn, the Court is obliged to resolve the homologation and determine the execution of the foreign judgment or award, within a period of no more than 30 days from the day on which the summons was made.

The COGEP recognizes that the procedure for enforcement of a judgment (and a foreign award with the same quality) is the enforcement procedure; thus, the COGEP, in its article 134, establishes that: “coercion refers to the coercive measures applied by the judges to ensure that their decisions are complied with by those who do not voluntarily comply with them within the established terms”.

The COGEP establishes requirements to be taken into

account by the Provincial Courts for the homologation to be legally valid in the country. Article 104 of the COGEP determines that a foreign award or judgment may be subject to homologation only if:

- a. They possess the necessary external formalities to be considered authentic in the State.
- b. That the judgment has become *res judicata*, in accordance with the laws of the country where it was issued and the necessary attached documentation is duly legalized.
- c. If applicable, they must be translated.
- d. The judgment is accredited with the pertinent procedural documents and certifications, the defendant was legally notified and the proper defense of the parties has been assured.
- e. The request must indicate the place of summons of the natural or juridical person against whom the decision issued abroad is to be applied.

It also establishes that foreign awards or judgments condemning the Ecuadorian State may be recognized by the national jurisdiction, as long as they do not contradict the country's constitutional or legal provisions, and are in accordance with the international agreements in force in Ecuador.

On the other hand, we should mention that the homologation procedure is not intended, in any way, to be a review of the fundamental decisions in foreign judgments or orders, or to create, based on this procedure, a kind of subsequent instance that renders nullifies the decisions rendered by foreign courts or arbitral tribunals. The actions of the Ecuadorian provincial courts are limited to a procedural examination of the judgments or awards, which seeks to identify possible flaws in the due process relating in regards to award issuance and validity, as provided for in Article 103 of the COGEP, which states that: “judgments, arbitration awards and mediation acts issued abroad that have been homologated and that have been handed down in contentious or non-contentious proceedings, will have in Ecuador the force granted to them by the international treaties and conventions in force, without being subject to a review of merits, which is the object of the process in which they were issued.”

The homologation procedure in the COGEP is the cornerstone for enforcement of foreign awards in the country. According to this regulation, any judgment or award that does not comply with the procedure or that violates the requirements for its homologation, is considered invalid in terms of Ecuadorian law and, therefore, unenforceable in Ecuadorian territory.

Landmark cases against Ecuador: deficiencies in the proceedings and rulings of the arbitration courts

CHEVRON II

Texaco Oil Company—currently Chevron Oil Company—began operations in Ecuador in 1964 and concluded them in 1992. Between 1991 and 1993, during the negotiations for the liquidation of the last concession contract, the company filed seven lawsuits in Ecuador's domestic courts to the tune of US\$553 million.

In 2006, the directors of Chevron, the company that took over Texaco in 2001, alleged that since the company had not obtained any judgment in the cases brought by the former company, the Ecuadorian State had systematically denied its right to access to justice. Based on this criterion, Chevron decided to file an international claim before the Permanent Court of Arbitration, under the UNCITRAL rules, based on the BIT signed between Ecuador and the United States. De igual forma, la compañía dedujo que la forma en que define “inversión” en el TBI, era lo suficientemente amplia como para amparar a las inversiones realizadas por Texaco en 1973 y 1977, e incluir las demandas legales y contractuales que podrían nacer de sus operaciones en el futuro.

In response, the Ecuadorian State contested the Tribunal's jurisdiction on the grounds that the BIT invoked entered into force after Texaco's investments in Ecuador. Likewise, the defense argued the action was inadmissible since the causes rejected in the judicial function of Ecuador are subject to Ecuadorian domestic legislation, which provides for the mechanism of recusal against judicial officials who fail to comply with the terms established in a judicial process, provided that the delays are attributable to their inaction.

Faced with both positions, the appellate tribunal decided that Ecuador had breached Article II(7) of the BIT due to undue delay on the part of the Ecuadorian courts in ruling on seven cases brought by Texaco and was thus liable for damages to the plaintiffs.

Particularities of the case:

- Chevron's claim was inadmissible and should have been immediately dismissed, since it sought to have the Tribunal take on the country's internal jurisdictional functions, in violation of national sovereignty.
- The BIT on which the Tribunal's jurisdiction and competence are based was signed well after the time up until which the oil company held investments in the country, which ended in 1992. The Treaty, on the other

hand, entered into force in 1997, five years after Chevron (Texaco) left the country, and therefore the Tribunal did not have *ratione temporis* jurisdiction to hear the case, since the BIT does not contain any retroactivity clause.

- With respect to the time elapsed, many of the judicial proceedings had a clear lack of momentum on the part of Chevron and Chevron had not even initiated complaint or recusal procedures against the judicial officials who, according to Chevron, denied it access to justice.
- In line with the previous point, in failing to exhaust the existing procedures in the national legislation, Chevron could not have claimed to be the victim of a denial of justice, since it was simply a consequence of its own inaction within the judicial system due to lack of procedural interest on the company's part.
- Many of the legal actions initiated by Texaco (now Chevron) had been, for the most part, dismissed at the time of the arbitration decision, and therefore it was not appropriate for the international tribunal to resolve a proceeding that was being heard in the national courts of domestic jurisdiction.
- The arguments put forward by the state's defense were clear and forceful. However, the oil company's legal team made an act of spontaneous creation of jurisprudence by means of which they provided a new interpretation for a legal institution as basic and fundamental as the principle of non-retroactivity of the legal norm.
- A fact that the Commission found during the investigation of this proceeding should be highlighted: in the Partial Award on the Merits of March 30, 2010, the Tribunal quotes verbatim Articles I, II and VI of the BIT, on which the dispute is based; where, when comparing the BIT cited by the Tribunal with the official BIT published on January 11, 2011 in the Official Gazette of Ecuador (Supplement) No. 360, some differences were found in the contents of the text, i.e. that the BIT used by the Tribunal and the official BIT are not the same, which constitutes a serious breach of the proceeding. For example, on page 55 of the Partial Award on Merits, in Article 1(a), cited by the Tribunal, words are added that do not appear in the text published in the Official Gazette.
- Below are the two versions:

Version cited by the Tribunal:	Version published in the Official Register:
Article 1	Article 1
1. For the purposes of this Treaty:	1. To the effects of the present Treaty:
(a) "Investment" means any class of investment in the territory of a Party, held or controlled directly or indirectly by nationals or companies of the other Party, such as, for example, participation contracts, indebtedness, provision of services, and investments; and includes:	(a) "Investment" means any type of investment such as equity, debt, and service and investment contracts, which is made in the territory of a Party and which is directly or indirectly owned or controlled by nationals or companies of the other Party, and includes:
(ii) a company or shareholdings or other interests in a company or interests in the assets thereof;	(ii) The companies or shareholdings or other interests in their assets;
(iii) a claim for monetary compensation or a claim for enforcement with economic value, and associated with an investment.	(iii) The right to money or any transaction that has economic value and is related to an investment.

Elaboration: CAITISA.

These inconsistencies in the texts cannot be overlooked because of the way in which they alter the meaning of the clauses; in the case of Article 1 of the text interpreted by the Tribunal, the definition of investment is drafted in a broader manner than the version in the Ecuadorian Official Gazette, which, in the international legal context and for the particular case, would mean that the State must grant broader investment protections.

The same occurs in subparagraphs (ii) and (iii), in which, due to the way in which they are worded, the meaning is changed by saying that the investment consists of "a company or shareholdings or other interests in a company or interests in the assets thereof" and, "a claim for monetary compensation or a claim for enforcement with economic value, and associated with an investment". We can thus establish that the Tribunal sought to adapt the figure of investment in the Treaty so that it would contain the obligation to protect the investments made by Chevron.

The Tribunal's interpretation was based on the text of the BIT submitted by Chevron, which contained broader definitions. This harmed the Ecuadorian State due to the illegal and malicious way in which it tried to demand the retroactivity of the agreement within the process.

The Tribunal assumed, incredibly and in the most disrespectful and intrusive manner towards the Ecuadorian justice system, that Chevron would not have obtained a positive outcome if it had filed any judicial remedy in the country, and therefore justified its failure to file a claim before the domestic courts to exhaust the existing judicial and administrative remedies. For the Tribunal and Chevron, there was virtually no rule of law in Ecuador.

For Ecuador, attempting to demonstrate a technical-legal thesis in its defense, no matter how clear, correct and lawful it might be, within forums blatantly biased towards the investor, turns into a unending, futile and pitiful exercise of legal barbarism; since, as has been demonstrated, the ad-hoc Tribunal has the constant pretension of declaring itself to be competent and collecting its fees, without prejudice to twisting facts along the way to match them with whimsical interpretations of a norm.

CHEVRON III

On September 23, 2009, Chevron Oil Company filed a new dispute before the Permanent Court of Arbitration against Ecuador. This new arbitration claim was preceded by a single civil lawsuit brought against the company by Amazonian citizens affected by its operations, and it contains the same temporal flaws as in the previous case, since it again invoked the BIT with the United States, in force since 1997, to protect investments made before 1992, without, as previously mentioned, there being a retroactivity clause in the Treaty.

The company argued that the state had agreed in advance with the plaintiffs to judicially prejudice Chevron's interests. In response, the state's defense argued to the Tribunal that Ecuador, by constitutional mandate, respects the principle of division of powers and, therefore, any interference by the executive branch in the decisions adopted, autonomously and sovereignly, by any organ of the Judiciary is expressly prohibited.

For its part, the Tribunal's decision was to order Ecuador to "(whether by its judicial, legislative or executive branch) take all necessary measures to suspend, or cause to be suspended, the enforcement and recognition, both within and outside Ecuador, the judgments of the Single Chamber of the Provincial Court of Sucumbíos of January 3, 2012 and January 13, 2012, (confirming Judge Nicolás Zambrano Lozada's judgment of February 14, 2011), against the claimant in the Ecuadorian legal proceeding known as 'The Lago Agrio Case' [...]"

Particularities of the case:

- The Tribunal acted without ruling on its own judicial authority and the State was ordered to request the judge who was hearing the case in the Ecuadorian Court to provide information on the tentative date on which he would issue his judgment. This is evidence of undue interference by the international tribunal in the sovereign decision of an autonomous judge.
- On February 14, 2011, after eight years of litigation, the Single Chamber of the Provincial Court of Sucumbíos, ordered Chevron to pay a multi-million

sum of money to the plaintiffs for the damages caused, as well as to pay the cost of the environmental remediation necessary to restore the area affected by its extraction operations, for an approximate amount of USD \$18,500,000,000. This was later reduced by the National Court in a cassation proceeding to USD 9,510,000,000. In response to the Ecuadorian ruling, the Tribunal ordered Ecuador to suspend execution of the decision of the National Court of Sucumbíos, in clear violation of the country's sovereignty.

- The Court, by itself and before itself, was invested with the authority to order the Ecuadorian State to violate its constitutional structure in order to prevent, by means of any of its functions, the execution of a judgment contrary to the interests of the plaintiff company, thereby affecting the principles of the Rule of Law.
- In this regard, it is noteworthy that all of the measures were ordered by the Tribunal before it had ruled on its jurisdiction and authority to settle the dispute.
- Without the slightest analysis, the Tribunal decided to dismiss any jurisdictional defect presented by the Plaintiff that would bar them from acting as Arbitrators to judge the case.
- A clear example of the inequitable treatment to which Ecuador has been subjected is the ongoing delay in carrying out an on-site review in the Ecuadorian Amazon, requested by the defense and opposed by the plaintiff company.
- Chevron presents motions and the Tribunal accepts them; when Ecuador presents motions, the Tribunal decides to rule on them in the future. This has been common practice by this biased Tribunal in dealing with this case. The patience of the State's defense ran out on September 19, 2014, when, in the face of a new refusal to deal with the requested inspection diligence, the State recused the members of the Tribunal from hearing the case due to a lack of impartiality
- Despite Ecuador's arguments, on November 21, 2014, the Secretary General of the Permanent Court of Arbitration, by resolution, rejected Ecuador's request.
- Between June 6 and 10, 2015, three years after the request for an on-site visit was filed, the Arbitral Tribunal and representatives of the parties visited the affected areas of the Ecuadorian Amazon, where the arbitrators were able to ascertain the extent of the damage caused by Chevron-Texaco.

OCCIDENTAL I

Occidental Exploration and Production Company (OXY) began its activities in Ecuador on January 25, 1985, when it signed a Service Contract for the Exploration and Exploitation of oil in Block 15 of the Ecuadorian Amazon. Subsequently, in 1993, Ecuador reformed its Hydrocarbons Law, establishing the ability to renegotiate Service Contracts as Participation Contracts.

On May 21, 1999, Petroecuador and OXY signed a contract that stipulated a partial restitution of the VAT payment to the company based on a mathematical factor X, which calculated the amounts of the returns to be received by OXY. Despite the signing of this document, OXY felt that these new tax rules directly affected its profits and interests, and in 2002, it filed a claim against Ecuador before the London Court of International Arbitration, arguing the violation of Article II of the BIT signed between Ecuador and the United States, which refers to fair and equitable treatment.

In response, the Ecuadorian State argued that the oil company was not denied the VAT refund that was provided for in the contract. Likewise, there was no discriminatory treatment against the company, since the tax reforms affected all companies equally. In view of both arguments, the Court found that the plaintiff company was entitled to the full VAT refund, and not only to the percentage agreed between the company and the state in the contract. Likewise, it determined that Ecuador violated the fair and equitable treatment clause, since the Ecuadorian Tax Law is discriminatory, as it excludes oil companies from the refund of this tax.

Particularities of the case

- The Arbitral Tribunal lacked the jurisdiction and authority to hear the case, because OXY had already filed claims against the Ecuadorian State for the same cause of action before national courts, which were being processed under Ecuadorian jurisdiction.
- The Tribunal ordered Ecuador not to take any legal action or adopt any measure that would deny the economic benefit of the VAT refunds to the oil company in the future, thereby interfering in national tax policy and prohibiting the country from altering the situation that the plaintiff company considered most beneficial to its interests.
- According to the rules of the BIT signed with the United States, specifically those contained in Article 10, only tax disputes involving expropriation or impediment to the free transfer of foreign currency can be resolved in international arbitration, grounds that were in no way applicable to the actions taken by the Ecuadorian State.

- In the process of jurisdiction and authority, the Arbitral Tribunal, in an extensive interpretation of the limits of its jurisdiction and the BIT clauses, decided to grant the claimant company reason, arguing that the functions of domestic justice and international arbitration were different and that disputes filed at the national level can coexist harmoniously with those that are settled at the international level, even though they deal with the same facts.
- In addition, in the process considering the claim's merits, the Tribunal decided to accept OXY's claims, ruling against Ecuador and obliging it to refund the total VAT paid by OXY as a result of the import or local acquisition of goods and services used for the production of oil for export, plus interest; it also determined that the Ecuadorian State had breached its obligation to provide OXY with fair and equitable treatment, and with treatment no less favorable than that granted to Ecuadorian nationals and other companies.
- The investigation carried out by the Commissioners determined the existence of diplomatic pressure by the U.S. Government, in complicity with government officials, such as the then Foreign Minister Heinz Moeller, who through Official Letter No. 654255/GM/SB, dated November 22, 2002, expressed to the Attorney General of the State that the Ecuadorian State, through him, had negotiated acceptance of the international arbitration proposed by OXY, as a requirement for Ecuador to be considered a beneficiary of the tariff preferences granted by the United States.

OCCIDENTAL II

OXY II was based on several alleged breaches by the Ecuadorian State of the BIT signed with the United States. The plaintiff company based its claim on the participation contract signed on May 21, 1999 between OXY and PETROECUADOR, for the exploration and exploitation of Block 15, located in the Ecuadorian Amazon.

In the ICSID claim, the company alleged that the 2006 Hydrocarbons Law was aimed at depriving it of a significant portion of its revenues. Likewise, it stated that the declaration of caducity or the state's unilateral termination of the participation contract and the operating contracts, as well as the confiscation of the totality of these investments in Ecuador without any compensation whatsoever, seriously injured the oil company. For this reason, on May 17, 2006, OXY

requested compensation of USD \$3.37 billion from the Ecuadorian State.

In response, Ecuador argued that the declaration of caducity and the unilateral termination of the contract—which resulted in the immediate return to the state of the contracted areas, and the delivery of all equipment, machinery and other exploration and production elements—was a legitimate act of the state since Oxy sold 40% of its shares to Encana Corporation, without authorization from the Ministry of Energy and Mines at the time, as stipulated in the contract itself and Ecuadorian law.

Faced with both arguments, the members of the Tribunal decided that Ecuador violated the fair and equitable treatment clause of the plaintiffs' investment, that it applied measures equivalent to the expropriation of investments prevented by the respective BIT and that it declared the caducity of the contract in violation of Ecuadorian law and customary international law, condemning it to pay USD \$1,769.6 million, plus interest, as compensation to the plaintiff.

Following the Tribunal's decision, Ecuador filed a request for annulment of the award before ICSID on October 9, 2012, alleging that the Tribunal manifestly exceeded its jurisdiction since the contract expressly excluded arbitration before ICSID. Likewise, Ecuador argued that the arbitration decisions were made without motivation or with insufficient or contradictory motivation; furthermore, fundamental rules of due process were violated.

In the counterclaim, Ecuador proposed that four aspects be taken into account: i) OXY's bad faith actions; ii) breach of the terms of the contract by the use of diplomatic or consular channels to request the settlement of the case; iii) the destructive conduct of the plaintiff company in Block 15 and; iv) OXY failed to pay an assignment fee and did not draft a new participation contract more favorable to Ecuador. The ICSID Tribunal essentially dismisses all the arguments presented by the Ecuadorian State, due to an alleged lack of evidence in the proceeding.

The hearing on the annulment phase was held from April 7 to 10, 2014, in Paris, with which the Committee formally closed the proceedings. The court's ruling was suspended pending the resolution of the ruling's nullity.

Particularities of the case:

- The Tribunal did not have jurisdiction to hear and resolve the defendant's claims, since the contract expressly excluded arbitration on issues of expiry.
- OXY's claims were premature and inadmissible because they did not challenge the administrative act of expiration before the Ecuadorian courts.

- The Tribunal concluded that the declaration of the expiration of the Block 15 contract constituted a measure tantamount to expropriation and invoked the North American Free Trade Agreement (NAFTA), to which Ecuador is not a party; a clear demonstration of the overreach of its power.
- In a contradictory act, the Tribunal declared that the lack of state authorization rendered the transfer of shares non-existent, meaning that OXY continued to be the sole owner; using this argument, it awarded OXY the full compensation amount.
- The Tribunal admitted that OXY violated the Participation Contract by not obtaining the authorization for the transfer of its shares; however, it arbitrarily considered that the declaration of expiration was disproportionate.
- Despite recognizing OXY's liability, the Court only reduced the compensation by 25% for its negligence in failing to seek authorization.
- The decision taken in the majority award was strongly rejected in the dissenting vote of one of the members of the Arbitral Tribunal, Professor Brigitte Stern, which reveals the serious violations committed by the tribunal by manifestly exceeding the limits of its own authority; it was also pointed out that the majority award lacked motivation, was contradictory and showed an evident excess of power.
- In the leaks of diplomatic cables from the U.S. Embassy in Ecuador, made by Wikileaks, the existence of pressure on the Ecuadorian State by the U.S. diplomatic delegation to favor the interests of OXY was determined, mainly during the government of Lucio Gutiérrez, a period in which Ambassador Kristie Kenney met with state officials such as Ivonne Baki, then Minister of Commerce; Mauricio Yépez, Minister of Economy; Patricio Zuquilanda, Chancellor and the Minister of Government, Raúl Baca.²⁶
- The diplomatic cable from the U.S. Embassy reveals that its top official made it known to the aforementioned Ecuadorian officials that continuing with a process against OXY, or any other U.S. company, would have serious implications for the renewal of Ecuador's tariff preferences and the negotiation of the Free Trade Agreement with the United States. For their part, representatives of the Ecuadorian State adopted a position favorable to Occidental's interests, as was the case of Ivonne Baki, who deemed the process carried out by the State Attorney against the company to be an outrageous act, and Minister Baca, who told the US Ambassador that,

on multiple occasions, he had tried to dissuade the State Attorney from taking action against OXY.²⁷

- Another diplomatic cable revealed that Yépez had considered suggesting to President Gutiérrez that a negotiating commission be formed with OXY, which would limit the influence and soften the tone of the Attorney General,²⁸ a suggestion that was adopted by Gutiérrez in later months²⁹ and supported by Foreign Minister Zuquilanda.

BURLINGTON-PERENCO

Burlington Resources Inc. began its activities in Ecuador in 2000, when, through its subsidiaries Burlington Resources Oriente Limited, Burlington Resources Andean Limited and Burlington Resources Ecuador Limited, it acquired shares in the Participation Contracts for the exploration and exploitation of oil reserves in blocks 7, 21, 23 and 24 in the Ecuadorian Amazon.

Perenco Ecuador Limited began its activities in Ecuador in 2002, when it acquired shares in the Participation Contracts for the exploration and exploitation of oil reserves in blocks 7 and 21 in the Ecuadorian Amazon; Perenco became the majority shareholder of the consortium, with Burlington controlling 53.7% of the shares of block 21 and 57.50% of the shares of block 7.

On April 19, 2006, the Ecuadorian Congress enacted Law No. 2006-42, which amended the previous Hydrocarbons Law, which established a 50% participation of the Ecuadorian State on the “surplus of oil sales prices not agreed to or not foreseen” to private contractors that had Participation Contracts in force with Ecuador.

Following the issuance of this law, Burlington and Perenco decided to file separate arbitration claims before the ICSID, arguing that the Ecuadorian State violated the clauses contained in the BITs signed with the United States (Burlington) and France (Perenco). In this regard, they argued that the increase in the participation of the Ecuadorian State in the “surplus of oil sales prices not agreed to or not foreseen” constituted an expropriatory measure on the investment made by these companies.

In its defense, Ecuador argued that Law No. 2006-42 did not imply a modification of the terms stipulated in the participation contracts, but rather only regulated a factor that had not been considered therein, explaining, in addition, that the actions of the Ecuadorian State did not correspond to expropriation measure: the Consortium formed by Burlington and Perenco abandoned the oil blocks in 2009, thus causing the expiration of the contracts signed with these companies.

As of the date of this Audit's completion, the Tribunal has not rendered a final decision on the claims, although it did issue decisions and awards on jurisdiction.

Particularities of the cases

BURLINGTON

- In the Burlington award, the Tribunal analyzed the possible existence of expropriation and, in order to do so, initially reviewed whether, based on the acts of the different instances of the Ecuadorian State, Burlington suffered a true expropriation. In other words, the Tribunal considered that, while probably one act in itself might not have constituted an expropriation, perhaps the succession of the different regulatory acts implemented by Ecuador, as a whole, could have masked an expropriation of the company.
- The Tribunal analyzed the application of Law 42, determining that it did not constitute an expropriatory act, since it was demonstrated that Burlington's revenues had not been significantly affected. This led to rejection of the expropriation argument advanced by the company and, consequently, the Tribunal declared the alleged violations of the contract and the Investment Protection Treaty to be non-existent.
- Subsequently, the Tribunal analyzed whether the act declaring the expiration of the Participation Contract with Burlington constituted an expropriation measure implemented by the Ecuadorian State. It found that, following Burlington's abandonment of the oil blocks, the fact that the Ecuadorian State took possession of, administered and exploited blocks 7 and 21 was a logical act on the part of Ecuador in view of the company's actions.
- However, the tribunal found that although the aforementioned measure was logical and legitimate for the Ecuadorian State, according to the terms of the BIT signed with the United States, it implied an obligation on the part of Ecuador to compensate Burlington for the acquisition of its assets, due to the measures taken by the Government at the time of the expiration of the contract with the company.
- It follows from the foregoing that the judgment determined that this “non-compliance” by the Ecuadorian State did in fact constitute a violation of the clauses of the BIT with the United States and, in an expropriatory and illegal act, Ecuador would have to pay the corresponding indemnities to Burlington, as a result of its violation of the rules of the BIT.

PERENCO

- Perenco Ecuador Limited is a company domiciled in the Bahamas, which in turn belongs to Perenco Gabon S.A. Of Perenco Gabon S.A., 92.5% of the shares are owned by Perenco S.A., which in turn is owned by another company called Perenco International Limited, whose shares are owned by the French citizen Hubert Perrodo, who passed away in 2006, and whose inheritance base remains suspended and has not been divided among his heirs. Based on said nationality, Perenco Ecuador Limited sued the Ecuadorian State for violation of the BIT signed with France, despite the fact that all of the aforementioned companies are located in The Bahamas.
- As we can see, Perenco used the registered address of its subsidiaries in a tax haven (Bahamas) for tax purposes; however, it assumed the nationality of its owner in order to be protected by the BIT signed between Ecuador and France.
- As in the Burlington case, the Arbitral Tribunal analyzed the possible existence of an expropriatory act against Perenco in the issuance of Law 42 by the Ecuadorian State, and determined that such action by Ecuador in no way constituted an expropriatory act.
- However, unlike in the Burlington case, the tribunal determined that the change made by Ecuador in the percentage stipulated for surplus oil prices, which increased the State's participation from 50% to 99%, implied a violation of the terms of both the participation contract and the terms of the BIT signed with France.
- Regarding the expiration of the Participation Contract, the Tribunal in the Perenco case found that, while the contract contained a provision empowering it to declare the expiration, Ecuador was not obliged to do so; and therefore, by declaring it, an act violating the Participation Contract took place, inasmuch as the Ecuadorian State should have waited for the ruling of the Arbitral Tribunal.

In the Commission's opinion, the existence of such explicit contradictions in two proceedings arising from the same factual situation, presented under the same circumstances and arguments, clearly reflects the deficiencies of the international investment dispute settlement system, since it denotes the inability of the arbitration centers (in this case ICSID) to avoid contradictory awards, the lack of a system of case analysis and rules limiting the broad interpretations by arbitrators, as well as the absence of an authority able to regulate

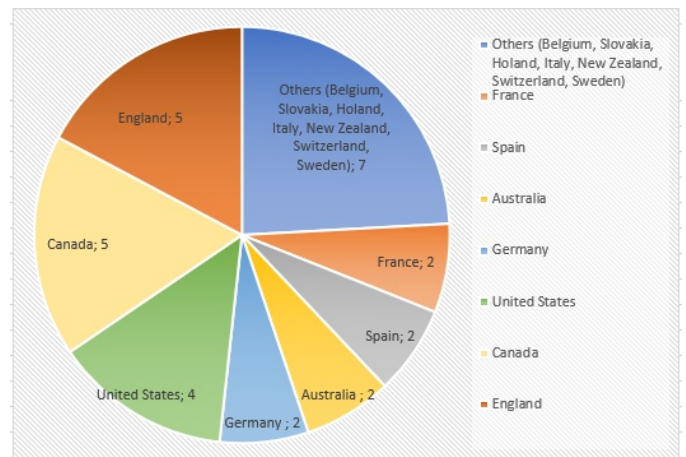
these situations or to act as an appellate body to remedy such disparities.

