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The Collateral Effect of an International Arbitration Award: A Capital Markets View

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The current state of affairs of arbitration within Latin America looks challenging. Many countries are having upcoming ICSID awards which could amount to tens of billions of dollars against them. Most international bonds have a final judgment event of default (EoD), which could lead to a default bond scenario on the sovereign debt of such Republic. Some Bonds from Sovereigns list the following event of default:

> "…there shall have been entered against the Republic…a final judgment, decree or order by a court of competent jurisdiction from which no appeal may be made, or is made, for the payment of money in excess of U.S.$100,000,000 or its equivalent and 30 days shall have passed since the entry of any such order without it having been satisfied or stayed."

In the case of International Oil Companies (the "Company") the wording of some Bonds is regularly similar:

> "…one or more judgments in an aggregate amount in excess of U.S. $100 million shall have been rendered against the Issuer or any of its Significant Subsidiaries and such judgments remain undischarged, unpaid or, unstayed, unbonded or not suspended by agreement for a period of 60 days after such judgment or judgments become final and non-appealable."

Typically, an ICSID or international commercial arbitration award (ICC, LCIA, SIAC, ICDR, among others) award may trigger an EoD but they need to be converted into a local enforcement order. Failure to pay the awards mentioned before would constitute an event of default on the external Bonds.

Article 54 of the ICSID Convention (the "Convention") obliges to enforce an ICSID award "as if it were a final judgment of a court in that state", the State must recognize and enforce awards immediately and without review, but they may execute them pursuant to their own national law. An international commercial arbitration award (ICC, SIAC, ICDR, among others) would be enforceable under the New York Convention against the Company, since it enacts a general

requisite that contracting states recognize arbitral awards made in other countries (Articles 3 and 4 of the New York Convention).

Most Countries and Companies pay ICSID and international commercial arbitration awards or settle prior to the issuance of the award. If Courts deny the enforcement, claimant could enforce the award on another state party to the New York or ICSID Convention (depending on the case). Of the ICSID case load registered until January 2010, only 4 out of 271 cases have concluded on execution proceedings.

EoDs may be remedied, however, if the Country or the Company decline to pay an award or to reach a reasonable settlement once the award is rendered it might trigger consequences on the Bonds. Bondholders would be entitled to accelerate at any time. However, 25% of the bondholders would have to agree on that. Depending on the Bond and if some investors hold lower price Bonds or if they hold Credit Default Swaps (CDS) this scenario could be possible. On the other hand, it could be counterproductive, since the Country and the Company would stop paying coupons, and a long and cumbersome legal process in order to recover the pending amount would start.

Once the local enforcement order is rendered, the phase of execution begins and the collection of money from the Country or the Company based on those enforcement orders can be challenging. The Country assets located in the US that are used for a commercial purpose would be the first target; the Country embassy bank account would be immune. Moreover, any money obtained by the Country Ministry of Finance following an initial bond offering in New York would be an objective.

Consequently, the Country, and possibly the Company, would be losing direct access to international financial markets. The issuance of the Bonds would then be domestically, the local investor will then sell it offshore. The Country might face disruptions to its oil export business, since creditors would try to seize such exports or payments to them to seek relief.

Nevertheless, there are restrictions by the domestic law of the place of enforcement on sovereign immunity and public policy which could jeopardize the ability to enforce against the Country or Company (see Article 55 of the ICSID Convention). In addition, the Country or Company may seek to create a disruption by applying to annul an award in the domestic courts or before an ICSID ad hoc committee (depending on the case). The ICSID annulment procedure can lead to substantial delays in procuring payment under an award which could add up considerable time.

The views contained in this article only express a personal scenario on possible international arbitration trends.

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This entry was posted on Thursday, February 5th, 2015 at 7:55 am and is filed under Bonds, ICSID Arbitration, ICSID Convention
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