

ENFORCING AWARDS AND STATE OWNED COMPANIES

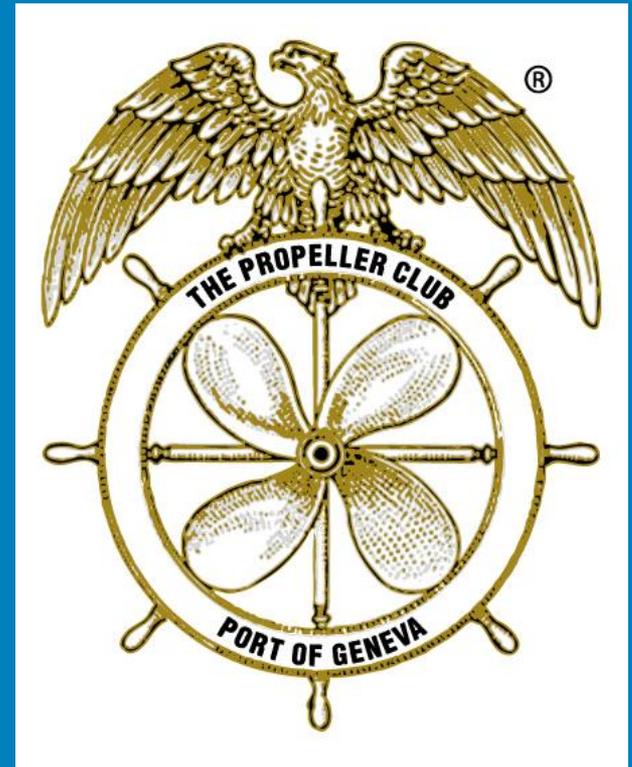
HOTEL BRISTOL, GENEVA

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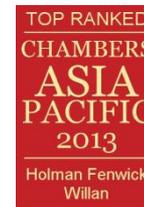
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SOMO -v- Taurus

- State Oil Marketing Company of the Ministry of Oil, Republic of Iraq (SOMO) v Taurus Petroleum Limited
- Original arbitration relating to commercial transactions between September 2004 and 31 December 2007
- Taurus claimed for:
 - Demurrage under sale contracts under which SOMO sold oil to, and purchased LPG from, Taurus
 - Unpaid war risk premiums
 - Monies improperly claimed by SOMO under performance bonds
- NB: Although the hearings were held in London with an English QC as the arbitrator, it was governed by Iraqi law and its 'legal seat' was Baghdad



The result of the arbitration

- Taurus won 95% of the demurrage claimed
- Under a Final Award in February 2013 it was awarded:
 - Damages of \$6,959,972
 - Interest of \$869,996
 - Costs of \$886,507
- But SOMO refused to pay...



What can you do when you win but are not paid?

- There are a number of potential ways to enforce an award
 - Where can you find the debtor's assets?
 - Are the rules of that jurisdiction helpful?

- Local enforcement proceedings in the country in which the award debtor is incorporated
 - E.g. Statutory Demand in England, leading to the company being wound up if payment is not made

- Arresting money in bank accounts, for example:
 - New York Rule B attachments
 - Swiss Poursuite
 - English freezing injunction

- Ship arrests for maritime claims

- May not have significant assets outside the state in which they are based, and proceedings there may not be appealing
 - It may not be a very sophisticated jurisdiction
 - Taking on a state entity in its own country's courts may be problematic
 - How its assets are held may not be transparent

- Any assets that are outside its home-country may be subject to sovereign immunity
 - Nearly all jurisdictions recognise some concept of sovereign immunity
 - Very wide definition of sovereign 'property' under English law
 - Difficult question of whether a state-owned commercial entity is part of the state

A solution

- In England, in order to enforce a judgment, two effective methods are to:
 - Obtain a 'Third Party Debt Order' ("TPDO") and/or
 - Get a receiver by way of equitable execution appointed
- Does not have to be an English award, any award can be converted into an English judgment
 - New York Convention 1958
 - Common law
- This makes the award due as a judgment in England, and allows the judgment creditor to access all of English law's remedies to enforce within the jurisdiction



- Under a TPDO the court orders a third party who owes money to the award debtor, to pay that money to the judgment creditor instead
 - Must be a debt 'due and accruing'
 - Two stage process
 - An Interim TPDO freezes the asset
 - Then, after a hearing, a Final TPDO can be made to have the money paid over by the third party

- Similarly a receiver by way of equitable execution can be appointed, who will be able to order third parties to pay money to the judgment creditor
 - Must have no other way of enforcing the judgment
 - The debt does not have to be 'due and accruing', so it can be a debt that is owing in the future

- Information is crucial
 - Where are the debtor's assets?
 - Who owes money to the debtor?