The role of arbitrators in the international investment arbitration system and the cases against Ecuador

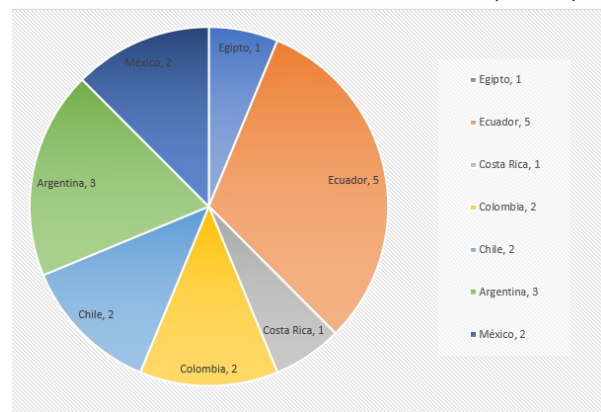
Arbitrators who have participated in proceedings against Ecuador

A total of 45 arbitrators have acted in the cases against Ecuador analyzed by the Commission, of which 64% come from “developed countries” (mainly England, the United States, Canada and other European countries).

Arbitrators from “developed countries” (64.4%)



Arbitrators from other countries (35.6%)



Elaboration: CAITISA.

In turn, of the 45 arbitrators who have acted in cases against Ecuador, only two are women. These statistics follow the global trend where the vast majority of arbitration panels are composed of men from Europe, the United States and Canada.

The international investment arbitration industry is dominated by a small and compact group of arbitrators, who have been described by academics, journalists and others close to the investment arbitration circuit as “a small secret club”,³⁰ “a closed circle”,³¹ “a hermetic homogeneous group made up of ‘Good ol’ boys”³²

These elite arbitrators³³ account for the majority of known investor-state arbitration cases. For example, just 15 arbitrators, almost all of them from Europe, the United States or Canada, have resolved 55% of all known disputes based on investment treaties.³⁴

This trend can also be seen in the cases against Ecuador, where 58%, or 26 of the nominated arbitrators, are considered “elite”, since they are part of the club of influential arbitrators with repeated nominations. Of these, 13 are considered to be among the main points of reference in the world of investment arbitration worldwide.

Arbitrators who are part of this group tend to support and defend the investment protection system, even when its contradictions are such that they threaten to discredit it. Many have a greater affinity with the commercial world and their position gives them the power to decide whether the national policies of state actors are “legal”. Furthermore, in their case analysis, they tend to ignore that, in certain circumstances, states must implement public policies in the interest of their citizens or the environment, even when these policies affect investors' profits.

When arbitrators with a shared vision and shared interests in the system represent the majority of the arbitration panel, they are in a position to interpret the law similarly and, potentially, control arbitral decisions.

In the analysis of cases against Ecuador, the presence of arbitrators considered super-elite seems to have influenced the outcome:

a. In most cases where two or more arbitrators are part of the super elite, the award has favored the investor: It is evident that, of the eleven cases where the Tribunal has issued an award, for six it was in favor of the Investor (Oxy I, Duke Energy, Oxy II, Chevron (II), Perenco and Burlington). What is striking is that in five of the six cases, two or more of the arbitrators who made the decision are considered super-elite. On the other hand, of the cases where the award was in favor of the State (M.C.I. Power Group, Encana, Emelec, Ulysseas, Murphy I), only in one were two of the referees were super elite.³⁵ This situation demonstrates that when two or more of the arbitrators are super-elite—who have the highest stakes in the survival of the system and whose main source of income is investor-state disputes—the chances of the outcome being pro-investor are increased.

b. In almost all cases where the award has been in favor of the investor, the president of the Tribunal is a super-elite arbitrator: In 5 of the 6 cases against Ecuador where the award has been in favor of the

investor, the president is considered a super-elite arbitrator, namely Oxy I (F. Orrego Vicuña), Duke Energy (G. Kaufmann-Köhler), Oxy II (Y. Fortier), Chevron II (President K.H. Böckstiegel), Burlington (President G. Kaufmann-Köhler); the only exception would be the Perenco case (P. Tomka). In contrast, in all cases where the award has been in favor of the State, the president of the tribunal is a well-known arbitrator, but not considered super-elite: M.C.I. Power (R.E. Vinuesa), Encana (J. Crawford), Emelec (President (B. Sepúlveda Amor), Murphy I (President R. Oreamuno Blanco) and Ulysseas (President P. Bernadini).

Commercial bias of arbitrators

Most arbitrators have built their careers around commercial arbitration, in which they maintain direct links with international arbitration centers, international law firms and have even acknowledged that “[...] they do not normally see themselves as guardians of the public interest”,³⁶ which is a determining factor in deciding whether or not the government's actions are justified, beyond the impact on private interests. Arbitrators do not have the power to decide whether the national policies of sovereign states are “legal” under international law, but in many cases, due to their mostly commercial and business-oriented vision, they tend to disregard public policies in benefit of citizens or the environment.

The education that arbitrators receive is paramount in the decisions they make. In Brigitte Stern's words, its importance lies in the fact that “arbitrators have to make decisions to resolve disputes and these decisions are, of course, in line with their political point of view.”³⁷ Furthermore, some research confirms that investment arbitration is driven by non-legal factors, such as arbitrators' political preferences and their social and personal backgrounds.³⁸

Thus, arbitrators coming from the public sector are more receptive to the need for states to regulate public policies to meet the needs of the population in terms of public health or environmental protection. On the other hand, arbitrators coming from the commercial field tend to protect the expectations and rights acquired by investors, to the point of considering that under no circumstances should they be altered.

An analysis of the education of the 45 arbitrators who have acted in cases against Ecuador shows that 69% come from the field of commercial arbitration and, throughout their careers, have been engaged in mediating commercial cases or advising corporations.

Other interesting observations that emerge from this analysis are the following:

In at least 50% of the cases, the state has nominated arbitrators who come from the commercial field, when one would have expected that the state would seek arbitrators with a profile more oriented to public international law, or a background not so close to the rights of investors.

In at least 89% of the cases, investors nominated arbitrators coming from commercial backgrounds.

The presidents nominated in cases against Ecuador, who are known to have a determinative weight upon the decision of the arbitration panels, come, in 62.5% of the cases, from the area of commercial arbitration.

The arbitration system structure creates conflicts of interest

Notwithstanding the investment arbitration system's semblance of independence and impartiality, in recent years significant shortcomings in the rules governing the system have come to light.

In the last five years, criticism of the operation of international investment arbitration, and of ICSID in particular, has intensified. The following is a summary of some of such problems that have been publicly discussed in different spheres and institutions, and which we find replicated in the case of the arbitrations against Ecuador:

The investor-state arbitration system borrows its practices from private commercial arbitration: Private-to-private commercial arbitration practices are inappropriate in cases of disputes against States when public policy decisions are at stake.

Cases are decided by arbitrators chosen on an ad-hoc basis, without institutional guarantees of impartiality and independence: There has been strong criticism of the fact that three individuals, appointed on an ad-hoc basis, are in charge of assessing the validity of state actions, particularly in cases involving public policy issues. In the case of investment arbitrators, there are no institutional guarantees of impartiality and independence, such as: security of tenure, prohibition from holding another paid position, prohibition from practicing law, among others.³⁹

Serious arbitrator conflicts of interest have been identified: One of the main criticisms lies in the fact that arbitrators frequently exercise, in parallel, the role of representatives of the parties. Arbitrators have also been identified as having monetary incentives to: a) benefit investors, since they are the only ones who can initiate claims, b) accept jurisdiction and extend their participation in the case as long as possible, since the longer the case,

the higher their remuneration, and c) defend the investment arbitration system as it exists today.

Arbitrators make a broad interpretation of the rules, thus favoring investors: Awards issued by international arbitrators against States have in many cases incorporated overly broad interpretations of investment treaty language. These interpretations have given priority to the protection of the property and economic interests of transnational corporations over the right of each state to regulate and the right of peoples to self-determination.

In ICSID, the system of arbitrator disqualification is particularly problematic: Investment arbitration lawyer Karel Daele has published a study outlining the difficulty of disqualifying arbitrators, even when there are clear conflicts of interest. The result of their research indicates that as of 2011, only one request for recusal (out of 32) had been accepted at ICSID. This is because the grounds for objection are too narrow and the two non-opposed co-arbitrators are those who decide on the objection. The result is that the arbitrators—usually part of the same elite group—are those who decide whether one of their peers is impartial.

Other problems include the lack of judicial review of awards: The rules of the current ICSID international arbitration system stipulate that awards are final, binding and there is no appeal mechanism. The lack of transparency is also criticized.

Conflicts of interest of arbitrators deciding cases against Ecuador

The arbitrators who assess the validity of the Ecuadorian State's acts have been chosen, on an ad-hoc basis, without prior institutional guarantees of impartiality and independence. Most of these individuals have continued to serve in other roles, such as party counsel in arbitrations, company advisors, company board members or expert witnesses.

Of the 45 arbitrators who have participated in cases against Ecuador, 73% continue to practice law in law firms, and combine their practice in law firms with their role as arbitrators. A total of 71% advise companies or sit on company boards. In practice, this modus operandi leads to a number of potential conflicts of interest.

Of the 26 cases against Ecuador, conflicts of interest have arisen that led to requests for recusal in relation to eight arbitrators. In five of these, the arbitrators were nominated by the investor. The conflicts of interest identified in these cases were related to public statements

denoting bias against the Ecuadorian Government or its legal representatives, a close relationship between the arbitrator and the law firm representing the investor, and involvement in other cases where the circumstances were very similar.

made use of his prerogative to resign “for personal reasons”. The same occurred in the case of the arbitrator Brigitte Stern, after Merck requested her recusal.

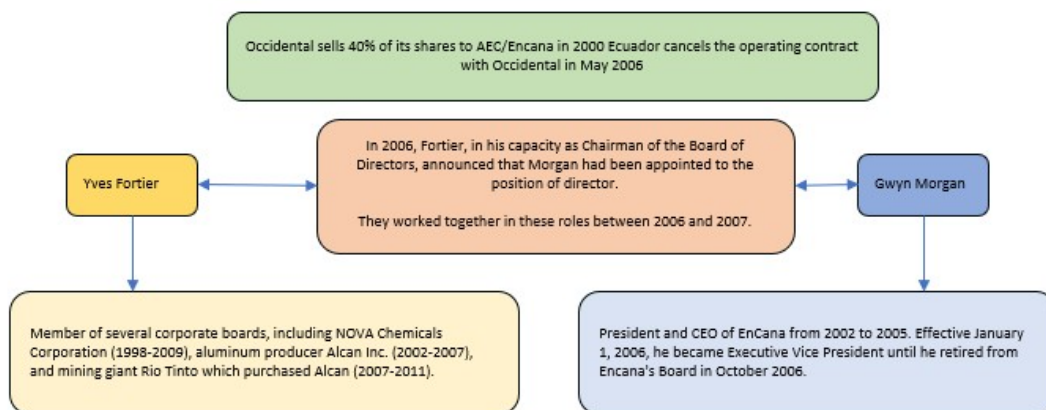
In two of the cases against Ecuador (Burlington and Perenco), the challenge was successful, and resulted in the removal of the contested arbitrator from the arbitral tribunal.⁴⁰ In one of the cases (Merck Sharpe) the objection was not successful, and the presence of the contested arbitrator in the tribunal was ratified. Finally, in the (Murphy) case, the challenge filed by Ecuador was not heard, as the recused arbitrator, Argentine Guido Tawil,

Arbitrator	Case	Conflict	Resolution
Charles N. Brower (Investor-Appointed Arbitrator)	Perenco v. Ecuador	The arbitrator has publicly criticized the state for its government policies. Brower gave an interview in The Metropolitan Corporate Counsel magazine called “A World-Class Arbitrator Speaks!” where he criticized governments’ moves to opt out of the investment protection system and called Ecuador recalcitrant. Brower was recused in the Perenco case on December 8, 2009. In the meantime, the Chevron/Texaco II case was ongoing and Brower was the investor-nominated arbitrator. In 2011, the Chevron/Texaco Tribunal issued an award against the state and ordered it to pay US\$96,000,000.	The recusal was accepted
Francisco Orrego Vicuña (investor-nominated arbitrator)	Burlington v. Ecuador	The arbitrator has been repeatedly nominated by the same law firm and is therefore presumed to have a relationship with one of the parties to the dispute. Freshfields has repeatedly appointed Orrego Vicuña as arbitrator. He was questioned about the lack of disclosure of these appointments in the case and about its behavior in the process, including: his dissent from the court’s decision on jurisdiction in 2010; his decision on liability in 2012; and his conduct during the July 11, 2013 pre-hearing teleconference. What led to his recusal, however, was not the facts originally alleged but his response to the recusal request, in which he questioned the ethics of Ecuador’s legal representative.	The recusal was accepted
Guido Tawil (Investor-nominated arbitrator)	Murphy v. Ecuador (III)	The arbitrator has cooperated in repeated cases with some of the law firms representing the parties in the dispute. The recusal request is based on the close relationship between Tawil and King and Spalding (Murphy’s representative in the case): Tawil served as co-representative with King and Spalding in three other cases: Azurix Corp. v. Argentina (ICSID Case No. ARB/01/12), Enron v. Argentina (ICSID Case No. ARB/01/3) and Azurix Corp. v. Argentina (ICSID Case No. ARB/03/3). And he was nominated by the firm as an arbitrator.	Stephen M Schwebel (Investor-nominated arbitrator)
resigned.	Merck v. Ecuador	The arbitrator has been repeatedly nominated by the same party to the dispute or the same law firm. Prior appointments as arbitrator and as expert witness by the company’s defense counsel, aggravated by the fact that the arbitrator did not declare these appointments.	Recusal denied
Brigitte Stern (state-nominated arbitrator)	Murphy v. Ecuador (III)	Has already acted in other cases against the same State in relation to the measures leading to the lawsuit. The request for recusal is based on the grounds that B Stern has already prejudged fundamental issues that constitute the subject matter of this dispute (through his participation in the Burlington v. Ecuador) and has a history of being appointed by plaintiff states.	V.V.
resigned Veeder Horacio A. Grigera Naón Vaughan Lowe	Chevron III	The State Attorney General argued that the tribunal did not comply with its obligations and did not dedicate the necessary time to make important decisions within the process, including the site visit requested by the country more than 3 years ago. For Ecuador, there was a pattern of conduct in actions that favored Chevron. The tribunal has failed to sanction Chevron-Texaco for procedural violations, such as submitting evidence without authorization and at the last minute, as well as violating its order not to exacerbate the dispute.	Recusal denied

Elaboration: CAITISA.

However, it is possible to identify several cases of potential conflicts of interest that did not lead to recusal requests. This seems to have been the situation with the President of the Tribunal in *Oxy vs. Ecuador (II)* Yves Fortier, where a possible conflict can be inferred as a result of his role in multinational companies. Despite this, there was no request for recusal by the Ecuadorian State.

Canadian Yves Fortier, who was president of the arbitration tribunal in the *Oxy vs. Ecuador (II)*, has also been a member of the boards of directors of companies such as NOVA Chemicals Corporation (1998-2009), the aluminum producer Alcan Inc. (2002-2007) and the giant mining company Rio Tinto (2007-2011), among others. Like Kaufmann-Kohler, he defends being part of the corporate world with the following statement: “Being on the board of directors of a publicly traded company—and I have served on several such boards—has helped me in my practice as an international arbitrator. It has always given me an insight into the business world that I would not have been able to gain as a lawyer.”⁴¹



Elaboration: CAITISA.

However, holding these multiple roles has created conflicts of interest.

Gwyn Morgan was president and CEO of Encana from 2002 to 2005 and executive chairman until October 2006. Encana is the company to which Oxy sold 40% of its shares, in violation of Ecuadorian law. Fortier and Morgan worked together at ALCAN between 2006 and 2007. In 2006, Fortier, in his capacity as Chairman of the Board of Directors, announced that Morgan had been appointed to the position of director.

Another example worth highlighting is that of arbitrator Horacio Grigera Naon. He is the arbitrator with the most nominations in cases against Ecuador. He has participated in Encana, Murphy I and Chevron III (as well as City Oriente and Repsol YPF), and has always been nominated by the investor. The conflict arises from his apparent relationship with the law firm King & Spalding. This firm represents the investor in three of the four cases where Grigera was nominated as arbitrator (City Oriente, Murphy I and Chevron III). Grigera was also nominated as arbitrator by King & Spalding in S&T Oil Equipment & Machinery Ltd. vs. Rumania. According to the guidelines of the International Bar Association, these repetitive appointments may be grounds for recusal.⁴²

This connection between Grigera Naon and the law firm King & Spalding was denounced in a February 2012 letter to the Attorney General by the collective Frente de defensa de la Amazonia, in which they claim that the arbitrator rules in favor of King & Spalding's clients.⁴³ However, this serious and obvious connection was not taken into account by the State Attorney General's Office in the October 24, 2014 request for recusal of all members of the Chevron III Tribunal for their lack of impartiality.

It is also important to consider whether a request to disqualify an arbitrator in one case may have repercussions in another case against the party that sought to disqualify the arbitrator. For example, Ecuador requested the recusal of Charles Brower in the Perenco case and the Secretary General of the Permanent Court of Arbitration accepted the recusal on December 8, 2009. In the meantime, the Chevron/Texaco II case was ongoing and Brower was also the investor-nominated arbitrator. In 2011, the Chevron/Texaco Tribunal issued an award against the state and ordered it to pay US\$96,000,000. Perhaps it would have been appropriate for the State to also question the impartiality of Arbitrator Brower in the Chevron II case.

Finally, it is necessary to point out that the thresholds and rules for challenging arbitrators in the current system are

extremely high and rigid, which is why many of the aforementioned considerations are extremely difficult to prove and have a low probability of being accepted.

Arbitrators promoting a broad investment protection scheme

Among the arbitrators who have served on arbitral panels in cases against Ecuador, there are numerous examples of members who are in favor of a broad investment protection scheme. As public figures, they argue for the signing of investment protection treaties or against reforms restricting the content of the clauses included in such treaties. These positions have been instrumental in promoting the investor-state arbitration system and in lobbying for the preservation of the status quo. We could argue that just as corporations captured the financial system, investment lawyers have captured the investment arbitration system. We refer to these types of conflicts of interest as conflicts of interest related to the system itself. Nevertheless, this clear pro-investor bias is not currently accepted as grounds for recusal. But it undoubtedly raises ethical issues that should be addressed in view of the financial incentives that investment lawyers have in perpetuating the investment scheme.

Academic research, as well as surveys of international companies, suggest that investment treaties are not a conclusive factor in investors' decisions to invest abroad.⁴⁴ Despite ample evidence, some arbitrators publicly argue that the signing of treaties is a necessary condition for attracting foreign investment. This is the case, for example, of Francisco Orrego Vicuña, investor-appointed arbitrator in the Burlington case and president of the Tribunal in the Occidental (Oxy) I case. He has stated, in a 2010 interview, that "if countries do not sign BITs, they will have nothing to offer and will lose investment, as has been seen on numerous occasions."⁴⁵ Ahead of the renewal of the Spain-Mexico BIT, Bernardo Cremades (the arbitrator proposed by the state in the Noble Energy Inc. and Machala Power case, and nominated by the investor in Copper Mesa) pointed out that the treaty was important for increasing foreign direct investment between the two countries; he noted in this context that "Mexico and Spain have signed a new bilateral investment treaty with a new chapter on dispute settlement. It refines the fundamental principles of investor protection and the dispute settlement mechanism" ... "The treaty is important for increasing foreign direct investment between the two countries".⁴⁶

Although the impartiality and independence of arbitrators has increasingly been called into question,⁴⁷ several arbitrators argue that investment arbitration is the only option that offers neutrality in the resolution of investor-

state disputes and that, in contrast, domestic courts are not neutral. This line of reasoning has been upheld, for example, by Horacio Grigera Naon (investor-nominated arbitrator in the *Encana*, *City Oriente*, *Murphy*, *Repsol YPF* and *Chevron III* cases). GrigeraNaon asserts that international arbitration centers can provide greater protection for local substantive law. He also asserts that “arbitrators' neutrality is ensured by the independence of the courts, cultural neutrality and the delocalization of the arbitration centers”; i.e., in his opinion, arbitrators do not have any influence or interference in their decisions.⁴⁸ Charles Brower (arbitrator in the *Occidental I*, *Perenco* and *Chevron/Texaco II* cases), also presented a similar defense in 2009, explaining that: “The problem with most state courts is that they are not—or at least are not perceived as—neutral enough to resolve disputes between foreign investors and host countries. In many developing and transitional countries, there are no independent courts that can decide cases in accordance with pre-established rules of law in an expeditious manner.”⁴⁹

Several arbitrators have publicly advocated for the need to keep investment rules vaguely written/open to interpretation, as a way to counterbalance the position of governments seeking to amend their treaties to protect their public policy regulatory space. For example, Stephen M. Schwebel (investor arbitrator in the *Merck Sharpe & Dohme* case) has strongly condemned changes to the US model BIT.⁵⁰ Schwebel served on the government's advisory committee and, together with business lobbyists, advocated a return to stronger investment protection.⁵¹

Chilean arbitrator Francisco Orrego Vicuña (who participated in the *Burlington* cases and was the chairman of the *Occidental I* panel), questioned the initiative of the Union of South American Nations (UNASUR) to establish a regional dispute settlement center, saying: “The result would be a kind of anti-investment arbitration forum, offering an alternative to ICSID and other instances that are perceived as too investor-friendly. I don't think it's a good idea, since any such institution would almost certainly be seen as too pro-state, and that would not be satisfactory to investors.”⁵² This comment appears to contain a double standard. While defending a system understood to be favorable to investors, the opinion is that a system that could be perceived as favorable to the state would be unacceptable.

Charles Brower has defended the rules of fair and equitable treatment and indirect expropriation because, according to him, they do not limit states' abilities to regulate in the public interest. He argues that “the concept of indirect expropriation, therefore, leaves a wide margin for host countries to regulate foreign investment, provided

that this regulation has a legitimate purpose, is non-discriminatory and maintains a reasonable or proportional balance between the protection of the investors' investment and the public interest” and, he continues “the same can be said with regard to the concept of fair and equitable treatment.” Although this standard seems particularly vague and is widely used by courts to condemn host state judicial, administrative and legislative actions, its application is not as unpredictable and capricious as some critics argue.”⁵³

Brower went so far as to question Canada's request for an interpretative declaration of the indirect expropriation clause included in NAFTA. He thus advocates that arbitrators, at their discretion, should interpret that rule.⁵⁴

On the disqualification of arbitrators and the criteria for their selection

While Ecuador's request to disqualify arbitrators was accepted on two occasions (Charles N. Brower, in the *Perenco* case, and Francisco Orrego Vicuña, in the *Burlington* case), it is clear that the threshold for disqualifying arbitrators is very high, even when clear conflicts of interest exist. The chief reason is that the accepted grounds for considering an arbitrator to lack a sufficient level of independence and impartiality for qualification are too limited, especially under the guidelines of Article 14 of the ICSID Convention. This difficulty is further increased when the decision on the disqualification is made by fellow arbitrators whose appointment has not been challenged. Until such point as there are stricter criteria for independence and impartiality to which arbitrators must adhere, and an impartial institutional body in charge of making the decision, it will continue to be very difficult for States to challenge arbitrators with clear conflicts of interest.

Despite evidence of bias towards investors by those who regularly serve as arbitrators, the criteria and principles upon which arbitrator selection and disqualification strategies can be developed are lacking. These criteria would help Ecuador define which arbitrators should be excluded from nominations to arbitration panels, and which should be challenged on the basis of being members proposed by the investor or as presidents of the tribunal proposed by the institution administering the arbitration. The proposed criteria fall into three categories: “conflict of interest” (“conflicto de intereses”), “conflict of issues” (“conflicto de cuestiones”) and “systemic conflicts” (“conflictos sistémicos”).

- a. “Conflicts of interest” refer to the arbitrator's lack of impartiality as a result of relationships with the parties to the dispute and/or financial interests in the dispute's outcome. Examples of

this type of conflict include: if the arbitrator is or has been the legal representative or counsel for one of the parties; if the arbitrator has a close family relationship with one of the parties; if the arbitrator is a shareholder of one of the parties; if there is a close personal friendship between the arbitrator and the attorney for one of the parties; if the law firm to which the arbitrator belongs has had or has a substantial relationship with one of the parties to the dispute; if the arbitrator has been repeatedly appointed by the same party to the dispute or the same law firm, among others.

b. “Conflict of issues” refers to cases in which the arbitrator's impartiality is questioned because the arbitrator has taken a clear position on a legal issue more than once and previously on one or more of the issues to be discussed in any new case. Examples of this type of conflict include cases where the arbitrator has publicly expressed opinions unfavorable to one of the parties, the arbitrator has expressed opinions unfavorable to the arguments presented by one of the parties, or the arbitrator has acted in other disputes involving the same facts, on the same grounds. The aim is to avoid what is understood in other legal systems as “prejudgment”.

A possible list of criteria for establishing whether arbitrators should be excluded on the grounds of **“conflict of interest” and/or “conflict of issues”** is derived from the (voluntary) guide on conflicts of interest in international arbitration⁵⁵ prepared by the International Bar Association (IBA). While the majority of these criteria have not been accepted by arbitration panels as justification for challenging of arbitrators, the list of criteria set out therein is still worth consulting as a guide to determine which arbitrators the Ecuadorian State should seek to veto in the selection process (see Annex 4 of this report).

c. Lastly, with “systemic conflicts”, the arbitrator's impartiality is questioned not because of involvement in a specific case, but rather because of other positions or roles that may indicate that a pro-investor bias and/or defense of and advocacy for the traditional investment arbitration system. Among these criteria, we find the following:

If the arbitrator argues that the signing of investment protection treaties is a necessary condition for states to attract foreign investment.

If the arbitrator contends that investment arbitration is the only option offering neutrality in dispute resolution and/or denies that there are deficiencies in its rules.

If the arbitrator publicly advocates/lobbies for countries to maintain investment protection that are vague or open to interpretation.

Arbitrators who criticize measures taken by governments to exit the investment protection system or to restrict its application (e.g. criticism of the denouncement of BITs, denouncement of the Washington Convention, termination of intra-US treaties, etc.).

Arbitrators who systematically apply an expansive (pro-investor) interpretation of the rules.

Arbitrators who abuse their power through bad faith and/or manifestly arbitrary technicalities/interpretations (e.g., in the Metalclad case, where arbitrators ruled on the powers of internal bodies and interpreted the constitution).

When through their interpretation, the arbitrators establish new obligations that the states had not considered.

When arbitrators sit on company boards of directors.

When arbitrators lobby on behalf of companies for improvements in investment protection laws or when they advise companies on how to make better use of investment protection treaties (e.g., by restructuring investments to enable treaty-shopping).

Arbitrators who repeatedly dissent when awards are in favor of the state.

Arbitrators who hold other gainful positions in the same field of investment arbitration (especially as investor representatives or lobbying for companies).

Arbitrators primarily trained and practicing in the area of commercial law.

Arbitrators who are regularly nominated by investors.

Once this list of criteria on “conflicts of interest”, “conflict of issues”, and “systemic conflicts” has been defined, we can begin to contrast them with the characteristics of each of the possible arbitrators to be nominated by the state and/or nominated by the investor or as President of the Tribunal. Eventually, this list of criteria would make it possible to establish a list of names of arbitrators with a pro-investor bias that the state should avoid selecting or should attempt to disqualify.

In addition to the negative criteria for arbitrators, it is also possible to identify certain “positive criteria” that state-nominated arbitrators should possess, for example:

- That they have experience in and deep knowledge of Public International Law.

- That they defend the fact that arbitrators should not be able to act as representatives of the parties.
That they have a history of interpreting investment protection rules in a restrictive manner and in line with what is known to have been the intention of the states when the treaty was signed.
- That they take into account social, economic and human rights and the public interest when analyzing the government policies that led to the case.
- That they take into consideration the behavior of the companies in the territory of the defendant state, (for example, whether they have committed social or environmental violations, if they have contributed or not to national development, if they have committed acts of corruption, etc.).

On the civil and criminal impunity enjoyed by arbitrators

Throughout history, the members of international arbitration tribunals have enjoyed a special immunity status, which immunizes them, during the performance of their functions, from any future claim by any of the parties submitted to their arbitration. The impunity enjoyed by this select group of arbitrators has allowed them to adopt whatever decision they wish while leaving them exempt from legal responsibility for the consequences of their actions. This becomes unacceptable when we consider that arbitrators can compromise the politics and economics of a state to the tune of billions out of its public funds.

Law firms involved in the proceedings against Ecuador. Nationalities, specializations, representations.

Ecuadorian law firms

The law firms involved in the cases against Ecuador

A total of 30 law firms have acted in the 26 investor-state BIT cases against Ecuador. Of these firms, 21 have been hired for representation by investors and nine by the state.

Of the 30 law firms that participated in the cases, 23 (77%) were international and seven were Ecuadorian. Of the international law firms, the vast majority (15) have their headquarters in the United States, and the rest in Canada (4), Great Britain (2), Switzerland (1) and Bolivia (1). Most of these firms are part of what can be considered international law firms, which specialize in international arbitration and are market leaders in

international investment arbitration.

OECD data shows that these firms can charge up to USD 1,000 per hour of work per lawyer,⁵⁶ and it is always a team that handles each case. The fees charged by law firms for representation generally range from USD 3 to 5 million.

In Ecuador, the counterparts of these foreign firms have a long trajectory and have been creating internal work areas specialized in international arbitration. These are large firms that dominate the legal market in Ecuador, such as Pérez Bustamante & Ponce and Bustamante & Bustamante, which are dedicated to advising energy companies regarding Ecuadorian governmental measures that affect their interests. In addition, several of these firms have among their associates renowned international arbitrators, such as Javier Robalino and Bruce Horowitz (of Paz Horowitz Robalino Garcés), Alejandro Ponce Martínez (of Quevedo y Ponce) and César Coronel Jones (of Coronel y Pérez Abogados).

Law firms representing the State

Like most governments in the Global South, the government of Ecuador hires outside law firms to handle the defense in investor-state cases.

Up until 2007, the State Attorney General's Office (PGE) entirely delegated cases to international law firms, without any competition, and simply by invitation. This was the case, for example, when the law firm Winston & Strawn was selected for the Chevron I case in 2004. The firm also later defended the State in the Chevron II, Chevron III and Murphy I cases.

Law firm representing the investor	Cases	Law firm representing the State	Cases		
King & Spalding (United States)*	6	Noble Energy-Machala Chevron (II) and Chevron (III); Murphy (I), Murphy (II); Murphy (III)	Foley & Hoag (United States)*	6	Oxy (II); Murphy (I); Murphy (III); Zamora Gold; Merck Sharpe & Dohme; RSM
Perez Bustamante & Ponce Attorneys at Law (Ecuador)*	5	Murphy (I); Murphy (II); Noble Energy and Machala; Perenco; Quiport	Dechert LLP (United States)*	5	Oxy (II); Perenco; Burlington; GLOBALNET-Únete Telecomunicaciones; RSM Production Corporation
Debevoise & Plimpton LLP (United States)*	2	Oxy (II); Perenco	Cabezas & Wray Attorneys at Law (Ecuador)	4	M.C.I. Power Group; Duke Energy; Emelec; Oxy (II)
Freshfields Bruckhaus Deringer (Great Britain)*	2	Burlington; GLOBALNET-Join Telecommunications	Winston & Strawn (United States)*	4	Chevron (II); Chevron (III); Murphy (I)
Covington & Burling (United States)*	2	Oxy (II); Perenco	Weil Gotshal & Manges (United States)*	2	Oxy (I); Encana
Paz Horowitz Robalino Garcés (Ecuador)	2	Burlington; Ulysseas	Squire, Sanders & Dempsey (United States)	1	Oxy (II)
Quevedo & Ponce (Ecuador)	1	Chevron (II)	Baker Botts (Great Britain)*	1	Ulysseas
Appleton & Associates International (Canada)*	1	M.C.I. Power	Fabara & Compañía (Ecuador)	1	Noble Energy and Machala
Borden Ladner Gervais LLP (Canada)	1	Zamora Gold	Lalive (Switzerland)*	1	Copper Mesa
Colonel and Perez Attorneys at Law (Ecuador)	1	Duke Energy			
Crowell & Moring (United States)	1	Duke Energy			
Fulbright & Jaworski (United States)*	1	Duke Energy			
Jones Day (United States)*	1	Chevron (III)			
McCarthy Tétrault (Canada)	1	Encana			
McMillan LLP (Canada)*	1	Copper Mesa			
Moreno Baldivieso (Bolivia)*	1	GLOBALNET-Únete Telecommunications			
Provost Umphrey LLP (United States)	1	Emelec			
Vinson & Elkins (United States)*	1	Ulysseas			
Wilmer Hale (Great Britain)*	1	Merck Sharpe & Dohme			
Astigarraga Davis (United States)*	1	M.C.I. Power			
Bustamante y Bustamante (Ecuador)	1	Encana			

Elaboration: CAITISA.

Some noteworthy characteristics of the law firms hired by the state:

- They actively seek new cases that could lead to claims in international investment tribunals: for example, Latham & Watkins, whose lawyers joined Cabezas and Wray's team in the Duke Energy, Emelec and M.C.I. Cases. Power provides advisory services to service and energy companies in the wake of the so-called “Arab Spring” in North African countries.
- They not only defend states; they also represent investors: Dechert and Latham & Watkins, for example, have also represented companies such as France Télécom, Total, Green Dragon Gas and Daimler Financial Services.
- They are specialized in Latin America. They represent countries, including Ecuador, and also represent companies against other Latin American states. For example, Dechert, which represents the state in five cases under the ICSID Convention, has advised

holdouts such as U.S. hedge fund NML Capital to obtain payment of Argentina's debt. In 2012, another of the State's law firms, Weil Gotshal & Manges, succeeded in having Argentina removed from the U.S. General System of Preferences for alleged non-payment of an ICSID award.

Regarding Ecuadorian law firms and lawyers

Some Ecuadorian lawyers and law firms have played a role in promoting investment arbitration. In 2000, for example, in a letter to the then Minister of Foreign Affairs Heinz Moeller Freire, the firm Coronel y Pérez requested that Ecuador ratify the ICSID Convention, which had been signed in 1985 but had not been ratified by the National Assembly. This letter was signed by César Coronel Jones, whose law firm represented, in 2004, Duke Energy, which went to ICSID because of disagreements regarding energy purchase contracts.

Dr. Edgar Terán was the signatory, on behalf of Ecuador, of the ICSID Convention in 1986; he was also, as previously mentioned, ambassador to the United States

when pressure was exerted for the signing of its BIT. Years later, in 2002, his law firm Terán & Terán was hired by IBM to represent it in its ICSID claim against Ecuador.

Economic impact of the cases and their impact on the State Budget

The Ecuadorian State has been sued for a total of USD \$21,223,947,079, in terms of compensation, for the alleged violation of the BITs providing protection to foreign investors.

So far, it has paid USD \$1,342,115,969 as a result of negative awards or by agreement of the parties (to IBM, Oxy I, Duke Energy, Noble Energy & Machala, Oxy and Chevron), minus the payment ordered in favor of the state in the Ulysseas case.

For awards that are also condemnatory, but whose annulment has been requested by the Ecuadorian State, the payment of **USD \$377,415,988** has been determined (Brulingthon, Murphy III and Cooper Mesa cases).

Apart from these sums, in the 2003-2013 period, Ecuador has had to assume the following expenses in order to address the 24 claims generated by apparent violation of the BITs:

- Tribunal fees and proceeding costs
USD \$11,581,137
- Fees and expenses of law firms representing the state
USD \$144,348,280
- **Total** **USD \$155,929,417**

Between payments already made for awards based on BITs, arbitration fees and costs and payments to law firms for defense expenses, the amount paid by the Ecuadorian State totals USD \$1,498,045,386, which is equivalent to 5.8% of the 2017 General State Budget.

Outstanding amounts

Additionally, of the cases that are currently open and for which the Tribunal has not issued a final award, the amount of the claims totals USD \$11,188,966,571 (Chevron III, Merk Sharp & Dome, Perenco, GLP and Albacora cases). Although the amounts can be considered speculative—the fact that the investor sues for a certain amount does not mean that the state will have to pay that amount (either because the award is contrary to the investor or because the Tribunal determines a much lower compensation)—they can create uncertainty in the national budget and in the programming of public investments to sustain the development process towards

Good Living.

In sum, there would be a threat of payments for certain amounts totalling USD \$13,409,667,571. (If we add the negative awards under challenge by Ecuador: Burlington, Cooper Mesa and Murphy III cases). This represents a value close to 52% of the 2017 General State Budget.

State Contracts

One of the ways in which foreign investment enters national territories is the signing of contracts between investors and states, especially in the fields of services and the exploitation of natural resources such as oil, gas, and water, among others.

This contract is defined as a contract entered into between the state, or a state entity, whereby control of an economic activity is granted to a foreign national or a legal entity of foreign nationality (investor).⁵⁷ This type of contract is not necessarily tied to a specific international investment agreement, and it may be entered into autonomously, including with an investor who is a national of a state not party to an investment treaty.

These investment contracts often contain rules that reflect the same standards of investment protection as BITs, including the transfer of jurisdiction to international arbitration tribunals. These contracts should therefore be considered a key element in the international investment protection scheme.

Article 422 of the Ecuadorian Constitution prohibits the State from exercising jurisdiction over international arbitration in the case of international treaties. However, its interpretation is ambiguous as to the application of this restriction to investment contracts. There are three possible legal interpretations of the rule:

- *Equation*: State investment contracts are “international instruments”. Consequently, the prohibition of Article 422, first paragraph, expressly extends to BITs and investment contracts alike.
- *Exclusive Separation*: Investment contracts are not “international instruments”. The prohibition in Article 422 applies only to Treaties. It does not include any provisions regarding investment contracts. Consequently, the transfer of sovereign jurisdiction by contract is not unconstitutional.
- *Inclusive Separation*: Investment contracts are not “international instruments”. The prohibition of Article 422 extends to Treaties and, a fortiori, to contracts. Investment contracts are not exempted from the constitutional prohibition, and, based on an integral

consideration of the articles of the Constitution, this exception cannot be presumed.

Ecuadorian legal practice appears to accept that the Constitution does not prohibit the transfer of jurisdiction to foreign arbitral tribunals via contracts. This can be seen in the large number of investment contracts that include a transfer of jurisdiction to international arbitration tribunals for the resolution of possible disputes. One consequence of this practice is that the termination of BITs, or the exclusion of the investor-state dispute settlement clause in international treaties, may have more limited effects than intended.

The relationship between Contracts and the current internal regulation, the Organic Code of Production, Trade and Investment (COPCI)

Investment contracts negotiated and signed by the state are subject to the regulations of the Organic Code of Production, Commerce and Investment (COPCI). This domestic regulation offers investors protection similar to that embodied in BITs, namely: non-arbitrary and non-discriminatory treatment, full protection and assurances, property rights, and prohibition of unlawful expropriation. It also explicitly authorizes the inclusion of international arbitration clauses in government contracts for the settlement of disputes with foreign investors.

Although COPCI includes extensive rights for investors, it safeguards the state's regulatory space to a greater extent than BITs. For example, it excludes the right to claims for alleged indirect expropriation, the most favored nation clause, and it states that tax matters will not be subject to international arbitration. It also provides for the possibility of giving certain investors, in strategic areas, differentiated treatment and incentives. But the major point of difference and innovation of the COPCI compared to BITs is the inclusion of investor obligations, such as compliance with existing national laws on labor, environmental, tax and social security rights. And, as a complement to the obligations, there are a series of corresponding sanctions in the event that the investor violates them. Another key restriction introduced by the COPCI, as compared to BITs, is the obligation for investors to exhaust domestic administrative remedies and a 6-month mediation period before international arbitration can be resorted to.

Another key restriction introduced by the COPCI, vis-à-vis the BITs, is the obligation for investors to exhaust domestic administrative remedies and to be granted a 6-month mediation period before resorting to international arbitration. The COPCI has taken some steps in this direction but could go much further. In order to recover

regulatory space through contractual means, the Ecuadorian State could include the following in any new negotiation or renegotiation of state contracts with foreign investors:

- Restrictions on rights and increased obligations for investors, such as performance clauses;
- Requiring the purchase of inputs from domestic suppliers with the importation of the investor's products;
Requirements for the participation of nationals in the management of the investee company and participation of local capital under various forms in the investee companies or corporations; and
- Technology transfer requirements.
- A clause that repeals the investor-state dispute settlement clause contained in the applicable BIT, and whereby the investor abides by the dispute settlement mechanism as incorporated and thoroughly elaborated on in the contract. This clause may provide for disputes to be settled in national jurisdiction, or incorporate a comprehensive stand-alone dispute resolution regime, including provisions on the requirements for state consent and all procedural aspects of the dispute, including the selection of arbitrators and the organization of the procedure.

17 UNCTAD (2015) INVESTOR-STATE DISPUTE SETTLEMENT: REVIEW OF DEVELOPMENTS IN 2014, IIA Issue Notes, http://unctad.org/en/PublicationsLibrary/webdiaepcb2015d2_en.pdf

18 UNCTAD (2015) INVESTOR-STATE DISPUTE SETTLEMENT: REVIEW OF DEVELOPMENTS IN 2014, IIA Issue Notes, http://unctad.org/en/PublicationsLibrary/webdiaepcb2015d2_en.pdf

19 The Commission completed its work in May 2015, notwithstanding which, an update was made on the status of the investor – state claims against Ecuador.

20 Cases Murphy I and II are antecedents of case Murphy III, therefore, only case Murphy III was taken into account when calculating amounts.

21 Ibid.

22 Ratione personae: condition that the investor making the claim be a foreigner and not a national of the State, ratione materiae: condition that the dispute be related to an investment and not excluded by the applicable BIT, ratione voluntatis: condition that the state has given its consent to arbitration, ratione temporis: condition that the facts pleaded do not predate the entry into force of the BIT whose

infringement is alleged.

23 This analysis excludes two claims (Albacora and GLP), filed after the close of the Commission's investigation phase.

24 Oxy I, Duke Energy, Oxy II, Chevron II, Perenco and Burlington.

25 United Nations Conference on Trade and Development (UNCTAD) (2012).

26 Diplomatic Cable from the American Embassy in Ecuador Canonical ID: 04QUITO2327_a, entitled "The Procurador Strikes Back at Occidental Petroleum".

27 Ibid.

28 Ibid.

29 Diplomatic Cable from the American Embassy in Ecuador Canonical ID: 04QUITO2380_a, named "Progress on Occidental Case".

30 Barker, Emily (2005) Editor's Note, Focus Europe. An American Lawyer supplement 27:6, summer.

31 Samuels, David (2006) Roundtable: the under 45s versus the heavyweights, Global Arbitration Review, Volume 1 - Issue 5, November 1, <http://www.globalarbitrationreview.com/journal/article/16467/roundtable-45s-versus-heavyweights>

32 Kapeliuk, Daphna (2010) The Repeat Appointment Factor - Exploring Decision Patterns of Elite Investment Arbitrators, Cornell Law Review 96:47, p. 77, <http://www.lawschool.cornell.edu/research/cornell-law-review/upload/Kapeliuk-final.pdf>

33 Criteria for identifying arbitrators who may be considered part of this elite includes: arbitrators who have been repeatedly nominated in the most recognized rankings published every two years by The American Lawyer magazine, or have been named as a favorite arbitrator by the Global Arbitration Review (GAR) magazine, and who have also sat on a high number of ICSID arbitrations. Other important factors include having prominent roles in international arbitration centers, teaching about international arbitration in the main training centers for investment lawyers and/or being a reference for publications on investment arbitration, and finally, belonging to international law firms or chambers specializing in investment arbitration.

34 Eberhardt, P y Olivet, C (2013) Cuando la Injusticia es negocio, TNI/CEO

35 Oxy I (Orrego Vicuna and Brower); Duke Energy (Kaufmann-Köhler and van den Berg); Oxy II (Fortier and Stern); Chevron II (Böckstiegel, Brower and van den Berg); Burlington (Kaufmann-Köhler, Francisco Orrego Vicuña and Stern)

36 Park, W. & Alvarez, G.2003, 'The New Face of Investment Arbitration: NAFTA Chapter 11', The Yale Journal of International Law, vol. 28, p. 394.

37 Ross, Alison (2010) Brigitte in Brazil, Global Arbitration Review, Volume 5 - Issue 3, 5 July, <http://www.globalarbitrationreview.com>.

38 Waibel, Michael and Wu, Yanhui (2011) Are arbitrators political?, <http://www.wipol.uni-bonn.de/lehrveranstaltungen-1/lawecon-workshop/archive/dateien/waibelwinter11-12> [citado con permiso].

39 Van Harten, Gus (2010) Investment Treaty Arbitration, Procedural Fairness, and the Rule of Law, in Schill (ed), International Investment Law and Comparative Public Law (Oxford University Press, 2010).

40 In the Burlington case, Rodrigo Orrego Vicuña was recused and in the Perenco case, Charles N Brower.

41 Ross, Alison (2010) An Interview with Yves Fortier, Global Arbitration Review, February 19.

42 3.3.7: "On more than three occasions within the previous three years the arbitrator was appointed as arbitrator by the same lawyer or law firm" (p. 25) <http://www.ibanet.org/Document/Default.aspx?DocumentUid=59C60328-61F3-4F0A-9A92-78F4F67C1C50>

43 <http://chevrontoxico.com/news-and-multimedia/2012/0223-chevrons-arbitrator-suffers-from-acute-ethical-problems>

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57 A State Contract is understood to be a contract entered into between the state, or a state entity, institution or organ, and a foreign national or a legal person of foreign nationality. One of the most common forms of government contracts is the contract for the exploitation of natural resources, sometimes referred to as a "concession contract". Cf. UNCTAD–State Contracts, UNCTAD Publications Series on Issues Related to International Investment Agreements, Geneva, 2004.

C. FOREIGN INVESTMENT AND ECUADORIAN NATIONAL DEVELOPMENT

From a macroeconomic perspective, the Commission has assessed three elements: 1) whether BITs have been determinant in attracting foreign investment and, in general, whether there is a causal relationship between the signing of BITs and the increase in investment flows; 2) whether the foreign investment that has come to Ecuador has contributed to achieving the economic and social objectives mandated by the constitution and embodied in the National Plan for Good Living; and 3) whether the results of foreign investment in the Ecuadorian economy are related to the rules established by the BITs.

This research focuses on the analysis of investment flows and their relationship with the signing of BITs, as well as on the macroeconomic effects of foreign investment in Ecuador. Collaterally, the limitations of the country's statistical system were established (some of which were derived from international technical guidelines) and recommendations were made for its improvement.

Analysis of investment flows

Both the 2013-2017 National Plan for Good Living and the 2008 Constitution state that FDI should be complementary. This is the case in quantitative terms of flows, since it is marginal, considerably less than public investment and, of course, less than national private investment. However, as explained below, over time it has come to dominate with respect to the percentage of total assets owned, machinery and equipment assets and, above all, intangible assets (such as intellectual property and resource exploitation concessions). FDI is dominant in terms of its contribution to Value Added and sales in the domestic market and while it is not yet dominant, it has also grown in the exports sector.

The results of this evaluation allow us to confirm, in the case of Ecuador, what UNCTAD and ECLAC stated in their latest reports: 1) the expectations of the 1990s when the BITs were signed were not met, 2) these treaties were not decisive in attracting FDI on a continuous basis, 3) they have been a constraint in guiding investment according to each country's development plans.

FDI to Ecuador is low

- FDI inflows to Ecuador are small relative to the Ecuadorian economy. On average, only 1.11% of GDP during the 2000-2013 period.⁵⁸ Gross Fixed Capital Formation is also less than 3% (2008-2013).⁵⁹

- Despite having more BITs than many countries in the region, Ecuador receives only 0.79% of FDI entering Latin America and the Caribbean from around the world, and it ranks 29th out of 32 countries in Latin America and the Caribbean for which ECLAC provides comparable information.⁶⁰
- The composition of FDI flowing into Ecuador indicates that half of it is due to reinvestment of profits. Although strong reinvestment is positive, these are resources generated in the country itself.

Foreign direct investment, 2002-2013 Millions of dollars

	2002-2013	Breakdown
Ecuadorians abroad		Not registered
In the country	6,937.40	100.00%
Shares and other equity investments	2,612.10	37.65%
Reinvested earnings	3,514.20	50.66%
Other capital: Credits from related companies.	811.10	11.69%

- In addition, the percentage of reinvestment compared to profits appropriated by shareholders declined sharply between 2003 and 2013. In 2013, large companies with FDI reinvested only 1.3% of their profits, whereas in 2003 they invested 5.5%. In the first years of the new millennium, the reinvestment of profits was very important, especially for FDI-holding medium-sized businesses associated with domestic businesses: in 2003, they reinvested 28% of their profits, but by 2013 only 1.3%.⁶¹
- Due to difficulties in the legislation, which does not oblige national investors to register the FDI they make outside the country, there are no Ecuadorian statistics on this matter. Based on OECD data, however, it has been found that: in the Czech Republic, data from one company of Ecuadorian origin was reported between 2008-2011; in Spain, further data from a company under Ecuadorian control was reported in 2008; and the OECD member country with the largest presence of Ecuadorian-owned companies is the United States, with three or four companies per year.⁶² This indicates

that net FDI is even lower than recorded.

- According to official data, the balance of foreign investment inflows and outflows is in deficit. Portfolio investment (i.e., in public or private bonds or in the purchase of company shares solely for financial gain) has resulted in an outflow of capital (minus USD 11,635 million),⁶³ which is greater than the inflow of foreign direct investment: 7,425 million.⁶⁴ The negative financial balance of foreign investment is even more pronounced if we consider the amounts paid for claims under BITs: a total of USD \$330.8 million in already paid legal fees and counterclaims, and a condemnatory award debt of USD \$2.632 million that has yet to be paid.⁶⁵

FDI is not a determining factor in Ecuador's economic growth

- The Ecuadorian economy has grown significantly more than the Latin American and Caribbean average (4.5%, on average, between 2001 and 2013)⁶⁶ but FDI has not been a determining factor in this growth. This can be seen in the following graph, which shows a decreasing weight as a percentage of GDP, both if we consider annual flows and if we look at the accumulated stocks for each year. This is because GDP is growing far ahead of FDI growth.
- Another indicator confirming that FDI is not a determining factor in Ecuador's growth is its relatively low contribution to Gross Capital Formation (GCF).
- Both indicators indicate that among the driving factors of economic growth, FDI is not very significant.

BITs have not been decisive in attracting FDI.⁶⁷

In Ecuador, no direct relationship has been found between investments from countries with which Ecuador has BITs and their share in the amount of FDI flowing into Ecuador.

- Only 40% comes from countries that have signed BITs with Ecuador; the remaining 60% comes from countries with which Ecuador has not signed BITs or which are tax havens.
- The two countries that invest the most in Ecuador do not have BITs with the country: Mexico and Brazil, with the third and fourth places being tax havens.
- Of the seven major foreign investors in Ecuador, only 23% of the total amount comes from countries with BITs.
- In the Latin American context, the contrast between

Brazil and Mexico supports the abovementioned findings. Despite not having any BITs or FTAs, since 1990 Brazil has maintained FDI flows, as a percentage of its GDP, at levels higher than those of many countries with BITs in force; Mexico, one of the countries with the most FTAs and/or BITs, is displaced by Brazil as the leading recipient of FDI in Latin America and the Caribbean.

ECLAC and UNCTAD agree with this analysis, and conclude that the most important determining factors when attracting FDI to a destination country vary according to the investor's primary interest.⁶⁸

For some investors, the draw lies in the search for natural resources. This is the case of the Andean region and, within it, Ecuador. The sector of the Ecuadorian economy with the highest percentage of investment flow is quarries, mines and oil; between 2000 and 2013 it amounted to 32.73%.⁶⁹ This type of FDI is heavily influenced by the rise or fall of natural resource prices. In 2010, the return on assets of the 500 largest companies investing in the mining sector in Latin America and the Caribbean was 25%, compared to 11% for beverages and tobacco, which ranks second in profitability.⁷⁰ This factor has been decisive in attracting FDI to the extractive sector.

Other investors are looking for markets. As the population's purchasing power has improved, Ecuador's domestic market has grown, attracting market-seeking investment. In fact, it is evident that companies with FDI have increased their share of sales in the Ecuadorian market.

Other investors seek preference, systemic advantages (particularly technological synergies between foreign companies interested in a country), and the contribution of the host country's own science and technology. The Ecuadorian government has made efforts to attract this type of investors, but for this reason the amount of FDI inflows remains very small.

According to ECLAC, a key factor in attracting FDI in the 1990s was privatization, which largely explains the increase in FDI flows. This coincides with the period during which BITs were signed, but does not necessarily imply a causal relationship between BITs and increased FDI.

Additional attraction factors, which have been recognized by international organizations, can be added: a) the existence of infrastructure, an area in which Ecuador has made significant progress; b) economic and political stability and public safety, aspects in which Ecuador performs better than other countries on the continent.

Consequently, public policy to attract FDI may be more effective in attracting FDI than the existence or absence of BITs.

FDI requires only clear, stable and enforceable rules, not special rights or privileges such as BITs. However, the most powerful factor in attracting investment is the perception of a successful economy.

FDI from Latin American countries investing in Ecuador (66% of the total)⁷¹ shows the importance of efforts by the continent's Southern Cone to advance integration.

Of this regional FDI in Ecuador, only 15% comes from countries that have signed BITs.

Ecuador has taken initiatives against the unfair operation of tax havens

Ecuador has refused to sign BITs with countries it considers tax havens, and rules out tax incentives for investments coming from these countries; however, FDI originating in these countries continues to be of great importance (22% of the total).⁷²

There are significant outflows of investment.

Between 2000 and 2013 the balance of portfolio investment inflows and outflows was negative USD 11,635 million.⁷³ This means that more FDI flowed out than came in (USD 7.5 billion). The data indicates that the tax on foreign currency outflows has not been enough to prevent it.

While the FDI balance is positive, there is a significant outflow of resources due to the repayment of loans between related companies. The parent companies of foreign companies investing in Ecuador have preferred to do so by means of credit between related companies, which allows them to remit resources without paying foreign exchange tax and to reduce income tax payments on profits.

As previously mentioned, reinvestment of profits continues to decline.

The extractive sector has slightly decreased as a privileged sector for FDI, but with one third of the total investment, it remains the main investment destination.

The percentage of FDI flowing into the manufacturing sector increased, but a lack of disaggregated information by branch prevented a more in-depth analysis of its impact on modernization and its contribution to the

change in the production matrix.

FDI is very significant for trade, and companies with FDI dominate large segments of both the domestic market and exports.

In the telecommunications sector, the main FDI flow comes from Mexico, but this is in contrast to a strong disinvestment from the United States. Although this is a high-technology sector, we were unable to carry out an in-depth analysis of whether or not technology transfer has been involved; regardless, it most certainly has had an impact on the country's systemic competitiveness.

The destination of investment flows in Ecuador's economic sectors shows modest changes.

Distribution of FDI by activities and its growth dynamics.

Millions of dollars.

Activity	Total periods				Structure %		
	2000 - 2013	2000 - 2006	2007 - 2013	% increase	2000 - 2013	2000 - 2006	2007 - 2013
Mining and Quarrying	2,430	1,261	1,169	-7.32%	32.73%	33.44%	32.00%
Manufacturing Industry	1,412	487	925	89.53%	19.02%	12.93%	25.31%
Commerce	1,096	440	656	48.85%	14.76%	11.68%	17.94%
Services Provided to Companies	880	411	469	13.99%	11.85%	10.90%	12.82%
Transportation, Storage and Communications	625	738	-113	115.26%	8.42%	19.57%	-3.08%
Agriculture, Forestry and Fishing	388	236	152	-35.59%	5.22%	6.25%	4.16%
Construction	352	119	233	94.87%	4.74%	3.17%	6.37%
Community, Social and Personal Services	153	56	97	73.11%	2.07%	1.49%	2.66%
Electricity, Gas and Water	88	21	66	209.62%	1.19	0.57	1.82
TOTAL GENERAL	7,425	3,772	3,653		100.00	100.00	100.00

Source: BCE.

Elaboration: CAITISA.

Effects of FDI on the economy⁷⁴

Inequality between the national productive fabric (high polarization) and the growing weight of companies with FDI.

- All the sources used agree that there is a high degree of polarization in the productive fabric. The largest companies concentrate the majority of assets, produce a large part of the value added and account for about 90% of total sales.
- Companies with FDI contribute substantially to this high level of productive polarization. While there are very few of them, they account for 18% of total production, 17% of intermediate consumption and 20% of national value added. However, they generate only 5% of employment at the national level (calculations based on an exhaustive survey of companies and economic establishments (INEC 2011)).
- Despite employing more than half of the economically active population, microenterprises produce only 16% of the National Added Value, while other national companies, with 47% of the EAP, produce 65%—calculations based on the Exhaustive Survey (INEC 2011)—.

Total assets are concentrated in large companies (quintile 5), whether domestic or FDI: around 98% in 2003, 2007 and 2013.

- Large companies with FDI have a rapidly increasing percentage share in the country's total assets: in 2003, they held 12.4% of the country's assets and by 2013 they held 32%.
 - The increase in concentration is even greater for assets held in machinery, equipment and software, which increased from 12.7% (in 2003) to 42.9% (in 2013).
 - Intangible assets (administrative rights or exploration and exploitation permits, as well as trademarks, patents, key rights, and other similar assets) increased from 37.8% to 80.3%.
 - Among intangible assets, 71.2% of patents and trademarks are owned by companies with FDI.

Trend towards foreign ownership of companies.

Between 2003 and 2013, the number of foreign-owned companies grew at an annual rate of 7.3%. This exceeded the growth rate of domestic companies (3.1%) and, by 2013, the number of foreign companies accounted for 13.1% of the total.

By 2013, the average foreign ownership in associated companies (less than 50% held by foreigners) stood at

36% (in 2003 it was 32%) while in subsidiaries (controlled by foreign capital) the increase is much higher, rising from 76.8% in 2003 to 92% in 2013.⁷⁵

The two previous elements indicate that, between the years 2003 and 2013, there has been a strong foreignization of the shareholding ownership of companies operating in Ecuador.

Growing dominance of companies with FDI in economic sectors.⁷⁶

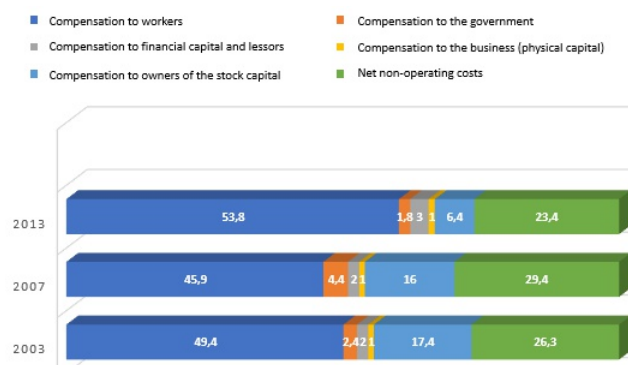
- The value added produced within the Ecuadorian economy is increasingly dependent on companies with foreign shareholdings. It increased from 19.8% in 2003 to 40.1% in 2013; not at odds with the previously noted modest contribution of FDI to the economy.
- In 2013, we found 17 sectors in which companies with FDI produced more than 50% of sector value added.
- Companies with FDI increasingly dominate the market. In 2003, they accounted for 17.9% of total sales and by 2013 they account for 40.1%. Subsidiaries (mostly foreign-controlled) have shown the greatest growth. Of these 17 sectors, nine belong to the manufacturing industries section and four to the transportation, warehousing and communications section. In the extraction of crude oil, natural gases and related products, subsidiaries account for 63.8% of the sector's value added.
- In general, the value added of subsidiary companies dedicated to manufacturing has its highest share in the food, beverages and tobacco sector; additionally, from 2003 to 2013, a reduction in the share of value added by companies in medium and high technological intensity manufacturing sectors can be observed. This was compensated by an increase in the share of companies in the value added created by medium and low technological intensity manufacturing companies.
- The participation of foreign companies in the domestic market is of increasing significance. In 2013, subsidiary companies (mostly foreign), in 2013 had a market share of more than 60% of total sales in 12 economic sectors (mainly manufacturing), including the tobacco sector, in which the subsidiaries' sales accounted for 100% of total sales. This means that they are gaining an increasing share of the market from domestic companies.

The external market is dominated by domestic companies (partially due to the recovery of the public sector from oil exports); but the weight of companies with FDI in exports is growing.

Distribution of added value

Companies receiving FDI are generally more capital-intensive than domestic companies; this was found (by comparison of averages) in 51 of the 56 economic sectors, according to the ISIC3 classification. The labor productivity of subsidiary companies is consistently 1.5 times higher than that of domestic companies. However, the distribution of this value added among production factors is distinct between FDI and domestic firms. The following table summarizes the basic data of this distribution. We will be able to draw certain conclusions from this.

Average compensation by factor of production (all companies), 2007-2013



Source: SRI.

Elaboration: CAITISA.

Total participation of production factors in Added Value, 2013

Compensation for Factors of Production	National	Associated	Subsidiaries
Compensation to Workers	56.1%	57.5%	47.8%
Compensation to Government	0.3%	1.3%	1.8%
Compensation to Financial Capital and Lessors	0.1%	3.7%	3.6%
Compensation to the Company (physical capital)	0.6%	2.9%	2.1%
Compensation to Shareholders	15.1%	16.4%	20.7%
Net Non-operating Expenses	27.9%	18.2%	23.9%
Total	100.0%	100.0%	100.0%

Source: SRI.

Elaboration: CAITISA.

Employee participation in added value

- In all types of companies, the majority of value added is appropriated by workers; this is significant and is at a higher percentage than in many countries in Latin America and the Caribbean. In addition, when considering all the companies operating in Ecuador, participation has improved over time in favor of the workers. In 2003 it was 47.9% and by 2013 it had increased to 55.2%.
- However, it is the subsidiaries (the largest and most controlled by foreign capital) that leave the lowest proportion of value added to their workers: eight points less than domestic companies. That is to say that, in relative terms, they pay less. In other words, the result of their increased productivity is primarily beneficial to shareholders.

Shareholder participation in added value

- In contrast, the proportion of added value appropriated by shareholders of subsidiary companies tripled from 2003 to 2013, from 7.3% to 20.7%. Even the shareholders of the subsidiary companies in quintile 5 (the largest) appropriate 23% of the value added. This is considerably more than national companies of similar size, which in 2013 appropriated 16.9%.
- We have already said that an important part of FDI in Ecuador is the reinvestment of profits. This is particularly true for companies with less than 50% foreign ownership and only in the first stage. As they grow and consolidate, they obtain the resources to do so from their operations in Ecuador, but, in a second stage they no longer do this, instead reemitting resources from abroad. The largest foreign companies reinvested only 3.9% of their profits in 2003, and 1.7% in 2013. This is in spite of the incentives that Ecuador grants to companies that reinvest and the tax on foreign currency outflows.
- In 2013, subsidiaries remitted around USD 3,822 million in profits; it is worth noting that this annual amount is about half of the inward foreign direct investment recorded in the last ten years.
- Another part of the added value goes to financial capital. In 2013, the figure for subsidiary companies was 3.6%; in companies in the 5th quintile, it was 5.3%. However, we should highlight that part of the

FDI is credit between related companies, meaning that part of this remuneration to the financial capital goes to the shareholders themselves.

Government participation via taxes on value added

- This is the only portion of value added in which foreign-invested companies contribute more than domestic ones. In 2013, domestic companies left 0.3% of the value added they generated in the hands of the government (associates 1.3% and subsidiaries 1.8%). In 2013, domestic companies left 0.3% of the value added they generated in the hands of the government (associates 1.3% and subsidiaries 1.8%). Moreover, with every passing year they contribute a smaller percentage of this value added to the government: in 2003, subsidiaries contributed 2.3%, and by 2013 this had dropped to 1.8%.

FDI companies in their relationship with the rest of the productive framework

- Due to lack of adequate information, we were unable to carry out an in-depth study of the economic relationships between companies with FDI and the rest of the national economy. The Comprehensive Survey of Businesses and Establishments (INEC, 2011), however, provides the following general information: FDI companies have less and less productive ties within the country. During 2006, these companies used 56.4% domestic inputs relative to total inputs; by 2010, their consumption of domestic inputs had fallen to 52.5%. On the other hand, domestic companies have increased their production chains within the interior of the country. During 2006, they consumed 45.7% of local intermediate products and in 2010, this rose to 58.9%.
- There are indications that FDI firms' large holdings of technological assets have not been transferred and have not contributed to modernization of the productive structure.

FDI and job creation

There are various types of difficulties in studying the relationship between FDI and employment, and these are not exclusive to Ecuador.⁷⁷ However, with the use of various sources and methodological resources, it was possible to establish the following:

FDI companies generate little employment, but it is increasing. Of the total number of jobs in the country (including informal jobs), FDI companies accounted for only 2.9% in 2007, but this proportion had grown to 9.6% by 2013.⁷⁸

FDI companies are, for the most part, capital intensive, and therefore generate very little employment per million dollars invested. Calculations based on different sources give similar numbers.⁷⁹

– Analysis from SRI records shows that for every US\$1 million of FDI, an average of 1.48 direct jobs were created annually (between 2007 and 2013). Indirect employment could not be calculated.

– Estimates made by Intelligence, from the Financial Times (FDI),⁸⁰ based on information from foreign investment announcements, said they would create an annual average of 2.6 jobs per million dollars invested, from April 2003 to June 2014.

– Based on information from ECLAC and on FDI, compared to the rest of Latin America and the Caribbean, Ecuador ranks 16th out of 26 countries for the indicator of jobs generated per million dollars invested.⁸¹

– ECLAC analyzes the various employment-generating capacities of FDI by economic sector and concludes that the extractive sector—where one third of FDI in Ecuador is located—has the least capacity to generate employment.⁸²

This is not to say that jobs created by FDI are not important. If we consider only formal employment (not including employment generated by companies or individuals registered with the SRI as RISE), in 2007 there were eight sectors (according to the CIUU 3 classification) in which FDI generated 20% or more of employment in the sector. In 2013 there were 12 sectors with FDI that accounted for 40% or more of sectoral employment.

FDI and the quality of employment⁸³

Few indicators are available regarding the quality of employment generated by FDI firms compared to domestic firms.

The key indicator—i.e. salary level—is noted below.

Average monthly compensation by type of company

Quintiles by Total Assets	Year 2007		Year 2013	
	National USD	Foreign USD	National USD	Foreign USD
Quintile 1	198	269	19.629(1)	153
Quintile 2	327	518	426	593
Quintile 3	347	310	502	619
Quintile 4	371	464	520	694
Quintile 5	773	867	818	954
Total	639	795	733	932
Annual Growth Rate 2007-2013			2.3%	2.7%

Source: Internal Revenue Service. Form 101 and 107, years 2007 and 2013.

Elaboration: CAITISA.

- FDI firms have higher average productivity per worker than domestic firms. As a result, they pay higher average wages per worker than domestic firms. This higher productivity, however, does not flow proportionally to workers' salaries; in fact, in terms of the value added generated, they pay their workers less than domestic companies.
- Depending on their size, both domestic and foreign companies pay better. Companies in the fifth quintile are the best payers.
- The annual growth rate of average compensation per worker is very low in both domestic and foreign companies (2.3% and 2.7%, respectively).
- There is a wide disparity in remuneration depending on the sector in which one works. There are several sectors and/or years in which domestic companies paid better wages than foreign companies.⁸⁴
- Naturally, according to ECLAC, the wages paid by FDI companies in Ecuador are lower than those paid in their parent companies. This can be seen in the following graph.
- Other indicators on the quality of employment
 - According to World Bank surveys,⁸⁵ FDI companies have more permanent employees than domestic companies.
 - According to these same sources, workers in national and foreign companies have similar levels of training.

- There is not sufficient information⁸⁶ to analyze the differences between domestic and foreign companies in terms of gender policies, but the WB surveys provide the following, very general, information.
 - Compared to foreign companies, domestic companies have a higher percentage of female employees, but in both cases these percentages decrease over time.
 - Foreign companies have a slightly higher percentage of female managers.
 - Both types of companies have similar percentages of women among their workers and in both cases this percentage is increasing.

The national statistical system on foreign investment

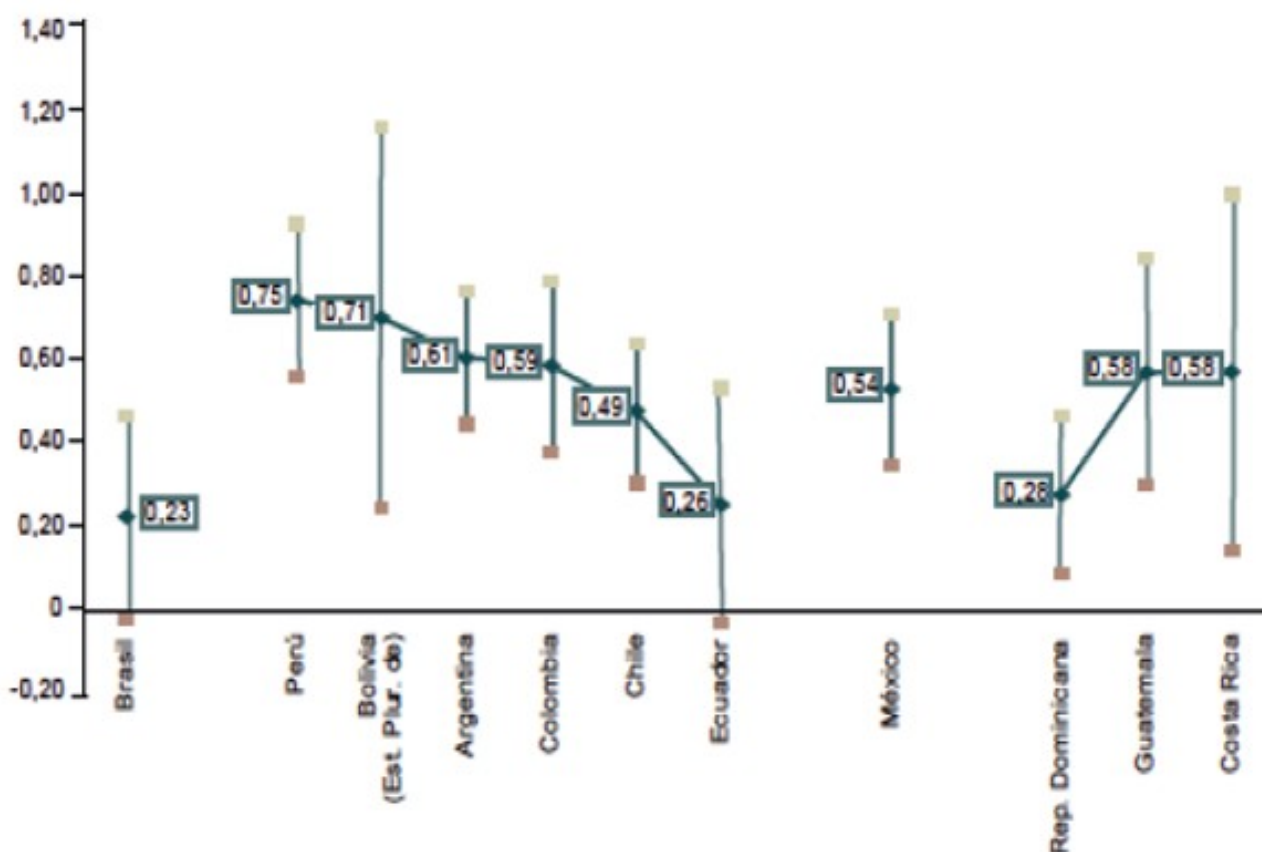
Foreign investment statistics, which are based on the application of IMF balance of payments manuals, do not provide sufficient information to quantify FDI's impact. They focus on investment inflows and outflows rather than the characteristics of these investments, which are indispensable for analyzing the socioeconomic and environmental effects of these investments from a development perspective.

No statistics have been found that were designed to study the behavior of foreign interests in the business network and the macroeconomic results of their investments. There is scattered information in various agencies, with different methodologies and definitions of statistical classification that are not comparable with each other. Statistics from various institutions need to be better integrated and coordinated.

Statistical records are lacking in three areas: a) investments by Ecuadorians abroad; b) FDI flows that allow us to distinguish new investments versus those that are purchases or mergers of existing companies; and c) statistics that provide a detailed analysis of production linkages.

There is an urgent need for studies and statistical sources on other investment flows, which cover the broad spectrum of types of investment protected by BITs, especially illicit outflows, which are a huge drain on developing economies.

Latin America (11 countries): wage gaps between local companies and subsidiaries of transnationals, 2010a, b



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of World Bank, Business Surveys.

a Gaps and 95% confidence intervals.

b Ordinary least squares (OLS) estimation of the logarithm of wages.

58 CEPAL CEPALSTAT database. Statistics and Economic Indicators/External Sector.

59 SENPLADES calculation.

60 CEPAL CEPALSTAT database. Statistics and Economic Indicators/External Sector/Net Foreign Direct Investment.

61 Calculated by Consultora Económica- Centro de Investigación Cuantitativa (hereinafter Consulting Team) based on information from the Internal Revenue Service ("Servicio de Rentas Internas", SRI), Forms 101 years 2003, 2007 and 2013 (SRI); Shareholders Annex 2013 (SRI); Information on participation of foreign shareholders in Ecuadorian companies: 2003, 2007 and September 2014 (Superintendency of Companies).

62 OECD's Activity of Multinational Enterprise (AMNE) database.

63 Central Bank of Ecuador, Balance of Payments ANNUAL BULLETIN # 33 of 2011 and # 36 of 2014.

64 Central Bank of Ecuador: Balance of Payments

65 CAITISA calculation based on official information.

66 Calculation based on Central Bank; Retropolation 1963 - 2007, Yearbook Bulletin No. 36 and Bulletin No. 1953 of November 2014.

67 All the information in this section was calculated based on balance of payments information from the Central Bank of Ecuador. To avoid distortions, we only list countries according to whether or not they have BITs with Ecuador; separating out the countries of origin that, while Ecuador has not signed BITs with any of them, are tax havens.

68 CEPAL (2012) La Inversión Extranjera Directa en América Latina y el Caribe 2011. Cited edition, p. 114-116.

69 Calculation based on information from the Central Bank of Ecuador.

70 ECLAC taken from América economía, December 2011 <http://www.americaeconomia.com/>

71 Calculation based on FDI information from the Balance of Payments provided by the Central Bank of Ecuador.

72 Ibid.

73 Central Bank of Ecuador, Balance of Payments ANNUAL BULLETIN No. 33 of 2011 and No. 36 of 2014.

74 Four sources were used for this analysis: a) the Administrative Records of the Internal Revenue System (SRI); b) World Bank Enterprise Surveys; c) the OECD's MNE Activity Database, and d) the Comprehensive Survey of Enterprises and their Establishments (2011) conducted by INEC and linked to the 2010 Census.

75 Calculation of the Consulting Team based on Form 101 years 2003, 2007 and 2013 (SRI); Annex of shareholders 2013 (SRI); Information on participation of foreign shareholders in Ecuadorian companies: 2003, 2007 and September 2014 (Superintendency of Companies).

76 In sections 3 and 4 below, the percentages are overestimated because they do not include the informal sector of the economy, not even companies registered with the SRI as RISE, since all companies in this sector are national. This does not invalidate the conclusion regarding the high concentration of large companies and the weight of companies with FDI in the national economy; it would only modify the percentages, as confirmed later with information from the Comprehensive Survey of Companies and Establishments, which includes microenterprises.

77 Traditional statistics, in both Ecuador and around the world, do not allow for a calculation of the direct generation of jobs through foreign direct investment. However, in CAITISA, based on the information provided to the IRS by each company, forms 101 and 107, we were able to estimate them. The problem with this source is that it only captures formal employment. There are other sources: the IESS also captures only formal employment but also includes those in the RISE regime. The ENEMDU household survey has the advantage of capturing absolutely all employment, but it does not allow classification by sector, nor does it distinguish between companies with FDI and domestic companies. The ENEMDU was used as the source to calculate the share of FDI companies in total employment in Ecuador.

The comparison between Ecuador with the rest of Latin America and the Caribbean used information from ECLAC (Foreign investment in Latin America and the Caribbean 2006, 2012, 2013 and 2014), World Bank surveys (International Finance Corporation - World Bank. Enterprise Survey. <http://www.enterprisesurveys.org> enterprisesurveys@worldbank.org) and the FDI Intelligence database, from the Financial Times Ltd. 2014.

The qualitative analysis of average remunerations and distribution to the labor factor of the gross value added generated by foreign companies is based on information from the SRI.

78 Calculations made based on SRI records for jobs generated by FDI companies, weighting jobs created with the percentage of foreign participation in the companies. The total number of jobs (including informal ones) is provided by ENEMDU.

79 We should point out that since all companies with FDI are formal, the SRI is an adequate source.

FDI Intelligence, from the Financial Times Ltd 2014. In the case of Ecuador, this database is located in SENPLADES.

80 FDI Intelligence, from the Financial Times Ltd 2014. In the case of Ecuador, this database is located in SENPLADES.

81 La Inversión Extranjera Directa en América Latina y el Caribe 2013 Chapter III, p. 138.

82 Ibid.

83 To analyze the quality of these jobs, two variables were compared between FDI and similar national companies (quintile 5): salary and worker training. The average salary was calculated based on information from the SRI. Information on percentages of full-time employment and training was taken from both World Bank and FDI enterprise surveys.

84 The detailed analysis by sector can be seen in the full report.

85 International Finance Corporation - World Bank. Enterprise Survey. <http://www.enterprisesurveys.org>, enterprisesurveys@worldbank.org.

86 Further information is provided in the full report based on the following sources: International Finance Corporation - World Bank. Enterprise Survey,

<http://www.enterprisesurveys.org> enterprisesurveys@worldbank.org.
Todaro, Rosalba (2003). El impacto laboral de la inversión extranjera directa: la importancia de análisis de género. In Economía y género: Macroeconomía, política fiscal y liberación. Análisis de su impacto sobre las mujeres. Paloma de Villota (ed.): 387-404. Spain: Icaria Editorial S.A. Mancero Piedad (2013) "Visibilización de género en las tendencias macroeconómicas". In Revista Análisis Económico No 25 Cambio de la matriz productiva. Quito: Association of Economists of Pichincha. Garcia, Juan Carlos and Patricia Cortez (2012). "Análisis de la participación laboral de la mujer en el mercado ecuatoriano". In Analítika, Revista de análisis estadístico, Vol. 4(1): 23-49. INEC: Quito.

D. SOCIOECONOMIC, MACROECONOMIC, HUMAN RIGHTS AND ENVIRONMENTAL IMPLICATIONS OF INVESTMENTS MADE BY COMPANIES THAT HAVE FILED CLAIMS AGAINST ECUADOR

Economic and geographic sectors where companies are located

Most foreign investment companies that have brought lawsuits against Ecuador in international arbitration tribunals are in the natural resource exploitation sector, with a predominance of hydrocarbon companies. This activity has attracted the majority of private foreign resources over the last four decades, drawn by high business profitability and a domestic policy of concessions and guarantees, which were later reversed against the country's interests.

The location of these companies' investments has allowed to situate and orient research, both in territorial space and in the time of business operations and, in particular, to determine the corresponding area of influence, which has caused economic, social, ethno-cultural and environmental impacts.

The area of influence covers not only the areas of the concessions and operations, but also the natural ecosystems and the elements of subsistence and coexistence of the surrounding populations. For the economic and social analysis, in the best of cases, the available information is at the parish level, which is the smallest territorial unit. In accordance with the current Political Administrative Division, the location of the respective companies has been identified, considering, for these purposes, the parish level as the area of influence.

As shown in the table below, this section presents an examination of the 24 cases of claims filed against Ecuador invoking BITs in effect, and four additional cases of claims filed before international tribunals involving contracts signed between the Government of Ecuador and foreign investors; therefore, the inclusion of contracts may differ, to some extent, from point II.2 of this Report.

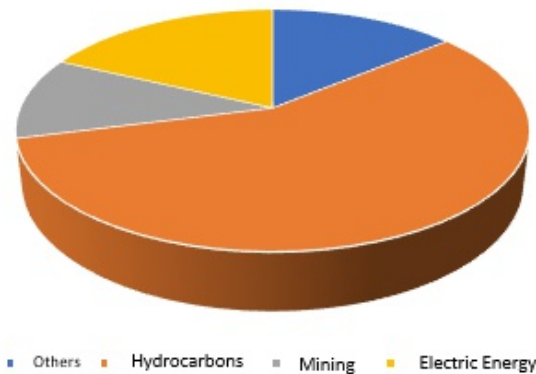
Classification of companies and cases of lawsuits filed against Ecuador

Sector / Activity	No. of Companies	No. of Cases	Location / Area of Influence	Conflict Situation
Hydrocarbons	10	16		
Oil Exploitation and Export	9	15	Amazon / Blocks Under Concession	6 Open 9 Concluded
Refinery	1	1	Esmeraldas / Project	Completed
Electrical Energy	5	5		
Infrastructure	1	1	El Oro / Machala	Completed
Acquisitions	1	1	National	Completed
Provision of Services	3	3	Guayaquil / Pichincha	3 Completed
Mining	3	3		
Concessions	3	3	Napo / Zamora / Imbabura	3 Open
Other	4	4		
Infrastructure	1	1	Pichincha / Quito Metropolitan District	Completed
Offer of Goods and Services	3	3	National / Others	1 Open
TOTAL CASES	22	28		10 Open 18 Completed
Cases with BIT	20	24		10 Open 14 Completed
Cases with Contract	2	4		4 Completed

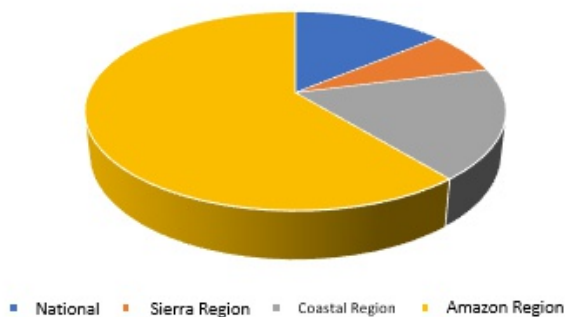
Source: State Attorney General. Elaboration: CAITISA.

Of the 28 lawsuits (Table 1.1), 16 are from the oil sector, 10 of which correspond to parent companies, some with subsidiaries that have been involved in the lawsuit; the number of companies is lower than the number of cases since several filed more than one lawsuit. With the exception of the Spanish company TécnicasReunidas S.A., which was involved in the Esmeraldas Refinery, the 15 cases were related to operations in blocks and concessioned fields in the Ecuadorian Amazon.

Lawsuit cases
Lawsuit cases by sector



Demands by Geographic Areas



Source: State Attorney General.

Elaboration: CAITISA.

Because the greatest degree of human intervention occurs in areas of abundant natural resources covering vast expanses, tangible impacts include sensitive ecosystems that are home to ethnic minorities, flora, fauna and wetlands of invaluable importance.

The second group of lawsuits relates to the electricity sector. In terms of companies' scope of action, as a result of contracts entered into with the sector's governing institution, there is one case with a national scope; the other four cases cover the Guayas province, principally the city of Guayaquil, and El Oro (an area of gas exploitation for energy production).

The energy sector is followed by the mining sector, with three companies that have filed lawsuits. They have local concession areas: two in the Amazonian provinces of Napo (Pungarayacu) and Zamora (Nambija), and one in Imbabura (in the north of the country).

The remaining four cases correspond to an equal number of economic sectors: IT services (IBM), airport infrastructure (Quiport), telecommunications (Globalnet), and pharmaceuticals (MerckSharp&Dohme). Its scope of action has been national, and local when dealing with air transportation.

Economic and social impact: primary indicators

Economic evolution

Provinces that significantly expanded their production in the nineties are those in which oil fields are located. This is a clear consequence of the investments made in this sector, the only sector that, at that time, attracted the interest of foreign companies.

For the 2007 to 2010 period, the Central Bank provided more detailed information on production levels by canton, which are smaller jurisdictions, and which may have been zones of influence of the operations of the companies under investigation. Oil and non-oil accounts were also available. During this period, a trend emerged that was still related to oil activities, though the companies with the broadest operational scope that were in litigation with the country had already left their area of intervention. There are also cantons such as Esmeraldas (where the refinery is located), Tena and Joya de los Sachas, where ties to oil production have resulted in a low growth or deterioration in production levels; on the other hand, non-oil production in the same three cantons has increased significantly.

In the cantons of Lago Agrio, Putumayo, Cuyabeno and Orellana, total production levels, including oil production, grew significantly between 2007 and 2010. During this period, Petroamazonas, a public company that also carries out social development projects and activities and offers productive opportunities to the local population, was in operation.

Employment

In the sectors where the majority of the foreign-invested companies audited are located, the creation of employment has been low due to the limited human resources involved in the activities in question. The National Employment Survey for June 2011 proves the foregoing: the oil sector generated only 0.53% of the

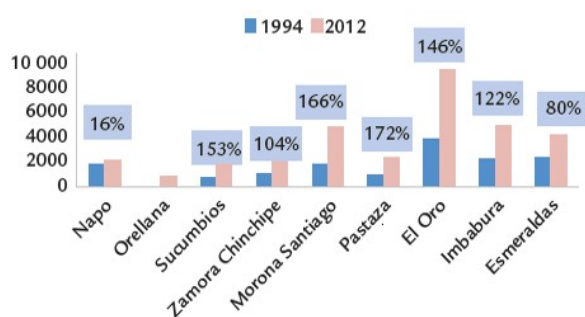
Economically Active Population (EAP), in spite of its weight in the Ecuadorian economic structure. Of this indicator, 94.7% were men and 5.3% were women. Another sector, to which five of the audited companies belong, is the electricity, gas and water sector. It also contributed only 0.49% of the EAP, again with low participation by women. In 2005, an average outsourcing rate of 10% was found in 15 of the companies investigated; since 2008, this practice has been eliminated by constitutional mandate.

In the Ecuadorian Amazon, employment indicators are still unfavorable for the female population. According to the INEC (2013), female unemployment was 6.1%, underemployment or inadequate employment was 43.6%, and gross underutilization was 55.1%.

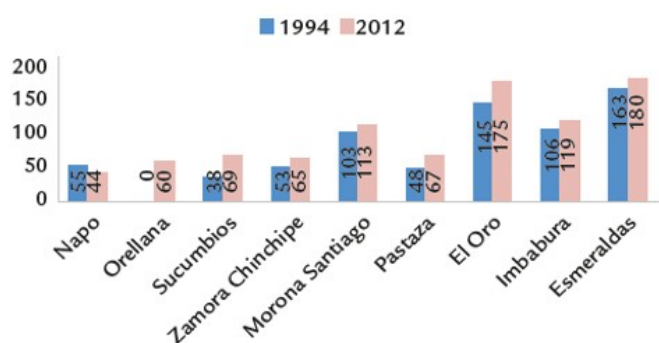
Education and health

As regards education and health, the following graphs show developments in the provinces where the companies under review are located.

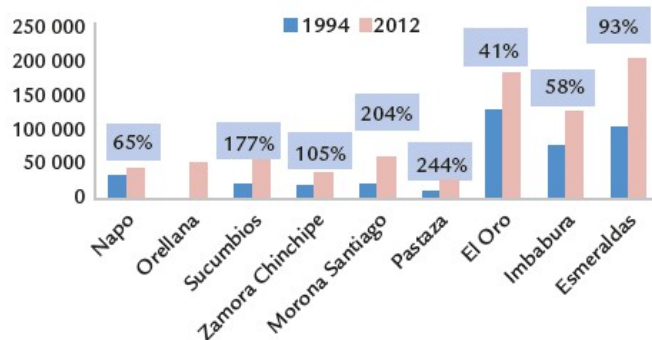
Health-Incidents



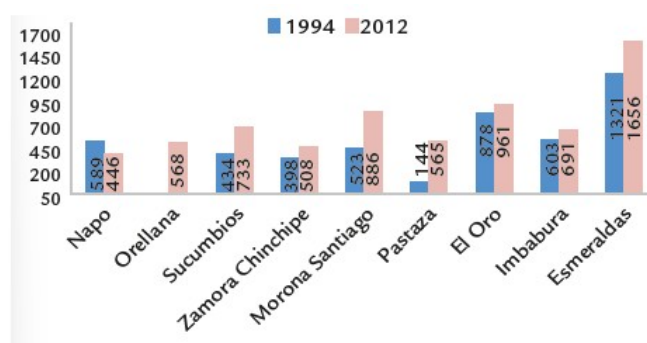
Health-Establishments



Health-Students



Health-Establishments



The increase in the student population (between 1994 and 2012, the period in which foreign investment is assumed to have had an impact) is high in the Amazonian provinces due to two factors unrelated to company operations: starting from incipient levels in 1994, with the greatest dynamism occurring in recent years, around 2012.

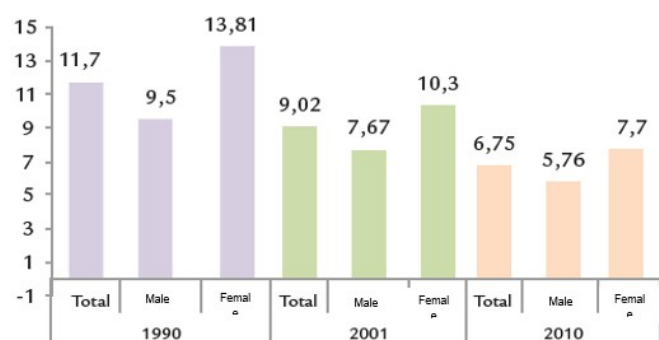
In health, the term morbidity includes diseases related to activities carried out by foreign companies in the extractive sector: contamination of potable water, hygiene, air quality, and malnutrition, among other factors.

Illiteracy

In the list of cantons examined in the last three censuses, in most cases, illiteracy rates have declined, but they are still unsatisfactory and even alarming in some cantonal jurisdictions, especially among the female population. In 2010, the highest rate was recorded in Cotacachi canton—both among men (15.05%) and women (22.35%)—an area where mining companies operate. Though it has declined somewhat since previous decades, this is due more to the state's educational efforts than to a contribution from the aforementioned companies.

In 2010, there were illiteracy rates of between 10% and 19% in the female population in places where oil activities have been carried out, though all were lower than those of 1990 and 2001. At any rate, the possible influence of foreign companies on this reduction is very limited, as the educational projects they implemented were located in territories very close to their locations, and were by no means extensive in their areas of influence.

National Illiteracy Rates



Source: National Information System.

Elaboration: CAITISA.

Rates of access to basic public services

The 20 cantons where the companies in question have established themselves exhibit fairly heterogeneous conditions of social development.

In 1990, in Quito alone, only 60% of households had access to public water, sewage, garbage collection and electricity services. Guayaquil followed, with an indicator of 47%. The other cantons reached 28%; in rural areas the highest percentage was 17%, even in the canton of Quito.

According to the 2001 Population and Housing Census, indicators of access to the aforementioned basic services showed positive but very irregular changes. The cantons of the Amazon region remained at a precarious level; despite providing valuable oil resources, most urban dwellings lacked the aforementioned water, sanitation and electricity services, which were even less accessible in rural areas, where only one house out of every 100 had those services.

By 2010, the situation in each canton's urban area had changed significantly. Most of the cantons, including those in the Amazon region, had indicators above 50%. Clearly, the impulse came from the policies and financing of the central and sectional governments, which have prioritized projects to provide the population with basic services, and not from the investments of transnational oil companies; in rural areas, where these companies operated, there is

still a lack of services.

In the Amazon region, there are very few homes with a piped water supply. In 2010, there were cantons in rural areas where only two out of every hundred homes had piped water. On the other hand, it is evident that electricity service in homes has been improving since 1990; by 2010, in the urban areas of all the cantons surveyed, coverage exceeded 90%. In the rural areas where oil projects were carried out, a significant portion of the homes still lack electricity.

Poverty in times of increased foreign investment and its subsequent evolution

In the cantons whose population was exposed to the effects of foreign investments, the indicators of poverty based on Unsatisfied Basic Needs (UBN) show surprisingly high levels of households lacking basic services, including basic health and education. In 1990, most cantons fluctuated around 90%, with only Quito having an unsatisfactory rate of 59% and Guayaquil 70%. In 2001, there were cases in which the percentage of households with insufficiencies dropped slightly, but remained high, especially in Amazonian cantons, where poverty rates were higher than 80%.

By 2010, as of the date of the last Population and Housing Census, conditions had improved in all of the cantons surveyed. However, in areas where oil activity had taken place, more than two thirds of the inhabited households lack basic services.

Incidence of Income Poverty

Poverty by income level (related to consumption capacity) that afflicts the country's population has been measured based on the Urban Employment and Unemployment Surveys conducted by the National Institute of Statistics and Census (INEC). Using a homogeneous methodology, figures are provided by tranches, between 2006 and 2013, with a breakdown by provinces for the Coast and Highlands, and aggregated solely for the Amazon region. The following table shows the results obtained by selecting locations where the investments of companies subject to this audit took place:

	2006	2010	2013
Amazon Region	45.7	48.6	35.6
El Oro	32.4	24.6	17.5
Esmeraldas	59.7	51.3	46.1
Guayas	34.6	26.2	23.2
Imbabura	41.4	37.3	28.5
Pichincha	17.7	16.5	9.1
NATIONAL	37.6	32.8	25.6

Source: National Institute of Statistics and Census.

Elaboration: CAITISA.

Impacts on community life, land tenure, food security, displacement and conflicts

Contact with community leaders, social organizations and affected people made it possible to confirm the effects on the enforcement of human rights and on the natural environment. These include: disruption of livelihoods, displacement of communities from their territory, deceit and non-compliance with commitments, provoked internal social conflicts, omission of information and prior consultation, concealment of damages, inaccurate, disregarded and unevaluated environmental impact studies.

Land holdings

By signing the Agreement and Code of Conduct, the Secoya nationality committed itself to the oil company OXY to receive compensation in the exploration phase, which implied a waiver of claims for environmental damage suffered in subsequent phases, despite the fact that the relevant Law has contemplated claims regarding the Management Plan, with criminal implications and the right to reparations and civil indemnities.

The same agreement establishes compensation of USD \$700,000 to be delivered in different periods of the exploration phase, according to proven well performance (USD \$600,000 was actually delivered, despite the fact that the exploitation phase had begun). For this amount – which is not related to the benefits received by the business owners – the company used material goods (wood, water), made use of the land and rights of way, without having contemplated payments for acquisition or for land leases; nor was it obliged to pay surface rights, having signed a participation contract.

The possession of land in oil production areas, as a result of the Hydrocarbons Law, has not recognized the property rights of communities and peoples of ancestral places. Therefore, neither the State nor the private companies that own it have applied procedures for declaring the land as public property and the corresponding payment or compensation.

In short, the numerous agreements and codes of conduct signed, especially in previous decades, have been used by oil companies as a means of control, appeasement and omission of human and collective rights, which has brought them economic advantages; they even committed themselves to replacing the State in environmental and social responsibilities and obligations, undermining people's access to official bodies. Due to the lack of legal clarity and consistency in land ownership, several farmers displaced from their plots continue to pay property tax on these invaded lands, since the respective Municipal Cadastre does not record any expropriation or declaration of any public utility.

Evidence of damage and testimonies collected in field work

Summary of testimonies

The audit investigation team traveled to oil blocks 12, 15 and 7, where the companies OXY and Perenco operated, the latter in consortium with Burlington, in the provinces of Sucumbíos and Orellana. Also, to the fields of intervention of Texaco (later Chevron) in the Aguatico area, Lago Agrio canton, towards areas of action of the companies Petrobras, Perenco and Texaco (this time the Sacha field, in the Joya de los Sachas canton), in the provinces of Napo and Orellana. In these places it was possible to collect the following testimonies (summary version) from affected residents:

- Minimum payments for land use. Compensation works are incipient, many of them incomplete, non-functional, only for the nearest community; clashes between communities occur due to this cause.
- Housing was offered in exchange for land; the land was handed over and the company did not build the housing. The leader loses credibility, which leads to the devaluation of his word and the affectation of good faith, an important factor in community relations.
- Information restricted and manipulated to suit companies. Inexperience and lack of knowledge of residents to demand rights.
- Precarious labor relations and hiring for works without legal benefits, all for very few residents. No training or efforts to improve the qualification of the workforce or reach any level of professionalization.

- Contracts for road cleaning, transportation and others, at a loss.
- From being landowners, they become, in some cases, day laborers dependent on oil work. Customs are degraded, begging and blackmail appear; traditional work and ancestral knowledge are rejected.
- Alcoholism; traditional drinks are replaced by beer, and high dependency is generated.
- Generator noise causing deafness.

Individual versions and testimonies in areas of two companies visited:

Petrobras. In the Kichwa Guataracu community, of considerable extension, made up of five sectors (Centro, Pukuna 13, Selva Alegre, Río Salvador and VenadoYaku) it was possible to hold discussions in meetings held with community leaders, from a pre-cooperative, with the school director, the political lieutenant and other participants, about economic and social relations with the Petrobras company. The testimonies give an account of the contributions made by the company and the non-compliance and problems generated. There was integrated management in health aspects (medical brigades, health posts, training for promoters) and in education areas, with delivery of school materials, food, transportation and small works such as fencing and classrooms; teachers were also trained in computing.



Interview to Guillermo López- Director of the “Imbabura” school located within the “Huataracu” community and Miguel Grefa.- President of the Parents' Committee.

Regarding **job creation** and hiring, it is reported that the company used outsourcing companies; in other cases, it coordinated with the community leaders and defined the people to be hired: *“With Petrobras, an assembly was held when the company needed personnel, and in the assembly the best people responsible for the work were sought, and they were sent to work,*

always coordinated with the management” (Grefa, Miguel. Personal interview. Sep. 16. 2014)

Another testimony recounts *“There were conflicts between communities because the issue of employment benefited some more than others.”* (Andrango, Rafael. Personal interview. Sep. 15. 2014) *“At that time, they worked 14-14 and paid \$240 for 14 days, and they didn't pay any kind of social benefits.”* (Bravo, Hermel. Personal interview. Sep. 15. 2014).

They also claim that the company left pending accounts by not delivering profits and other benefits; there are lawsuits to collect profits.

Community relations were, in general, through **agreements signed** in which the company agreed to compensate for physical damage and to carry out works as social compensation. There are different versions about the degree of compliance. Petroamazonas professionals consider the level of achievements to be high, but local residents also cite standstills and demands, due to delays and provocations.

One of these agreements—signed between the company ECUADORTLC S.A (the Ecuadorian subsidiary of Petrobras) and the Pre-cooperative Unión Alamoreña, under the name Agreement for Compensation of Petroleum Activities—mentions the works and donations of community benefit that the company undertakes to execute. It also indicates that the Pre-cooperative is obliged not to request any additional increase or compensation, as well as the contribution of unskilled labor, based on community mingas, for social and human development works and projects. *“With Petrobras we have gone on strike over the issue of the expansion of the road, we as the first users of the road, have gone on strike for the advancement of the road, so that it continues to advance and benefits all families”* (Grefa, Miguel. Personal interview. Sep. 16. 2014)

There were also training workshops for residents, especially women: *“With Petrobras there were several training workshops for women in cooking, cutting and sewing, there was also a bakery workshop here, all of which has been done with the women. These trainings were followed with this company”* (Grefa, Miguel. Personal interview. Sep. 16. 2014).



Interview to Hermel Bravo, President of the Alamoreña Union Pre-Cooperative – San Juan Parish

"I have heard of many people from the surrounding communities who were given food without working, and when we (Parroquia 3 de Noviembre) had to work and sacrifice ourselves to be able to eat" (Andrango, Rafael. Personal interview. Sep. 15. 2014)

The company managed agricultural development plans. *"Petrobras provided support to the fish farming and poultry farming community, there were cocoa, coffee, banana plantations, etc. Within that we had an agricultural development plan with all the communities, where we bought all the products that were produced on their farms and were sold to the company as part of their food." (Caicedo, John. Personal interview. Sep. 15. 2014)*



Interviews to Moses Irumenga. President of one of the Huaorani Communities, located in the Chontapunta Parish. (September 18, 2014).

Perenco. In block 21 (Yuralpa) the observations corresponded to the company Perenco, which operated until 2009. Testimonies were obtained from native inhabitants and settlers, all members of the communities,

and from the director of the local school.

In **labor aspects**, the company employed workers through contractors, for a limited time, under the following modality: *"Perenco only hired workers from contractors and for a limited time. They asked us for 20 workers for 8 communities, and we had to work two for each community, and that was detrimental because there were even conflicts between the communities."* (Tapuy, Ricardo. Personal interview. Sep. 16. 2014) According to Antonio Nemguimo, president of one of the Huaorani communities visited, Perenco did not hire local people for any type of work.

There were community works but what was in the agreement was not fully fulfilled. Petrobras said that the water system would be operating for two years but this was not fulfilled and now the water system is useless" (Bravo, Hermel. Interview Sep. 15. 2014)

"I say education because at that time there were some missionaries who worked for education, who told us what we should do and why... it was for a time, it was not permanent. Those from the Summer Institute of Linguistics came and conducted some interviews and as we always had to protect our culture, they did not let us down" (Irumenga, Moisés. Personal interview. Sep. 18. 2014)



Interviews with Juan Luis Grefa, Former President of the Community Yuralpa Center. (September 19, 2014).

“I have stains on my mouth and arms from pollution” (Grefa, Juan Luis. Personal interview. Sep. 19. 2014) “He built a medical dispensary and paid the professionals until the Provincial Health Directorate of Pastaza took over the management of this service” (Andrango, Rafael. Personal interview. Sep. 15. 2014)

The Company's relations with the communities suffered from little equity and caused internal problems and problems between the groups: *“At that time, Perenco negotiated with the leaders, and they did not have a direct relationship with the true needs of the community, and there was no necessary information, and the company only took the leaders and negotiated and the population did not know what the negotiation was about.”* (Irumenga, Moses. Personal interview. Sep. 18. 2014)

Alteration of customs and attempts at cultural changes through education:

The company made minor contributions to **education** that was offered to the inhabitants, and scarce contributions in aspects of **health**, at the same time, was the cause of the water used for consumption being contaminated and the surrounding population suffering from digestive problems: *“We drank the water from the estuary because it was our only source of water and since it was contaminated, it made us vomit and have diarrhea.”* (Nemguimo, Antonio. Personal interview. Sep. 18. 2014);

skin conditions also occurred: *“Because we bathed in contaminated water we had skin problems”* (Nemguimo, Antonio. Personal interview. Sep. 18. 2014); *“Children had skin problems because they bathed in contaminated water”* (Irumenga, Moses. Personal interview. Sep. 18. 2014);

Limited modalities and reduced concessions for the community: *“To install the entire pipeline, they helped us with the materials, not with the money, so we couldn't ask for a slightly larger project, we had to wait two years to request another project.”* (Nemguimo, Antonio. Personal interview. Sep. 18. 2014)

Levels of conflict caused by companies

The records of the Ministry of the Environment contain references to agreements and incidents that occurred in the relations between oil companies and social groups in the respective area of operation, as indicated in the following table:

The data reveal the tendency of certain companies (Perenco and Petrobras) to maintain relative group control through agreements, under conditions proposed by the companies and accepted without further information or advice by the communities. Most of the conflicts arose from failure to comply with what had been agreed and from the permanent lack of dialogue, consultation and communication. In many cases there was intervention by the public forces against the residents and peasants.

Cases of violations of human rights

In a report submitted by the Ombudsman's Office at the end of 2014, complaints were detected by individuals and social groups whose rights were affected by interventions by three companies (Chevron, Perenco and Repsol) and who are turning to the official body in search of solutions. The cases presented confirm the abuses reported during visits made by CAITISA, as well as those referred to in documented studies.

The affected population, which is certainly large, has turned to the authorities for order and justice, including the Ombudsman's Office; however, it has suffered the difficulties of dealing with powerful oil companies that have controlled every obstacle in its environment. This is how reality is perceived by those affected who have not received any compensation for their violated rights.

Number of agreements, claims and conflicts

Operations	Agreements		Claims		Conflicts	
	Originals	Renegotiations	Amount	Predominant Causes	Amount	Predominant Causes
Encana	8	0	2	Non-compliance with compensation. Environmental damage. Activities without prior or environmental consultation.		
Western	3	1			2	Road closures due to failure to heed community requests
Perenco	52		6	Non-compliance with compensation.	5	Residents' discomfort due to company presence
Petrobras	30	5	41	Non-compliance with compensation. Environmental damage. Impacts on production. Activities without prior consultation. Damage to community infrastructure.	4	Lack of dialog between communities.
Repsol	3	0			1	Arrest of community members
City East					2	Use of force and violence by the police

Source: Ministry of Environment, SIESAP-HN-1 Conflict.

Elaboration: CAITISA.

Environmental impacts and liabilities: areas investigated

Environmental legislative trends have moved from a sanitary conception in the 1970s, as applied to permit regulation, to the conservationist conception of the 1980s and the contemporary approach, which links productive and extractive activities with sustainable development as the guiding principle of such activities. Ecuador's environmental legislation received a prominent position with the approval of the 2008⁸⁷ Constitution, which recognized nature as a subject of law.

In hydrocarbons

Hydrocarbon activities carried out in the country have been the main source of wealth in the last four decades, although revenues have been generously shared with foreign contractors. The cost to the natural heritage is represented in the ecological footprint of varying intensity left, in the majority of interventions, by the resource's exploration and exploitation.

• **Definitions.** According to the environmental

nomenclature and the information recorded, environmental alteration and pollution incidents are related to operational factors, natural events and, occasionally, attacks. Such events are: spills that extend from wells or pipelines into land, rivers or lakes, and are also produced in storage tanks and terminals; swimming pools, that is, excavations for the storage of chemical waste, sludge, drilling cuttings and production tests; pits, minor excavations, on average 2m x 2m x 3m, which were carried out, as bad practice, near the banks of rivers, lagoons or swamps to confine contaminated material resulting from hydrocarbon spills. Hydrocarbon structures also cause environmental impacts and are: wells, platforms, stations, flares, industrial complexes and refineries.

- **Information from the Ministry of Environment.** Within this framework of definitions, the Ministry reports on the magnitude of environmental liabilities recorded by hydrocarbon field operators (TEXACO data is excluded, because it is presented in a separate section).

Although the number of pools open as waste disposal

sites is indicated in five of the six companies, there is very little data on their size. However, one can assume the liberality with which spaces were excavated and left without any treatment or remediation. The affected population corresponds to that registered in the 2001 Population Census, in the parishes where the camps are located.

The contamination produced by the open ponds was highly harmful, especially due to the lack of wall linings,

which led to leaching of toxic hydrocarbon components, formation water and heavy metals into the soil, which rendered it unproductive. If located near estuaries and rivers, the flows reached the streams with substances that were deadly for fish and animals that had access to those waters. The inhabitants suffered from health problems, with the risk of death if medical attention was difficult to obtain. They often suffered from illnesses that developed over a long period of time.

Environmental liabilities: swimming pools

OPERATING COMPANY	POOL		LOCATION		AFFECTED POPULATION
	Number	Area (m2)	Parish	Canton - Province	
CITY	SD	SD	Tarapoa	Cuyabeno - Sucumbios	5 185
PETROBRAS	10	SD	San Sebastian del Coca, November 3rd	Jewel of the Sachas - Orellana	6 980
ENCANA	2	SD	Dayuma	Orellana - Orellana	11 695
OXY	12	SD	Eden, Pompeii, Limoncocha, Milagreña Union	Orellana, Jewel of the Sachas, Shushufindi - Orellana, Sucumbios	9 215
PERENCO	37	1 200	Chontapunta, Puerto Francisco de Orellana, Nuevo Paraíso	According to the environmental nomenclature and the information recorded, environmental alteration and pollution incidents are related to operational factors, natural events and, occasionally, attacks.	35 289
REPSOL	53	42 349	Cononaco, The Eden, Alejandro Labaka	Aguarico, Orellana	2,496

Notes: Sd: The data is not in the database. In Perenco the extension corresponds to 5 pools. At Repsol, the extension corresponds to 14 swimming pools.

Source: Ministry of Environment, SIESAP-HN.

Spills are the worst causes of pollution. They are general caused by operational failures such as corrosion, negligence or bad practices; they can also be caused by attacks, natural disasters and criminal motives.

Contents of expert reports and fieldwork

In addition to the reports submitted by the State Attorney General's Office, which are part of the legal defense in international judicial proceedings, there are observations on the sites carried out by CAITISA during field work in the blocks operated until 2006 by Occidental, 7 and 21 in charge of **Burlington** and **Perenco**, to the Pata and Palo Azul fields operated by **Petrobras**, to the Aguarico wells (Lago Agrio canton) and to the Sacha field, block 60 (Joya de los Sachas canton), the latter intervened by the Texaco company, now in charge of Chevron, from which the

following statements are made:

From the time when OXY operated blocks 15 and 12, as well as Burlington and Perenco in blocks 7 and 21, the community states:

- Lighters and generators have interfered with hunting and fishing activities. Han desaparecido las especies.
- Changes in tourism potential. Loss of natural beauty. Fireflies that illuminated the night around the Limoncocha lagoon have disappeared.
- Irresponsible practices by the Perenco company, in technical aspects, with serious environmental impacts, when, in the phases of seismic studies, pentolite was buried at a depth of 20 meters and explosions were caused in places with water holes (Testimony of

Environmental liabilities: spillover

OPERATING COMPANY	SPILL			LOCATION		AFFECTED POPULATION
	Area (m2)	Volume (Barrels)	Cause	Parish	Province	
ENCANA	Sd	SD	Mechanical Failure	Dayuma	Orellana	11,695
OCCIDENTAL	4,893	10	Human Failure	Limoncocha	Sucumbíos	3,819
REPSOL	79,000	2,500	Corrosion	Cononaco	Orellana	359
PETROBRAS	Sd	SD	Human Failure	Tres de Noviembre	Orellana,	3 138
PERENCO	41 985	583	Natural Event, Mechanical Failure, Human Error, Attack	Chontapunta, La Belleza, Nuevo Paraíso, Puerto Francisco de Orellana, San Luis de Armenia	Orellana, Napo	41 434

Notes: Sd: The data is not in the database.

Fuente: Ministry of Environment, SIESAP-HN.

Elaboración: CAITISA.

Camilo Grefa and Roberto Francisco Audi; Unión San Miguel, El Coca parish).

For similar pentolite planting practices by the oil company CGC, which intervened in Block 23 in association with Burlington and Perenco, the KichwaZarayaku community filed a lawsuit in 2003 before the Inter-American Court of Human Rights. In June 2012, the Ecuadorian government obtained a favorable ruling, which meant that, in addition to removing the harmful material, it had to pay monetary compensation, commit to prior consultations, train officials on human rights issues for indigenous peoples, and apologize at public events.

In expert reports it is described that the threat of suspension of activities by **Burlington**, raised unilaterally and speculatively, seeking to configure an alleged expropriation, put Blocks 7 and 21 at risk of significant environmental damage, due to leaks and/or spills related to the closure. Faced with such imminent risk, the Ecuadorian State was forced to intervene and prevent mechanical, environmental and deposit damage. However, the foreign company declared itself a victim before international courts.

There are also serious issues regarding the state in which Perenco abandoned Blocks 7 and 21, despite the high environmental fragility of that sector of the Amazon rainforest. Far from the reasonable care that a prestigious company should have, Perenco was more interested in low costs than in the measures necessary to preserve the environment. According to the same reports, Perenco decided to acquire mature fields that were at the end of their productive life, in order to invest as little as possible. He also engaged in deception and concealment towards

the Ecuadorian authorities regarding damage to the Blocks and adjacent fields.

The independent environmental experts hired by Ecuador, Integrated Environmental Management Services, S.A. de C.V. (IEMS), detected significant environmental deterioration regarding soil and groundwater in Blocks 7 and 21. At the site, significant volumes of soil and groundwater are contaminated with hydrocarbons and/or heavy metals (zinc, barium, copper, chromium, nickel) in all seven facilities of the blocks tested and atmospheric emissions, due to improper mixtures of diesel and crude oil in power generation engines, converted into gases potentially harmful to the local population, as well as to the fauna and flora of the area. IEMS conservatively estimated that environmental impact costs would amount to at least USD 484.5 million, without considering other forms of damage to public health and socio-environmental damage.

In the Yuralpa field, block 21, **Perenco** caused the contamination of the water in the nearest estuary. Crude oil was used for the open roads, which, with the rain, would slide into the streams in the area, as described by one of the people interviewed: *“Perenco contaminated the water of the stream that is nearby, and the river too because what they dumped on the roads went down to the river, and we had nowhere to get water from”*. Did not perform any remediation: *“Perenco contaminated and left it there, he never cleaned up and left everything there”* (Nemguimo, Pancho. Personal interview. Sep. 18. 2014)

The expanded version of this Report describes the damages generated in Block 7 and in the Coca-Payamino field, also in Block 21 –operated by Perenco and Burlington–, the magnitude of the damages, the contaminating impacts on crops, fishing and other

productive activities of the communities existing in the included territories, as well as the effects on natural diversity, flora and wildlife; all due to lack of adequate maintenance and the use of old and obsolete technology to save costs.

Other testimonies of environmental impacts were received during the visit to the Pata and Palo Azul field operated by **Petrobras**. Local residents report cases of contamination, both of the water and of spills during the transportation of crude oil:

“There was contamination here, but Petrobras never aired it, the community always complained but they had the upper hand, what they mainly contaminated was the estuary, because about 7 heads of cattle died on me, I complained but they never recognized anything” (Bravo, Hermel. Personal interview. Sep. 15. 2014)

“Mismanagement or poor handling of oil pipelines, with poor maneuvering, has sometimes led to spills in the ravines, and as a result of this, a contingency team was formed in all the ravines and estuaries and they prioritized it so that there would be no more spills.” (Grefa, Miguel. Personal interview. Sep. 16. 2014)

Comprehensive audits carried out by the MAE on the companies Ecuador TLC, which operated block 18 (Palo Azul field and Pata field) and City Oriente in block 27, report on minor accidents that were remedied and the soil cleaned up following good environmental practices and in accordance with current and applicable environmental regulations; discharges of industrial and domestic water, which were re-injected. They have developed community relations programs and signed agreements with eight communities in the area of influence, as well as with the Municipal Government of Joya de los Sachas, with the Provincial Government of Orellana and with the Provincial Health Directorate in El Coca. In consultation with these institutions, they have stated that what was agreed has been fulfilled.

Environmental damage in the area of the Esmeraldas State Refinery

Among the documents that make up the file of the TécnicasReunidas lawsuit case that the State Attorney General's Office is handling, the non-compliance of the project is reported, the design and construction flaws that caused spills, measured from 1997 to 2006, of 2,230,000 m³ of wastewater, without proper treatment, into the rivers of the province of Esmeraldas, causing high environmental impact. {However, the foreign company sued the ICSID for allegedly unpaid wages. The conflict

ended in 2008, by agreement between the parties.

Aggravated case: Chevron

The information presented here has been taken in part from expert reports from the trial brought by the group of people affected by Texaco and which led to a conviction by the Provincial Court of Sucumbios. Also included are observations and testimonies obtained during visits made by the CAITISA team, as noted on each occasion.

Between 1967 and 1990, the TEXACO company carried out oil exploration and exploitation operations in the Ecuadorian Amazon, in an initial consortium with the company GULF and the state-owned company CEPE. GULF then left and CEPE acquired its stake; but at all times, the exploration and exploitation phases were carried out by TEXACO's operator, called TEXPET.

The concession area covered approximately 400,000 hectares. The operator drilled 356 wells in 28 fields, built 22 production stations and several substations, in addition to the SOTE pipeline.

Thus, TEXACO extracted 1,312.9 million barrels of oil, released 16,000 to 18,000 million gallons of formation water into the environment and burned 230,464,948 cubic feet of gas. It built almost 2,000 km of roads and highways.

Recorded spills.- Spills estimated at 26,388.62 barrels occurred during the TEXPET operation for three main reasons: 20.4% (5,389 barrels) were due to force majeure, 1.02% (276 barrels) were attributable to persons other than the company. the operator and the remaining 58.8% (20,723 barrels) due to problems in the oil operation. In these operating failures, the majority (58%) can be considered normal, but they also occurred due to corrosion (30.85%) and negligence or bad practices (11.06%).

Contamination and damage in spill areas.- The greatest number of impacts were suffered by the rivers and estuaries in the area: the Quijos River, the Shiripuno River and, mainly, the Aguarico River. In April 1976, the first spill into the Aguarico River was documented; immediately after, the contamination of this same river by diesel spillage was recorded. Se mencionan varios más en el Pozo Lago Agrio N° 15 y en líneas de cruce fugas de diesel.

Pool inventory.- 916 pools were located, 832 by aerial photointerpretation; the remaining 84 pools were verified in field inspections. By 1976, at least 287 pools were opened in the Aguarico, Auca, Lago Agrio, Palo Rojo, Sacha and Shushufindi fields.

Environmental impacts.- Texaco's oil exploitation activities led to the release of toxic chemicals into the environment. In these areas, aquatic life is exposed to water-soluble hydrocarbons, such as bitex, and inorganic pollutants such as chloride, cadmium, chromium, copper, nickel, and lead. The concentrations of these polluting substances measured in the rivers and streams in the concession make these waters unsuitable for aquatic biota.

Site soil data indicate that concentrations of Total Petroleum Hydrocarbons (TPH), barium, copper, chromium and zinc are high enough to produce toxicity in plants, invertebrates, birds and mammals. 1,618 cases of land loss were detected, along with damage to property (buildings) due to oil pipeline spills, pool breaks, seismic activity, discharges into rivers and estuaries, the oil facilities themselves, and road construction.

Soil remediation costs.- The Amazon District Contaminated Pond Removal Project (PEDPA) is designed to clean up contaminated soils in and around some waste ponds in the concession. The total estimated cost to remediate the volume of contaminated soils across the site is USD \$1,852,000,000.

Impacts on living conditions and human rights

Ethnic component, culture and customs

It is estimated that before Texaco arrived in the Ecuadorian Amazon, the population and territorial extension were approximately as follows:

1. Secoyas 380 people in three territories (San Pablo 7,043 ha);
2. Whirlpool Redwood 24,371 ha, Eno Field (8,000 ha.)
3. Siona 350-400 people (territory 47,880 ha);
4. Huaorani 2,200 people (2 million ha) (p. 18)

Other groups, the Kichwa population associated with the Federation of Indigenous Organizations of Sucumbíos Ecuador, are 56 communities. In Orellana, in the Federation of Communities Union of Natives of the Ecuadorian Amazon (FCUNAE) there are 78 Kichwa grassroots communities, in communities of 100-250 inhabitants. The Shuar are 17 communities in Orellana, in Sucumbíos there are 10 communities, with 1,500 people.

For indigenous peoples, life is determined by three basic elements: Territory, Food and Cultural Traditions.

Huaorani 2,200 people (2 million ha) With the beginning of oil activity, the Cofan, Secoya, Siona and Huaorani nationalities were forced to leave their ancestral lands due to the alterations in the ecosystem that impeded their

subsistence activities, especially food that came from hunting, fishing and gathering forest products; the rather large family structure was fragmented and some villages were subjugated with the introduction of alcohol and money.

Collective health impacts.- The expert reports cited include a psychosocial study based on a survey of 1,064 families who lived in areas near Texaco wells. A total of 69.0%, or 734 families, were made up of mestizos, 30% indigenous families and 1% Afro-Ecuadorians. They responded that there were 306 cases of cancer: stomach cancer, 20.27%, uterine cancer, 19.6%, and leukemia, 9.3%; of the total cases, 10.2% were children under fifteen years of age.

Complaints and Demands.- It is known that 214 people filed private lawsuits, most of them for loss of crops; others for illnesses caused by contamination, for experiences of repression and mistreatment by company operators and threats received.

Evidence of an official claim at the time is found in letter 83-294-GPN dated March 21, 1983, addressed by the Governor of the Province of Napo, Ney Estupiñán Recalde, to Eng. René Bucaram, General Manager of Texaco, where he states the following:

“It is a public outcry, Mr. Manager of TEXACO, regarding the serious damage that is being caused in the Shushufindi sector by the contamination of waters, rivers, estuaries, and ravines, due to the dumping of hydrocarbon waste to which they are being subjected by workers of the CEPE-TEXACO Consortium.

Based on the above, I would like to request that you design to take measures to prevent further damage, which, as will not escape your enlightened judgment, will ultimately have incalculable repercussions for the ecological system and, above all, for the agricultural sector in the area.”

Observations and testimonies obtained during the audit field work

What follows below is evidence captured in the **field work** carried out in the areas of the Aguarico wells (Lago Agrico canton) and Sacha field – block 60 (Joya de los Sachas canton).

During the first visit, in addition to verifying environmental damage caused during the period of exploitation in the Lago2, Lago 20, Lago Norte Reinjection Station and Aguarico 4 wells, interviews were conducted with affected individuals and ethnic groups, the evidence of which remains visible. The tour was captured

on video, allowing for a complete audiovisual record that complements this report.



Photo: Sample of the contaminated soil inside the closed well of Lake 2. (12/09/2014).



Photo: Gooseneck pipe forestuary drainage. Aguarico 4 wellzone. (12/09/2014)



Photo: Comunidad Cofan, cruzando el Río Aguarico. Parroquia Dureno. (12/09/2014).

Vast tracts of land were found that were “remediated” pools, some before 1990, prepared (covered) for the delivery of fields to the State Company CEPE; others

covered rustically with stones and earth between 1995 and 1998, for the signing of the contract with the President at the time, Sixto Durán Ballén and received to the satisfaction of Jamil Mahuad.

Oil residues can be detected everywhere, at shallow depths, by the colour of the earth and the smell.

Gooseneck pipes were seen draining the formation water from the pools into nearby estuaries, whose beds contain toxic waste and heavy metals.

On the contaminated land there are homes of farmers who subsist in small spaces because, in addition, their lands were taken by Texaco without any compensation. The nearby estuaries are polluted, so they lack water for subsistence and animal husbandry. They are occasionally supplied with water from tankers supplied by the respective municipality.

The Aguarico 4 well is one of 33 pits that remain open; an estimated 300 pits remained open after Texaco's "remediation" and handover in 1998; some unfinished cleanup efforts have been carried out by Petroamazonas since 2008. This 60x40m pool is located in a large swamp, some of which are 100m wide and 800m long.

The interviews carried out gave testimony of diseases unknown to the natives and settlers that were incurable, ancestral medicine was useless and ended in death. This was usually cancer, as the Secoya community leader relates:

"And when we reacted was when people started dying from certain diseases unknown to us because the shamans didn't know about them. Women died because they had many hemorrhages, they had tumors in the ovaries, in the throat, in the stomach" (Piaguaje, Humberto. Personal interview. Sep. 11. 2014)

Due to lack of registration or erroneous registration of the deaths of people in the 1980s, the magnitude of the mortality caused is unknown: “My mother died of poisoning and on her death certificate the reason for her death is given as cardiac shock, meaning that her heart stopped, they registered everyone like that, since every dead person's heart stops, what happens is that at that time there were no specialists here, only general practitioners and they gave you anything as the cause of death” (Moncayo, Donald. Personal interview. Sept. 12. 2014)



Interview of Mariana Jiménez (North Lake Station)
(12/09/2014)

A fundamental consequence of the company's negligent activities is the impact on the very existence of ancestral peoples and the reduction and even destruction of native habitat, in many cases with the support of public forces. The team spoke about this with the leader of the Cofán nationality, on the banks of the Aguarico River, who said:

The second visit to the areas intervened by Texaco for oil exploitation was made to the Sacha-Bloque 60 field, which is under the jurisdiction of Amazonía Viva, a public entity created by the current administration for the remediation of pools left in the area.

The environmental liabilities left by Texaco are mostly found in forested areas and constitute compelling evidence of the damage caused by the transnational company.

The following statements reflect the problems suffered as part of an open and recurring violation of the human rights of the inhabitants in the area of intervention of the oil company Texaco:

“For example, the man who lived next to my house died of cancer, another man died of the same thing. My wife's aunt who lived in my house died of cancer, her husband of prostate cancer. My grandson just passed away here from a heart disease. I don't know if it was due to pollution. That's for the doctors to determine. Because of that, my wife has had a stroke for 11 months now. Doctors have recommended that we get out of here since we live in pollution” (Baths, Hannibal. Personal interview. Sept. 16. 2014)

“One of my children who was born here became deaf and mute because of the pollution and we suffered a lot with the child, we went looking for someone to help us” (Intriago, Enrique. Personal interview. Sept. 16. 2014)

“This well was drilled 36 years ago, neither Texaco nor anyone else has compensated anything and I am still paying taxes to the municipality since it is my land” (Intriago,

Enrique. Personal interview. Sept. 16. 2014)

Another testimony: “Texaco has been a terrible criminal who not only owes us the land, but also our lives, because I have had to leave Quito three times without consciousness, because I lost three children due to abortion” (Jiménez, Mariana. Personal interview. Sep. 12. 2014)

“They thought they owned the area and built pools wherever they wanted, and they told me that if they wanted, they could build a pool inside my house.”(Intriago, Enrique. Personal interview. Sept. 16. 2014)



Interview with Professor Silvio Chapal, member of the Cofán community. (12/09/2014)

The damage caused to their territories, the absence of respect and solidarity, the lack of means of subsistence due to displacement and the arbitrary changes to their habitat have created inhospitable environments and overwhelming poverty that has afflicted the peoples involved.

“We used to have the whole jungle and we walked around freely, but now with Texaco the settlers have come too, and they continue working and taking over the farms and then they block our way, they say we can't walk there, not even fishing or hunting, and the space for survival is getting smaller” (Chapal, Silvio. Interview Sep. 12. 2014)

Electricity sector

The second group of lawsuits relates to the electricity sector. The scope of action of the companies is national, in one of the cases, due to contracts that were signed with the governing institution of the sector at the date of subscription. The remaining four cases are provincial in scope (three companies in Guayas, mainly for the city of Guayaquil; and, in El Oro, the gas exploitation area for energy production).

The five cases of conflicts raised in the electricity sector have, to date, been concluded with different results:

- MCL Power Group L.C. and New Turbine INC: Ruling in favor of the State (2007)
- Duke Energy Electroquil Partners: Award in favor of the investor (2008); the State paid USD \$10,776,178.
- Empresa Eléctrica del Ecuador-EMELEC: Laudo a favor del Estado (2009).
- Ulysseas Inc.: Laudo a favor del Estado (2012).
- Machala Power – Noble Energy Inc.: Agreement between the parties. There was no award (2009).

The EMELEC company took the risk of suing the Ecuadorian State under audacious circumstances of irregularities, such as the fact that it was not even a foreign investment and the poor electricity service to the city of Guayaquil. The ICSID Arbitration Tribunal issued an award in favor of the State.

Other cases of lawsuits filed by companies in the electricity sector are related to contractual differences and breaches that lead the Ecuadorian institutions responsible for the sector to declare the termination of contracts and to take regulatory measures such as those provided for in Constituent Mandates.

Mining

The mining sector follows, with three companies filing lawsuits; naturally, they have local concession areas, two in provinces of the Amazon region: Napo (Pungarayacu) and Zamora (Nambija), and one in Imbabura, in the north of the country. All three processes are open.

- RSM Production Corporation, which began operations with the Cotundo project in 2006. The arbitration notice was in 2010, at ICSID.
- In 1986, Zamora Gold Corporation began exploration operations with the Cumbaratza project. Notice of

arbitration in 2011.

- Copper Mesa Mining Corporation, which had operated since 1975 in the parish of Junín, in Imbabura. Notice of arbitration in 2012.

The institutional changes that the mining sector has undergone have drastically made it more difficult to obtain specific information about companies. With such restriction, the references and evidence obtained through consultations with officials of official entities and in the expert reports of the judicial proceedings held by the State Attorney General's Office are available.

The expanded version details the incidents caused by the companies Zamora Gold Corporation, linked to the then owners of Ecuadorian banks Hermanos Isaías and Alejandro Peñafiel, and by Copper Mesa Mining Corporation, warned about the severe environmental impacts in the region that included water contamination (concentration of lead, arsenic and chromium up to 100 times their natural content), extensive deforestation and desertification of the area, as well as social implications, such as the forced partial relocation of local communities.

Maximizing corporate profit: Speculative practices of foreign companies

Differences between declared domicile and nationality

A first anomaly has been detected in the statistical records provided by the Superintendency of Companies, where curious differences appear in the declarations of domicile and nationality, and then the same companies resort to another counterparty country of the TBI signed with Ecuador in order to, as nationals of that other country, bring litigation before foreign courts.

NATIONALITY SC	No. COMPANIES
Bermudas	3
Bahamas	2
Grand Cayman Islands	1
Panama	1
United States	6
Ecuador	5
Canadá	1
Spain	2
Brasil	1
TOTAL	22

Source: Superintendency of Companies
Elaboration: CAITISA.

a. The declared nationality,⁸⁸ in seven of the 22 companies, indicates countries identified as tax havens (details below), six are from the USA, five from Ecuador

(registered as local subsidiaries of foreign companies), two from Spain; one from Canada, and one from Brazil.

b. However, of the same 22 companies, 14 claim domicile in the U.S., 3 in Canada, two in Spain and one in each of the other countries (France, Argentina,⁸⁹ Bolivia), thus relying on the BITs of each of these countries.

c. Thus, of the 26 cases of claims against Ecuador that invoke BITs, 16 use the BIT with the United States; in 4 claims, the one with Canada; in 3 claims, the one with Spain; and, the rest, one by one, invoke the BITs of France, Bolivia, and Argentina.

It is obvious that such preferences for different registers are due to speculations by investors to increase advantages and benefits such as lower – or even no – tax obligations, free flow of funds, lower risk of distortions when resorting to fictitious transfer prices and the use of undercapitalization and evasion of regulations and control. This duality of records also produces computer chaos, which makes it difficult for institutions to manage the qualification of intra-firm loans, the qualification of FDI and the identification of the origin of capital.

In this investigation, it has been possible to deduce that there are legal loopholes and official constraints that discourage officials responsible for the corresponding registrations and records from demanding transparent procedures.

Tax havens

On the other hand, the perverse use of tax havens by foreign investors is well known, as is the liberality with which businesses originating from these territories were established, and what the opacity with which operations and money transfers are handled means for states; the consequence has been the flight of capital and the loss of the legitimate state right to receive tax payments. Ecuador cuenta, recién desde el año 2008, con disposiciones legales y administrativas para identificar y limitar las relaciones con los declarados paraísos fiscales.

Seven of the 22 companies audited in the following list were established in the country in the past. Intervinieron en la extracción del petróleo y en la prestación de un servicio también estratégico, como la energía eléctrica; aprovecharon las ventajas que les brindaba el paraíso fiscal y con facilidad se acogieron a la protección de un TBI, sin corresponder a su nacionalidad, para colocar a Ecuador ante multimillonarias demandas que se ventilan en tribunales internacionales.

DOMICILIO	No. COMPANIES
United States	13
Canada	3
France	1
Spain	2
Brasil	1
Bolivia	1
Other	1
TOTAL	22

Source: Superintendency of Companies.

Elaboration: CAITISA.

These are the companies that have rounded up, with no shame or consequence, advantages in their favor.

Lack of transparency in the formation of consortiums

Finally, the investigation by companies has identified three consortiums: Consortium Block 7 and Block 21 (Perenco – Burlington), Consortium Petrolero Block 18 (Petrobras – Ecuador TLC) and Consorcio Petrolero Bloque 16 (Repsol – YPF), each of which has its own Unique Taxpayer Registry (RUC) and, nevertheless, does not have any kind of registration or information with the Superintendency of Companies.

Under-capitalization practices

With significant illicit returns on tax compliance, foreign companies used under-capitalization, which became common practice.

Among the many incentives available to investors to attract their capital to the country was the unlimited deduction of interest expenses and other financial expenses for loans granted, in most cases, by the companies' parent companies abroad, related entities, or financial institutions located in tax havens. This allowed them to inflate expenses, reduce the corresponding tax base, and, as a result, pay less income tax or even report losses, thereby avoiding paying that obligation.

The practice of thin capitalization is one of the most important aspects of auditing because it allows for the assessment and verification of recurring business procedures to evade tax responsibilities, which, added to the benefits and concessions legally granted, result in a huge fiscal sacrifice and less public financing in the country receiving the investment.

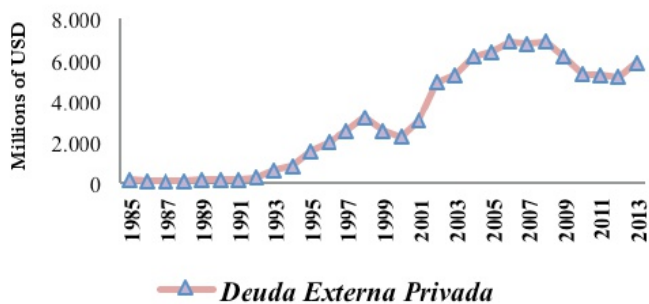
Trends in private external debt. To understand the magnitude of the abuse by foreign companies that have disguised their capital inflows in the form of loans, the following graph is presented. The notable growth of debt

Empresas con Nacionalidad en paraísos fiscales

N°	NOMBRE	SECTOR	DOMICILIO	NATIONALITY SC	TBI INVOKED
1	Perenco Ecuador Limited	Oil Company	France	Bahamas	France
2	Empresa Eléctrica de Ecuador (EMELEC)	Energía Eléctrica	United States	Bahamas	United States
3	Chevron Corporation	Oil Company	United States	Bermudas	United States
4	Burlington Resources, Inc and others	Oil Company	United States	Bermudas	United States
5	City East	Oil Company	United States	Bermudas	United States
6	Noble Energy Inc	Energía Eléctrica	United States	Grand Cayman Islands	United States
7	Murphy Exploration and Production Company International	Oil Company	United States	Panama	United States

can be observed since 1993, when the opening to FDI was encouraged, contracts were modified to offer greater profits in oil activity and processes for signing bilateral investment protection treaties were opened:

PRIVATE EXTERNAL DEBT



Source: Central Bank of Ecuador: 85 Years of the Central Bank. (Economic Statistical Series) and Monthly Bulletin No. 1953, November 2014.

Elaboration: CAITISA.

The trend has been reversed since 2008, when tax regulations were enacted to control and limit such distortions.

Another effect of the distortion of capital inflows is in statistical information. When comparing the figures for loans with those for foreign direct investment, which have not grown much and are irregular, they diverge significantly in the 1990s and the first decade of the 2000s, which suggests that the statistical data for both concepts are unrealistic.

There are legal proceedings for undercapitalization glosses, one of them instituted by the Internal Revenue Service (SRI) to the company OXY, in whose appeal, the National Court of Justice states regarding the credits with the

parent company or related branches: “it is an operation between companies that constitute an economic group, since they are related companies, which is not denied by the plaintiff, that there is no debtor-creditor relationship, since no one can contract with himself [...] resorting to the figure of a credit between related parties, materializes an economic effect, which is the deduction of interest paid, achieving to benefit from the deduction contemplated in numeral 3 of art. 13 of the Internal Tax Regime Law, in force at that date, harming the final result of the fiscal year [...] the nature of the credit operation is questioned, since only interest is covered, but not capital, which would have been the consequence of a true loan [...]”.⁹⁰

In 14 companies and in the majority of the years reviewed, related or intra-firm credits cover the majority (in some cases exceeding 90%) of the liabilities.

Concessions and incentives that have been granted to FDI

The country has offered other forms of benefits to attract foreign capital, such as tax reductions: the Income Tax rate is one of the lowest in the Region, concessions, exemptions, tax shields, liberalization through agreements to avoid double taxation and reduced prices, with a high international advantage for business users abroad in the public offer of consumer goods and services with subsidies assumed by the State. All of which has meant a considerable fiscal sacrifice for the country.

Revelations about critical Texaco procedures

The judicial process followed by the organization of those affected by Texaco has allowed this audit to have access to documents that reveal commitments of national authorities with the company's directors at times when the defense of national interests was required.⁹¹

Some of these executive documents from Texaco Ecuador

report on the “improvement” in relations with the current government, headed by Osvaldo Hurtado, compared to the previous one, headed by the late Jaime Roldós, which allowed for clear economic advantages for the company due to the increase in the oil pipeline tariff and the rise in the price of crude oil for domestic consumption, applied retroactively.

Another document instructed from abroad that only major events (spills) “that attract the attention of the press and/or regulatory authorities” should be reported.⁹² This is evidence of the low ethical level and minimal commitment of the company's directors to assume responsibility in cases of damage and harm to the ecosystem of the concessions granted since the beginning of oil exploitation operations.

Likewise, the letter that Donald G. Sawyer of Texaco Petroleum Company of Quito addressed to Dr. J. M. Quevedo, Manager of the Consortium Office, dated June 1, 1988, with the following statement: “REVIEW OF CONTRACT MC-E-OP-3010 OFFER OF BRIBERY TO AUDITORS”; the content reads as follows:

- “3. The report relating to the bribe offered to auditors should be handled separately.”
- This is further evidence of the lack of ethics of the company that is suing Ecuador for multimillion-dollar sums and that adds benefits to the widespread exploitation of Ecuadorian natural and economic resources.

⁸⁷ The main laws considered in the investigation of environmental impacts: Environmental Management Law, of July 30, 1999; Hydrocarbons Law, Law for the Promotion of Non-Conventional Energy, Law for the Regulation of Production and Marketing of Fuels in Ecuador, Special Law for State Decentralization and Social Participation (October 8, 1997), Substitute Regulations for the Environmental Regulations for Operations.

⁸⁸ The Superintendency of Companies registers the nationality certificate issued by the Ministry of Foreign Affairs in the allocation of investor category visas.

⁸⁹ The Brazilian company Petrobras availed itself of the BIT with Argentina.

⁹⁰ Extract taken from the First Body of the judgment issued by the National Court of Justice (2013) to the appeal filed by OXY against the SRI, p. 14 and 15

⁹¹ The different transcripts of point 2.9 are taken from the translated and notarized versions, the originals of which are part of the files of the trial followed by the group of People Affected by Texaco and which received a guilty verdict against Chevron in the Provincial Court of

Sucumbíos.

⁹² Phrase that is part of telex 2728 of June 1, 1988, sent, in a confidential manner, between executives of Texaco Petroleum Company, with address in Quito Av. December 6 No. 2816. The translated version has been notarized and is included in the file of the trial held by the social group of those affected by Chevron in the Provincial Court of Sucumbíos.”



GENERAL CONCLUSIONS

The negotiation and signing of the BIT by Ecuador is part of a process of policy implementation, institutional and regulatory restructuring aimed at promoting the free flow of transnational capital implemented in several countries around the world and which was, to a large extent, promoted by the World Bank and the IMF.

The empirical fact of increased foreign investment flows in Latin America in the 1990s was interpreted as a consequence of the BITs. However, a review of the evidence shows that other circumstances, such as the high granting of benefits to oil companies, contributed to this flow of capital, and that the BITs were not decisive. At the same time, the commitments undertaken by the BITs contributed to the weakening of the State's official planning, regulatory and control powers and to minimizing the responsibility of the transnational companies that brought their capital to Ecuador.

1. Since 1965 Ecuador has negotiated 30 BITs, of which twenty-seven have entered into force. Most of these took place between 1992 and 2002 at the height of neoliberalism in Ecuador. In 2008, 26 BITs were in force, the year in which the Executive adopted the political decision to initiate the process of denouncing all BITs.

2. The ICSID Convention and the BITs negotiated, entered into and ratified by Ecuador were not properly processed by the Executive and Legislative functions of the time. During the investigation, irregularities, superficiality and vagueness were identified in the approval of these international treaties, as well as evidence of internal and external pressures to sign them. Furthermore, administrative decisions were taken and reformulations of the national legal system were dictated in order to comply with admitted obligations in these treaties, to the detriment of the state's responsibility to protect and defend national interests.

3. The TBI signed by Ecuador contain clauses that conflict with the Constitution and internal regulations.

4. The most obvious tensions between national legislation and BITs have to do with the dispute resolution mechanisms that imply a session of sovereignty by subjecting the country to international arbitration tribunals, without first going through national instances. Other incompatibilities with the constitutional text relate to the priority assigned by the Constitution to national investment and the complementary nature of foreign investment, conditions that are contrary to the preferential treatment and supremacy of foreign investors

established by the BITs, because the national investor does not have the right to direct recourse to international arbitration; as well as the right of the State, enshrined in the 2008 Constitution, to expropriate and nationalize, in accordance with the customary international rule, which it exercises for reasons of public utility or social and national interest; there is no classification in the Constitution or in national laws of the notion of expropriation under different figures, nor of "indirect expropriation" or "equivalent to expropriation" as has been resolved in some awards.

5. The privileges granted to foreign investors as evidenced by the BITs have, in many cases, displaced the obligations assumed by the Ecuadorian State in terms of human rights, whose compliance has priority as erga omnes norms.

6. The denunciation of BITs is a lawful act, recognized by International Law, and is included in the text of all BITs signed by Ecuador. Therefore, it is a sovereign act of the State, and the explanation of its motives is not obligatory.

7. Nine of the current BITs were terminated through diplomatic channels, in accordance with the rules of the 1998 Constitution; of these, six remain in force due to the application of the survival clause. Seventeen of them initiated their denunciation process under the rules of the 2008 Constitution, but they remain in force, either due to the application of the survival clause, as is the case of the BIT with Finland, or because the denunciation process has not been concluded.

8. These complaints are currently being processed in 16 cases, some of which are in the final stages. In the cases of Great Britain, Sweden, France and Germany, the complaint process must be completed and made effective, according to international law, by notifying the counterparties.

9. In total, 23 BITs are in force while the complaint process is underway.

10. Today, governments of countries in different regions and international organizations such as UNCTAD and ECLAC – supported by numerous empirical investigations on foreign investment flows and their effects on host economies – have begun to question the benefits of the investment protection system and, at the same time, have begun to search for alternatives.

11. The most criticized aspects of the current investment system are: the conflict of interests of

arbitrators, the commercial bias of the arbitration system, ad-hoc arbitration without institutional guarantees of impartiality and independence, and the lack of adequate instances of recusal and appeal.

12. The erroneous interpretation and application of the compensation rules when quantifying compensation for damages has also been questioned. The general nature and lack of objectivity of such rules make them inapplicable in specific situations, since they are not adapted to the particular situation of each case and each State and contravene national legislation, as is the case with compound interest, which is prohibited in the Ecuadorian constitution.

13. On the other hand, it has been considered inadmissible that the State's responsibility is the only one called into question within the analysis of violations of the clauses of the BITs. This gives the international dispute settlement regime a pro-investor bias that unbalances investor-State relations.

14. These problems, typical of a biased system, have caused serious economic damage to Ecuador in the various awards issued on biased and unfair grounds.

15. Ecuador has been sued under BITs on 26 occasions, with the majority of the plaintiff companies operating in the oil exploration sector (50%). Other areas where the plaintiff companies have operated are related to the supply of electricity (19%) and mining (12%). The period in which these claims were filed began at the same time as government policy changed towards the recovery of sovereignty over the use of its natural resources (2006).

16. Of the 26 cases registered against Ecuador, 16 have concluded and 10 remain open. Of the cases still open, that is, those on which the courts have not yet issued a final award, the claims total **USD 11,188,966,571**. It should be noted that in two cases, RSM Corporation and Zamora Gold, it has not been possible to identify the amount of the damages. Of the open proceedings for which a ruling has been issued but appeals are pending, the amounts established total **USD \$ 377'415.988**.

17. So far, the Ecuadorian State has paid **USD \$1,342,115,969** as a result of negative awards or by agreement of the parties (to IBM, Oxy I, Duke Energy, Noble Energy & Machala, Oxy and Chevron), minus the payment ordered in favor of the state in the Ulysses case.

18. In the claims for investment arbitration based on BITs, in the period 2003-2013, the State disbursed a total of **USD \$155'929.417** for payments to law firms

and other arbitration expenses.

19. If the payments already made for awards based on BITs and defense expenses noted are added, the amount disbursed by the Ecuadorian State amounts to **USD \$1,498,045,386, a value equivalent to 5.8% of the 2017 PGE and which could have been used in social programs and in greater efforts required to reduce poverty in the country**. These are the financial consequences experienced by signing a TBI.

20. An analysis of the 26 cases against Ecuador reveals that the arbitrators have repeatedly made expansive interpretations of the applicable rules, which has allowed them to comply with the demands of investors and issue high-level awards against the State. As a result, Ecuador has faced and continues to face multi-million dollar sentences.

21. The application of international standards enshrined in the New York Convention of 1958 and the Panama Convention of 1975 has not materialized, in relation to the power of control that the Ecuadorian State could have exercised for the execution of awards. With the support of such international provisions, Ecuador is able to demand non-execution in the event of an aberrant, manifestly arbitrary decision, collusion, corruption, manifest partiality of the arbitrators, as well as in the event that it is demonstrated that said decision contradicts the provisions of the Constitution. For the time being, it is necessary to incorporate determining conditions in this regard into domestic legislation.

22. State investment contracts often contain clauses reflecting the same investment protection standards as BITs, including the transfer of jurisdiction to international arbitral tribunals. Public procurement regulations lack provisions that safeguard the national interest, in an equitable regime for the protection of foreign investments.

23. The arbitrators who assess the validity of the acts of the Ecuadorian State have been chosen, in accordance with the rules in force, on an ad-hoc basis, without prior institutional guarantees of impartiality and independence. Most individuals who serve as arbitrators continue to serve in other roles such as: party counsel in arbitrations, corporate counsel, academics, corporate board members or expert witnesses.

24. Among the arbitration panels that have taken on cases against Ecuador, there are examples of arbitrators who position themselves in favor of broad investment protection. From their position as public figures, they argue in favor of signing investment

protection treaties or against reforms that restrict the concessive wording of the clauses incorporated in them.

25. Given the evidence of bias in favor of investors on the part of those who regularly serve as arbitrators, we propose the adoption of a series of criteria and principles, on the basis of which it would be feasible to develop strategies for the selection and challenge of arbitrators. The defined criteria fall into three categories: “conflicts of interest”, “conflicts of issues” and “systemic conflicts”.

26. Throughout history, the members of international arbitration tribunals have enjoyed a special immunity status, which immunizes them, during the performance of their functions, from any future claim by any of the parties submitted to their arbitration. The immunity granted to this select group of arbitrators has turned them, in practice, into an impunity for any decision they make, leaving them exempt from legal liability as a consequence of their actions.

27. There is a threat of payments for a total amount of **USD \$13,409 million** (if negative awards under challenge by Ecuador are added), which approaches 51% of the 2017 General State Budget.

28. BITs have not been decisive in terms of attracting FDI; according to ECB statistics, the flow of FDI comes mainly from Brazil, Mexico and Panama, countries with which Ecuador does not have a BIT. The 66% of total FDI comes from Latin American countries, which shows the relevance of regional integration initiatives.

29. FDI amounts arriving to Ecuador are small in relation to the Ecuadorian economy, representing only 1.11% of GDP on average in the period 2000-2013. The contribution of FDI to gross fixed capital formation is also low, standing below 3% (2008-2013). And half of this investment consists of reinvested profits. Therefore, its contribution to Ecuador's economic growth is questionable, taking into account that the Ecuadorian economy has grown above the average for Latin America and the Caribbean.

30. ECLAC and UNCTAD have concluded that the most important factors that attract FDI and determine the country of destination for its investments vary according to the investor's primary interest. Consequently, public policy could be more decisive in attracting FDI than the existence or not of BITs.

31. It is estimated that in 2013, the subsidiary companies remitted around USD 3,822 million in

profits. That annual amount is nearly half of the inward Foreign Direct Investment recorded in the last ten years.

32. Foreign investment statistics, based on the application of IMF manuals, do not provide relevant information to quantify the impact of FDI. They are limited to measuring investment inflows and outflows and not the characteristics of these investments, data that are indispensable for analyzing the socioeconomic and environmental effects of these investments from a development perspective.

33. There are no statistics in Ecuador designed specifically to study the behavior of foreign interests in the business network. There is scattered information in the integrated economic table by institutional sectors, in the exhaustive survey of companies and their establishments (product of the Economic Census), and in administrative records, particularly tax records.

34. Regarding the identification of the economic impacts generated by foreign companies that, under BITs, have filed claims against Ecuador in international arbitration tribunals, official figures show a low dynamism of global production in the provinces where the investments of such corporations were located; at least, in the times when they operated. Indeed, from 1993 to 2005, the period of greatest external intervention, the zones of influence experienced a low level of productive expansion.

35. The contribution of FDI to direct employment generation in the country has been minimal due to the nature of extractive activities, which require intensive use of equipment and machinery. There has also been no interest in generating indirect employment in the areas of operation, such as local purchases of supplies or services.

36. The social indicators of the population located in the areas of influence of the plaintiff companies reveal a precarious situation in terms of health, education, illiteracy, access to drinking water, electricity and sanitation services during the stay of the foreign investors. The contrast is evident, and is evidenced by the figures, when people and communities are receiving fair and compensatory attention, which is the case with the current administration of the State.

37. Impacts on peasant and community property. Unrecognized property rights. Certain oil concessions granted by the State to companies were carried out without recognition of previously established property rights of peasants and communities. Those affected, mostly indigenous

peoples, have felt that they have been invaded and even displaced without any compensation. There are cases of properties where wells were drilled and the farmer-owner continues to pay municipal cadastral taxes, because there was no expropriation.

38. Evidence of alterations in habits, productive activities, food, and cultural values. Changes occurred in food production and means of subsistence (gathering, hunting, fishing), substitution of natural native beverages for alcoholic beverages, resulting in dependence, violence and social degradation. The agreements signed between companies and indigenous communities or nationalities imposed codes of conduct, which became forms of control and appeasement against possible lawsuits and claims.

39. Environmental impacts caused by the oil sector. Based on the reports submitted by the environmental authorities, as well as on field work carried out by the audit, environmental liabilities were found left by certain oil companies, which are in litigation against the country, such as open pools for crude oil deposits, sludge and waste laden with toxic heavy metals; pits on the banks of rivers, lagoons or swamps to confine polluting products; spills of crude oil and fluids, such as the worst cause of contamination. It appears that in the Ecuadorian Amazon, they applied rudimentary and harmful practices that were not allowed in other places where they operated.

40. Chevron is the most serious case. The former Texaco company, acquired by Chevron, acted irresponsibly and disrespectfully, with obsolete technologies, causing spills of more than 26,000 barrels of crude oil into important rivers: Aguarico, Quijos and Shiripuno, and numerous estuaries, it also dumped 18,000 gallons of formation water, which is more toxic than crude oil itself, causing the death of fish, cattle and wildlife. Texaco opened 916 pools, whose leaks have caused soil toxicity, and water and air pollution. Written communication between company executives stipulated that spills will be reported only when they "attract the attention of the press and/or regulatory authorities...". Due to the high level of contamination, the health of the population was severely affected. In a survey of 1064 families, 306 cases of cancer were found, but it is likely that more damage was done, since there was no record of this cause of death, due to lack of knowledge of the disease.

41. The openness and liberality with which foreign investments were received allowed corporations to speculate in order to increase profits, even if it implied

the avoidance of obligations. Seven of the 22 companies investigated were registered as nationals of tax havens, but used BITs subscribed with other countries (USA, France, Canada) to sue Ecuador before international courts.

42. Undercapitalization for tax avoidance became a recurrent strategy of companies in the 1990s. This figure consists of disguising capital income as credits; the magnitude of this irregular practice is reflected in the disproportionate growth of private debt since 1993.

43. The examination of financial statements and income tax returns has made it possible to identify numerous irregularities practiced by most of the companies investigated, which can be outlined as follows: losses in continuous fiscal years, which would have incurred in grounds for dissolution; the relationship between sales income and income tax paid has not much justification, the higher the income, the lower the taxes paid; the highest credits are recorded in subsidiaries (hidden purpose of consortiums); there are cases in which intra-firm credits reach up to 99% of liabilities, while the values of subscribed capital are perennially maintained at the minimum required for the establishment of the company.

44. Foreign corporations have been beneficiaries, without limitation, of the reduced prices of fuels, electricity, telecommunications and drinking water services. Compared to what it would have cost them in their countries of origin, there is a considerable saving that has not been quantified or recognized.



RECOMMENDATIONS

The Commission submits the following recommendations to the Ecuadorian State for consideration:

1. Conclude the BIT termination process

Based on an analysis and evaluation of the Bilateral Investment Protection Treaties (BITs) signed by Ecuador that are currently in force, the Commission proposes that the Ecuadorian State continue the process of terminating the BITs that was initiated by the Executive Branch in 2008.

The termination process is included in each of the treaties, which makes this act legally valid and legitimate. Termination should be carried out in accordance with the provisions stipulated in each Treaty. However, in some cases, the State may explore the option of mutual termination, negotiation of new agreements, or renegotiation on the basis of an alternative model proposed here in order to avoid the effects of survival clauses or ultra viability of the treaty. For example, after stating the reasons for the withdrawal, the diplomatic note may state the intention to explore this avenue.

While it is not legally required to state reasons for filing the request, the Commission proposes a withdrawal from the BITs on the following grounds:

- The Constitutional Court of Ecuador has ruled on the incompatibility of such treaties with the constitution. These treaties are contradictory to erga omnes obligations adopted by Ecuador at the international level, such as those deriving from human rights treaties.
- There is already a practice (*opinio juris*) developed by Ecuador—which cannot be disregarded—insofar as it has completed the termination of at least ten BITs.
- The new constitutional framework of 2008 was an unforeseen and unforeseeable event at the time the BITs were entered into, which implies a fundamental change in the legal circumstances as compared to those under which they were entered into.
- Some treaties included objectives in their preambles on development and welfare that were not fulfilled, with effects contrary to those objectives, and therefore maintaining these obligations means sustaining commitments that are, in fact, ruinous for the Ecuadorian people and contrary to the treaty's own objectives.
- The arbitral tribunals that dealt with the disputes against Ecuador have significantly expanded the scope and meaning of the clauses originally agreed to by the parties in the Treaties, far beyond the intention of the

signatory states. This amounts to a change of circumstances that justifies treaty termination.

- Ecuador's decision on the complaint is part of a global trend by governments to restrict the protection of foreign investments and to ensure the states' sovereign right to regulate themselves in favor of the public good.

The termination of these agreements should follow the procedure indicated in the 1969 Vienna Convention on the Law of Treaties, the 2008 Constitution of Ecuador, the Organic Law of the Judiciary and the Organic Law of Jurisdictional Guarantees and Constitutional Control. Finally, this should be formally communicated to the counterparty in order to obtain legal effects at the international level.

If a foreign policy of alliances, coordination and blocs were developed, international circumstances would strengthen Ecuador's position on the challenge of the BITs. The sum of circumstances over the last two decades has marked a change of course in some countries in terms of openness in investment policy. Questioning the legal framework that defends the rights of companies over those of the state is currently at the center of investment policies in several countries. Various nations have expressed their dissatisfaction with the system, and have expressed their criticisms, highlighting the need for revision and reform.

2. Negotiation of new instruments between the state and private investors

International investment contracts with restricted rights and obligations

Investment contracts allow for greater flexibility than BITs, since they are signed on a case-by-case basis and not with an international scope. Moreover, as long as the BITs terminated remain in force due to the survival clause, the signing of international contracts between the state and foreign investors is a solution that allows the state to file arbitrations under other rules, establish a framework of certainty and incentives, restrict the rights of investors, and impose obligations on them.

We recommend that the Ecuadorian State seek to renegotiate contracts (in the case of established investors) or negotiate new ones (in the case of future investors), in which:

- The investor waives dispute settlement rights under the BITs and, in their place, subscribes only to ad hoc tribunals under national laws, as has already been applied by the Ecuadorian State with several

investment contracts.

- The investor accepts binding obligations such as those proposed in the alternative treaty model.
- The possibility for states to sue investors in the event of breaches of such obligations or contractual breaches is included.
- The option for communities affected by human rights violations to also have the possibility of filing claims against investors before a competent jurisdiction should be included.
- Valued investment schedules should be included.

Given the importance of these contracts, the Commission recommends that the contracts be public and subject to public control and oversight based on legally established regulations and criteria.

Principal guidelines for an alternative investment treaty model⁹³

Objectives of the Treaty

The principles and objectives of an alternative investment treaty should be as follows:

The primacy of human rights over commercial rights;

Subsistence of the state's sovereign regulatory capacities;

Ensure the principles of Good Living, which requires a comprehensive investment policy guaranteeing not only the protection of investment but also the protection of human rights, particularly the rights of indigenous communities, the rights of nature, labor rights and other social interests;

Avoid unequal conditions: for example, that only companies can sue states and not the other way around, and the opportunities for abusive or expansive interpretations of the treaty's clauses.

Firstly, any possible treaty on foreign investment should respect human rights, and the labor and environmental rights enshrined in the Constitution and other international treaties ratified by Ecuador, as a constraint on the actions of foreign investors and companies.

For this to be possible, the Commission endorses and recommends continued support for the initiative presented by Ecuador, within the framework of the United Nations, for a Binding Code for transnational

corporations in the area of human rights. All of the state's diplomatic and political capabilities must be employed to continue gathering allies in this transcendental endeavor.

Secondly, any possible treaty on the subject should be based on the recognition of the states' right to regulate foreign investments—within the framework of their national legislation and their commitments under international law—in order to tie these investments to the objectives set forth in their development plans.

Treaty Structure: Preamble and definitions

Preamble

The preamble deserves special consideration because it defines the treaty's nature and purposes and outlines the interpretation that may be applied under international investment arbitration. Specifically, together with investment protection, the preamble should take sustainable development⁹⁴ into account, in order to reaffirm that investment protection is not the treaty's sole purpose.

Investor

The concept of investor must be clearly and strictly defined. This will make it possible to characterize the subject carrying out the activities protected under the BIT. The *jus standi* may also thereby be determined in claims arising from disputes derived from the treaty. Ultimately, the state must decide whether the investor's entitlement is appropriate.

The investor must be a legal person, a company legally incorporated in the state where it is a national, which has been established and actively operating for a period of at least two years, and it must have its headquarters of control and management exclusively in the state of origin. It must annually submit information regarding its name, address and a Certificate of Corporate Good Standing. The investor must also indicate its partners or shareholders, and the attorneys-in-fact of legal entities holding shares or stock in the company.

If the obligations set forth in the Treaty have been breached, including through the act of corruption, we propose that investor status, and therefore the treaty's protections, be revoked.

Investment

Investment must be defined strictly and specifically. In accordance with Ecuador's domestic law, any investment admitted by the competent authority shall be subject to the BIT's protection. Ultimately, it should be restricted to tangible and intangible assets or property, with a duration of at least two years. The investment must be made with a

substantial commitment of capital or other resources, an assumption of risk, and a tangible contribution to development. The assets to be protected under the investment must be owned directly by the investor, through a company incorporated in Ecuador.

The competent investment authority must have sufficient tools to approve the admission or expansion of all foreign investments provided that they are considered beneficial to the country's development. This must be an obligatory condition for the protections granted in the BIT.

Based on Ecuador's experience, we can recommend the following points regarding the scope of investments protected by any future investment treaties:

- No retroactivity commitments should be included: the protection provided by the treaty should not cover investments made prior to its signing, particularly if they are investments that have already withdrawn from the country.
- Any abuse of the treaty by investors, such as fabricating a protection not provided for in the treaty, should be expressly foreseen and prohibited; particularly corporate restructurings by nationals of a state other than the direct party to the treaty, or by nationals of the Ecuadorian state who assume a nationality other than their actual nationality.
- In order for an investor to file claims under the corresponding BIT, the investor must be the controlling shareholder of the company holding the investment, and in no case only a minority or majority shareholder.

The definition of protected investment in future treaties should exclude, at a minimum, the following elements:

- Portfolio investment, including public or private debt bonds. This does not mean that the Ecuadorian State or companies cannot use this form of financing in the stock exchanges; rather that they would not be covered by the treaties due to the speculative nature of this type of financial investment. This restriction must be subject to domestic and/or international legislation expressly ratified by Ecuador.
- External debt, whether it be private, public, banking debt or debt in the form of bonds or debt securities, should be subject to the specific applicable legislation.
- Rights granted by concessions governed by administrative law for the exploitation of natural resources or public assets (e.g., radioelectric or air space, among others).
- Public works contracts, long-term commercial

contracts, and service contracts, which should be subject to the contract terms, which, in turn, should be valid only to the extent that they do not contravene domestic laws.

- Any investment where the investor is proven to have participated in acts of corruption (directly or through third parties) prior to its implementation or at any stage of its execution.
- Intellectual property rights should be governed by domestic laws or intellectual property treaties expressly ratified by Ecuador.
- In the event that the Ecuadorian State grants an extraordinary concession to invest in sectors for the provision of public services and use of public goods, as defined in Art. 314 of the Constitution, these investments should be excluded from the scope of investment treaties.

State rights to be included

We recommend that the following topics be considered in the content of any new treaty:

- Insofar as progress is made in the approval of a Binding Code on human rights for corporations, investment treaties should include investor compliance with the legal obligations assumed in the territory in which they invest, regardless of whether these obligations arise from national or international norms. The Treaties should also specify the tribunals where these obligations may be enforceable by states, individuals and affected communities, including arbitral tribunals with jurisdiction for the resolution of disputes under the treaty.
- Measures taken by a state party to comply with its international obligations under other treaties and/or conventions should not constitute a breach of the investment agreement, and should not entitle an investor to compensation for violation of the agreement.
- Include clauses that acknowledge a state's right to impose performance requirements, be they general requirements for any investment or specific requirements stipulated through contracts. Performance requirements should be guided by national development plans and collective benefit, within the framework of the National Constitution's mandates. The search for productive interlinking and purchases of domestic inputs by foreign investors is of particular importance, given that this is the only way for foreign direct investment to have a carryover effect on the rest of the national economy and the

generation of indirect employment.

- Include clauses that allow the state to take measures to encourage technology transfer.
- Include clauses that preserve a state's right to exclude areas considered strategic according to national development plans from the scope of investment treaties, or to demand the inclusion of national partners in corporations operating in these economic areas, turning them into joint ventures with national capital and majority state participation.
- In order to protect the state's regulatory capacity, any investment treaty should contain clauses that explicitly recognize the state's ability to grant, in accordance with its domestic law, preferential treatment to any enterprise in order to achieve national or sub-national regional development objectives.
- Include clauses recognizing the state's ability to take all necessary measures in its domestic legislation to prevent tax avoidance and tax evasion practices.
Include clauses that recognize the state's capacity to establish laws or regulations preventing illicit capital flows (e.g., under- or over-invoicing in intra-firm exchanges).
- Include clauses acknowledging the state's ability to take the measures it deems necessary to prevent flows of 'swallow' or highly volatile capital.
- Include clauses granting the state's right to legislate in favor of profit reinvestment.
Include clauses recognizing the state's ability to implement selective tax concessions and exemptions, based on national planning objectives and guidelines, which are temporary and renewable on the basis of evaluations of compliance with goals and conditions defined on a case-by-case basis.

Obligations to be included for the investor

We recommend that obligations be established for investors under the new investment treaties according to the following criteria:⁹⁵

- Respect the norms of national and international law enshrining civil, political, social, economic, cultural and environmental rights, and refrain from any act of collaboration—economic, financial or services—with entities, institutions or individuals perpetrating human rights violations.
- The rights granted to investors under the treaty should be subject to the principles and obligations established in general international law, including those relating to

human rights, the environment, and national and international legislation on racial and religious crimes and sexual discrimination.

- Activities should be carried out in accordance with national environmental laws, regulations, administrative practices and policies, and in conformity with international agreements, principles, standards, commitments and objectives relating to the environment, human rights, public health and safety, respectively.
- Be legally responsible for any environmental liabilities caused by them, and assume the obligation to compensate the affected people and communities for the resulting damages, and, where appropriate, repair such damages by restoring the environment to pre-intervention conditions, and/or financially compensating whoever is legally entitled to compensation.
- Comply with national standards and ILO international agreements to ensure that a safe and healthy working environment is provided; pay wages guaranteeing a decent living for workers; and ensure freedom of association, effective recognition of collective bargaining, the right to strike, and the rights of migrants.
- Territorial rights of indigenous and Afro-descendant peoples should be respected through acceptance of the results of prior and informed consultation following validation by the state, in accordance with Article 57 of the Constitution and Article 83 of the Organic Law on Citizen Participation.
- The ILO Convention 169 and the UN Declaration on the Rights of Indigenous Peoples must be respected. Consultation and participation rights are inalienable and non-delegable for the establishment of relations with states, companies and other stakeholders.
- In order to avoid tax evasion, tax avoidance or illicit intra-firm capital flows, the identity of the counterparties with whom commercial and/or financial practices of any kind are carried out must be made public. Transfer pricing should be minimized and part of their profits should be reinvested in accordance with national legislation or regulations.
- Actions must be subject to the intellectual property, science and technology policies and programs of the recipient countries and to international human rights standards.
- Performance must be in compliance with the requirements determined by the applicable internal

legislation. A contribution must be made to the transfer of technology, under the terms established in the law, national regulations or contracts.

- The BIT should include performance requirements for foreign investment. At present, foreign investment does not have performance parameters that must be met in the execution of its activities.
- National labor should be hired, preferably from the investment's areas of influence.
- In the event that the possibility of investment arbitration is included in the BIT, we propose to indicate that the state should confirm its consent to arbitration on a case-by-case basis. The state's consent to arbitration must take into account the investor's compliance with the obligations established in the approval of its entry into the country. We recommend incorporating the mandatory requirement that all domestic remedies, both administrative and judicial, be exhausted before proceeding to international investment arbitration.

Investor privileges to be excluded and rights to be reconsidered

We recommend that the following clauses, which are often present in existing BITs, be excluded or reconsidered in any future investment treaties:

- **Fair and Equitable Treatment:** The purpose of this clause is to fill gaps with other more specific norms, in order to potentially obtain a higher level of protection for the investor than that established in the treaty. Its scope must therefore be strictly defined, so as to prevent interpretations that conform to investors' expectations as a criterion for establishing the parameters of the state's international responsibility.
- **Full Protection and Security:** The full protection and security clause should be replaced by an international standard of minimum security and treatment.
- **National treatment:** This clause shall apply only with respect to the operation, management, maintenance, use and sale or transfer of the investments. National treatment should not extend to existing or future laws and regulations established for the benefit of small and medium-sized domestic enterprises or those relating to the regulation of natural resources. The State shall reserve its right to designate whichever sector to which it will not apply national treatment, due to national security and the need for the development of specific sectors.
- **Most Favored Nation:** This clause should be excluded in order to prevent investors of a certain

nationality from acquiring or extending their rights under various treaties entered into by the Ecuadorian State with countries other than the country of which the investor is a national. A clause should be included warning that the protection shall not extend to treatment established in existing or future regional economic integration agreements, customs agreements, trade agreements, free trade areas, or other agreements of similar subject matter; or in bilateral or regional investment protection and promotion treaties; and any preference system offered by the state to less developed countries.

- **Expropriation:** The concept of “indirect expropriation” or “measures equivalent to expropriation” should not be included. The definition of expropriation should be restricted to direct action by the state, as permitted by law, to appropriate an investor's tangible property for a public purpose, in accordance with due process and without discrimination, whereby, under the BIT, the state must pay adequate compensation within a reasonable period of time, in the context of the investment covered by the BIT.
- **Umbrella Clause:** The exclusion of this clause is proposed in the terms of the BITs signed by Ecuador, as it attempts to elevate the violation of a contract—an instrument of domestic law—to the violation of an international standard.
- **Survival Clauses:** We recommend setting a termination date with the possibility of renewal or renegotiation of the treaty by express agreement (not tacit or presumptive, as is currently the case) between the parties.

Likewise, any clause that:

- **Forbids the State from imposing performance requirements on investments.**
- **Bar the application of limits and rules to the free flow of capital.** This type of clause is especially dangerous in a country like Ecuador, which does not have its own currency and, therefore, has no control over exchange rates.
- Restricts the State's ability to establish rules and procedures to prevent tax evasion and avoidance or covert mechanisms for capital flight or money laundering. In tax matters, foreign investments should be subject only to Ecuador's domestic law and not to an investment treaty, from which it must be expressly excluded.

3. On the international arbitration system in investment matters

On the investor-state dispute settlement clause

The Commission recommends that the investor-state dispute settlement clause be excluded from existing and future International Investment Protection Treaties (BITs) that would allow investors to sue the state before international tribunals under ICSID or UNCITRAL rules.⁹⁶ In its current form, the investor-state dispute settlement clause grants excessive rights to foreign investors, and has resulted in abuses by foreign investors. For the most part, national courts are the ideal instrument for resolving investment disputes.

Legal security for investors in national courts

As a matter of priority, the Commission recommends that disputes between investors and the state be resolved in the national courts. Ecuador has a judicial system capable of transparently and impartially hearing and resolving potential claims from foreign investors.

Proposals for a transition period to minimize Ecuador's exposure to investor claims, for as long as the state is still tied to the current system of international investment protection.

Even if the Ecuadorian government takes actions to recover full sovereignty over its regulatory space and avoid future lawsuits by foreign investors before international tribunals, given the ultra vires clause, it will be a long time before it is completely free of the commitments assumed in the context of the current system of international investment protection.

In order to minimize the possibility of lawsuits (and threats of lawsuits) by foreign investors before international arbitration tribunals under ICSID or UNCITRAL rules, as well as to limit the investors' rights and the abusive interpretation of some BIT clauses by the arbitrators involved, the following actions are proposed for this transition stage:

On claims before the ICSID

In the event of a new claim by a foreign investor against Ecuador before the International Centre for Settlement of Investment Disputes (ICSID), we recommend that Ecuador decline to file a claim.

In 2009 Ecuador denounced the Washington Convention and thus withdrew its consent to be sued before the ICSID. The Commission thus understands that under no circumstances does the ICSID have jurisdiction to resolve disputes against Ecuador initiated after termination, much

less after the six month period for the termination to take effect, in accordance with Article 71 of the ICSID Convention.

On the interest on the amounts of awards in cases against the State

By affirming national juridical sovereignty, the prohibition of anatocism established in the Ecuadorian Constitution should be respected in the awards establishing the cumulative application of interest on amounts.

Conflict criteria that raise doubts as to the independence and impartiality of arbitrators

Given the evidence of pro-investor bias on the part of those who regularly serve as arbitrators, we propose the adoption of a set of criteria and principles by which arbitrator selection and recusal strategies can be developed. These criteria would help Ecuador to identify a “list of arbitrators with a pro-investor bias” who should be excluded from nominations to arbitral panels, and those who should be recused as members when proposed by the investor or as presidents of the tribunal proposed by the institution responsible for arbitration. The proposed criteria fall into three categories: “conflicts of interest”, “conflicts of issues” and “systemic conflicts”.

- a. “Conflicts of interest” refer to the arbitrator’s lack of impartiality as a result of relationships with the parties to the dispute and/or financial interests in the dispute's outcome.
- b. “Conflicts of issues” refers to cases in which the arbitrator's impartiality is questioned because the arbitrator has taken a clear position on a legal issue more than once and previously on one or more of the issues to be discussed in any new case.
- c. Lastly, with “systemic conflicts”, the arbitrator's impartiality is questioned, not because of involvement in a specific case, but rather because of positions or roles that may indicate that a pro-investor bias and/or defense of and advocacy for the traditional investment arbitration system.

Reforms to the international arbitration system

There are a series of reforms to the international investment arbitration system that, without totally denying the investor recourse to domestic arbitration, reduce the possibilities of abuse and provide greater guarantees of impartiality and independence. However, even the implementation of these reforms will not solve the problem of investors being able to challenge legitimate measures adopted by the State in favor of its citizens or

the environment.

Proposal to make arbitration the last resort

- Ensure that domestic administrative and/or judicial remedies have been exhausted before international arbitration is initiated.

Proposals to increase transparency

- The principle of transparency should be transversal throughout the system. Accordingly, all documents submitted by the parties and issued by the arbitrators should be public and freely accessible. Likewise, hearings on jurisdiction, merits and/or damages should be public and open to the participation of interested parties, including the use of new digital means of communication (e.g. live streaming). In addition, the participation of interested non-disputing parties, such as civil society organizations, should be allowed through appeals such as *amicus curiae*. Finally, the court or the parties should not be able to justify a lack of transparency due to reasons of confidentiality.

Proposals that seek to restrict arbitrators' discretion and increase their independence and impartiality

- Create an appeals procedure and a permanent appeals body to review the merits of awards (following the institutional design of the WTO),⁹⁷ while being aware that appeals will not solve the system's shortcomings.
- If the practice of submitting the review or annulment of awards to ad-hoc arbitration tribunals is maintained, their independence must be ensured. The members of this annulment tribunal should not act as arbitrators or as counsel to the parties within the institutional circuit of international investment arbitration; these tasks are incompatible with that of reviewing the performance of other arbitrators and impartially deciding whether the decisions in question should be annulled. A comprehensive list of highly recognized arbitrators from diverse backgrounds, dedicated exclusively to reviewing annulment proceedings, should be established.⁹⁸
- Create a binding code of conduct for arbitrators that includes, at a minimum, all of the above conflicts of interest and issues. Ideally, some of the elements of systemic conflicts should also be included, such as the prohibition that the arbitrator also acts as a representative of the parties.
- A cap should be placed on the fees that arbitrators can

charge.

- Allow for the conclusion of interpretative agreements between the signatory states, without the need for the intervention of an arbitration or judicial body and based on the clauses of their treaties, in order to reduce the arbitrators' freedom of interpretation.
- Relax the standard for resolving challenges to arbitrators. Decisions on disqualification of arbitrators should be based on a lack of appearance of independence and impartiality from the perspective of a third party reasonably evaluating the available evidence, and based on a comprehensive list of potential conflicts of interest detailed in the binding code of conduct.
- The decision on the challenge of arbitrators should never be made by the co-arbitrators or the directors of the institution conducting the arbitration, but by an independent panel with no other professional ties to the investment arbitration system.

Ecuador should seek to implement these reforms in different international and regional forums.

At the international level, such reforms could be implemented as part of a package of reforms to the ICSID and UNCITRAL rules, or as reforms in arbitration centers such as the Permanent Court of Arbitration and the International Chamber of Commerce.

At the regional level, the UNASUR Dispute Settlement Center has the enormous advantage of providing a forum for the resolution of investment-related disputes outside the orbit of influence of the WB, the US and the EU. Within the possibilities that the state of progress of the negotiations may offer, we recommend that Ecuador propose the above-mentioned reforms to improve negotiation design.

Permanent International or Regional Court of Investment Arbitration

Notwithstanding the development and conclusion of the UNASUR Investment Dispute Settlement Center negotiation process, the Commission suggests consideration be given to supporting the proposal for the creation of a permanent international court to settle disputes between investors and states.⁹⁹

While this proposal does not remedy the fact that investors continue to enjoy extensive rights enshrined in existing (or ongoing ultralife) BITs, nor does it ensure that judges appointed are not the same individuals who currently serve as arbitrators, nor that they are free from similar ideological interests and biases as the arbitrators,

the creation of a court with a body of standing judges, as an autonomous entity or as part of another existing institution, rather than ad hoc arbitrators, has the potential to help eliminate the conflicts of interest and bias currently present in the arbitration system. This would have the effect of isolating judges from external economic interests. This could also help to ensure greater consistency in the interpretation of applicable rules and decisions. The creation of said court should not be a pretext for the signing of new investment agreements.

4. International Observatory on Investment and Transnational Corporations

We recommend using the Commission's wealth of information and methodologies to create an Observatory of Transnational Corporations and Interests.

5. Recommendations concerning the state's scope to minimize contingencies

Based on the analysis of the investment arbitration cases against Ecuador, we observe that the state has faced claims for acts carried out in the exercise of its regulatory powers. In order to prevent future conflicts, we recommend the adoption of state policies to avoid conflict escalation.

Comprehensive public policy for investment protection

One of the highlights of this audit is an alternative treaty model useful for potential new bilateral and multilateral treaties, as a medium-term solution that takes into account the probable continued validity of the BITs after their termination. It is, however, essential that the government take the fundamental decision to implement a series of policies that will allow for a coherent and integrated management of foreign investment.

The instruments of these policies must define the investment methods, as well as the conditions to which the investor is subject, and the protection and security guarantees offered by the Ecuadorian State when exercising and receiving the benefits of successful investment management. It must contain mechanisms to ensure that the destination of foreign investment follows the priorities set forth in national planning, particularly in the context of new productive matrix. It should also indicate specific considerations in the case of foreign investments in strategic areas, sectors and activities, which must be safeguarded for national security, broad spectrum collective services and natural resources under protection and in environmental reserves.

Likewise, public policies should serve to guide foreign investment qualification processes and stipulate that they include general performance requirements such as minimum labor utilization rates, transfer of technologies aimed at innovation and increased value added, labor training components, productive supply chain conditions and other specific elements in accordance with the sector in question.

The transparent flow of capital must also be safeguarded and mechanisms must be put in place to regulate and control forms of tax evasion used by foreign firms when investing and conducting business operations in the country.

State of public records, non-existence and concealment of information

One of the serious drawbacks that the Commission encountered when conducting its audit was the deplorable state and, at times, non-existent public archives of some public institutions. We noted a lack of institutional memory, the disorganization of archives, the physical shifting of archives (which has led to the loss of documents) and a lack of knowledge of the current public servants in charge of archives regarding information that their respective institutions possessed in the past.

In some cases, a failure to digitize archives, poor handling of documents, and the loss of information due to aging documents in poor condition have led to the loss of the public administration's documentary history. Public archives should therefore be modernized, organized and digitized, to ensure that documents do not depend on public officials, and can remain for future reference.

We should point out that in the information search process, the Commission has encountered difficulties in accessing archives and identifying documents therein. The Commission's requests for information from different institutions were sometimes met with a response stating that the documentation did not exist, implying that it may have been concealed. This led to a prolonged investigation by the Commission and the absence of the elements required for the audit to be carried out.

Professionalization of Public Administration

One of the most important aspects for strengthening public administration is the training of public servants. Those responsible for the negotiation or review of international investment treaties and the administration of government contracts should endeavor to prevent possible contingencies during the negotiation and drafting of such treaties. In the future, they should avoid the escalation of conflicts and seek solutions that benefit the country. This

requires the professionalization of public servants, so that their work responds to the needs of the state and not of governments.

The state apparatus must be consolidated and guided by policies and guidelines that guarantee legal security in all aspects. Investment is thus promoted under clear rules that encourage the realization and execution of large-scale investment projects. These objectives should also encourage greater transparency in the management of public administration, while avoiding conflicts of interest.

Recommendations regarding speculative activities, tax evasion and capital flow control

The audit's findings include the figure of thin capitalization—the entry of capital as credits instead of investment—which has been used by foreign companies in a progressive and recurrent manner since the 1990s. The formation of consortiums and subsidiaries to hide or disguise capital flows is also presumed. The audit suggests setting up detailed investigation bodies for cases, including legal cases, to determine the magnitude of the damages caused to the state throughout the time of the company's operations.

Creation of a new metric to evaluate the behavior of foreign capital.

The global investment system has directed the type of metrics used to monitor Foreign Direct Investment (FDI) in different countries. FDI statistics are based on the application of IMF manuals, but do not provide information to quantify the impact of FDI. This is because they focus on measuring inflows and outflows of investment, rather than on the characteristics of these investments.

The creation of a new metric is required to evaluate and monitor the behavior of foreign capital in terms of criteria associated with constitutional rights, prospective planning for Good Living, and current regulations such as: generation of added value, employment generation, technology transfer, and tax contribution. Since several public institutions are involved in the collection, monitoring, systematization and verification of investment data, we suggest that the policies or guidelines outlining the new metrics be developed in an inter-institutional manner by the national statistical system.

Using this new investment metric, a decision-making tool should be designed enabling the responsible public authorities to define the level of protection provided to the investor and the appropriate instruments that would promote investment complying with the Constitution, the Plan for Good Living, and the law. It must also provide

criteria to design and monitor full compliance with the performance requirements agreed to by the investor, in the case of signing investment contracts. One example of a decision tool is presented in the corresponding annex of the CAITISA Final Report.

Due to its innovative nature in the region, the generation of this new metric requires a new institutional framework, or the generation of innovative capacities in the national agencies responsible for FDI monitoring. Likewise, we need to adjust statistical information systems and administrative records in order to gather reliable information.

93 We should point out that many of the recommendations presented are based on new types of treaties that have been signed in other regions. For example, the ASEAN Investment Treaty (2011) contains provisions on the environment, labor rights, and safeguards on the basis of health, morals and welfare. The United States Model Treaty also contains such safeguards. A model treaty recommended by the Commonwealth Secretariat contains similar provisions. The draft model treaty for the Southern African Region is also similar. While the recommendations included here do not deviate from modern trends in the field, they may express them in a more definite way.

94 Sustainable development (SD) is an integral concept that takes into account environmental protection and human rights. The Brundtland Commission Report defined SD as development that meets the needs of the present without compromising the ability of future generations to meet their own needs. SD has been mentioned in several treaties, such as the 1992 European Economic Area (EEA) Agreement, the preamble of the WTO Agreement and Article 19 of the ECT. Several courts and tribunals have also mentioned SD, in notably the International Court of Justice (ICJ) in the *Gabcikovo - Nagymaros case (1997)* and the *Advisory Opinion on the Legality of the Threat or Use of Nuclear Weapons (1996)*.

95 Many of the obligations listed here arise from the proposal for an International Peoples' Treaty on Controlling Transnational Corporations developed on a global scale by the Campaign to Dismantle Corporate Power <http://www.stop-corporateimpunity.org/wp-content/uploads/2015/02/PeoplesTreaty-EN-dec2014-1.pdf>

96 Given this scenario and contrary to the argument generally presented, in the event of suffering a non-commercial loss on their investments (investors should be prepared to assume commercial risks), they would not be left unprotected, since they would have the possibility of resorting to:

* Private political risk insurance: this covers both assets and contracts. Asset coverage may include risks such as confiscation, nationalization and expropriation. Contract coverage may include

losses due to repudiation of the contract, currency inconvertibility, and contract termination due to political violence. Policies for the seizure, nationalization and expropriation of insurance can generally be extended to cover license cancellations, trade embargoes, strikes, riots, loss of income following expropriation and other types of political risk. One thing to note is that for private political risk insurance, the existence of BITs is not relevant when assessing investment project risk.

* Under the World Bank's Multilateral Investment Guarantee Agency (MIGA) investors are provided with state-subsidized guarantees against losses caused by risks such as expropriation, currency inconvertibility, currency transfers, civil war or riots.

* Insurance offered by the investor's country of origin: Most capital exporting countries provide insurance coverage to their companies that invest abroad similar to that of the World Bank.

Likewise, in some circumstances companies' home states are inclined to offer some form of diplomatic protection: in some cases this includes the possibility of resolving state-state disputes, but informal channels also exist. Examples include tariff preference restrictions or other economic pressures that the home state has successfully exerted on the investor's host state.

97 Under current ICSID rules, annulment of the award can only be sought on the basis of narrow criteria, such as excess of power of the tribunal or procedural non-compliance. The mechanism is highly insufficient in ensuring the system's integrity.

98 Ziadé, Nassib (2015) Is ICSID heading in the wrong direction?, *Global Arbitration Review*, 24 February <http://globalarbitrationreview.com/news/article/33574/is-icsid-heading-wrong-direction/>

99 A proposal for an International Investment Court that we consider an actual improvement to the system is that originally made by Professor Gus Van Harten in 2008 (see: Van Harten, Gus, (2008) A Case for an International Investment Court, Society of International Economic Law (SIEL) Inaugural Conference. Available at SSRN: <http://ssrn.com/abstract=1153424>) and not that one currently proposed by the European Commission (http://trade.ec.europa.eu/doclib/docs/2015/may/tradoc_153408.PDF).