- Taurus was aware of a particular SOMO cargo
 - The b/l was for around \$220 million dollars of oil being sold by SOMO
 - It showed the names of the buyer and the financing bank

- Using this information Taurus applied to the Commercial Court in London for:
 1. The Arbitration Tribunal's Award to be entered as a court judgment
 2. Interim TPDOs against the buyer and their financing bank
 3. An order allowing Taurus to appoint a receiver

- The court granted the orders

- Once the orders were made the financing bank had to disclose the letter of credit under which they would owe SOMO the price of the oil cargo
- The bank then had to disclose when a presentation had been made
- The l/c provided for payment to be made into the Central Bank of Iraq's ("CBI") account at the Federal Reserve Bank of New York
 - Payment from the sale of all of Iraq's (non-Kurdish) oil is made into this account
 - 5% is then deducted and paid to Kuwait in reparations for the Gulf War
- After negotiations with their solicitors, the buyer's bank paid the money that SOMO owed under the award into court, pending the outcome of the final hearing
- SOMO then brought a challenge to the orders on the basis of sovereign immunity

Sovereign immunity

- Sovereign immunity is a judicial doctrine that prevents states being sued without their consent
- It stems from the ancient English principle that the King can do no wrong
- Under English law the immunity of foreign states is now governed by the State Immunity Act 1978
- Whether a state-owned company is counted as being part of a 'state' is a difficult issue



- There are state-owned entities in a wide range of industries across the world:
 - Oil companies – Saudi Aramco
 - Oil refineries – RECOPE owned by the Costa Rican government
 - Railway companies – SBB CFF FFS owned by the Swiss government
 - Shipping companies – COSCO owned by the Chinese government
 - Central Banks
 - Commercial banks – RBS Group 81% owned by the UK government
 - Mining companies – LKAB owned by the Swedish government
 - Airlines – Air New Zealand

- Whether or not each of them is able to claim state immunity will depend on the circumstances

- SOMO relied on a number of provisions of the State Immunity Act
 - Under s13 the property of a state cannot be used for any enforcement proceedings
 - However there is an exception for "*property which is for the time being in use or intended for use for commercial purposes*"
 - Under s14 a state does not include "*any entity which is distinct from the executive organs of the government of the State*"
 - Unless "*the proceedings relate to anything done by it in the exercise of sovereign authority*"
 - Or the property of the state's central bank s14(4)



s13 of the State Immunity Act 1978

- "(2)(b) the property of a State shall not be subject to any process for the enforcement of a judgment or arbitration award."

BUT

- "(4) Subsection (2)(b) above does not prevent the issue of any process in respect of property which is for the time being in use of intended for use in commercial purposes. "

s14

- "(1) The immunities and privileges conferred by this Part of this Act apply to any foreign or commonwealth State other than the United Kingdom; and references to a State include references to –
 - ... (b) the government of that State; and
 - (c) any department of that government

But not to any entity (hereafter referred to as a "separate entity") which is distinct from the executive organs of the government of the State and capable of suing or being sued."

- SOMO disputed the jurisdiction of the English court, saying that it enjoyed sovereign immunity and that the funds arrested were also protected

- Regarding SOMO's status, it argued that though it was legally a separate entity, it was so close to the Iraqi state (which they said controlled it completely) that it should be treated as if it were the Iraqi state

- Regarding the nature of the funds that had been arrested, SOMO argued that although selling oil might look like a commercial activity, it was in fact an exercise of sovereign authority because under Iraqi law all the proceeds from selling oil belong to the state
 - Article 111 of the Iraqi Constitution: "*Oil and gas are the ownership of all the people of Iraq in all the regions and governates*".

- The court reviewed SOMO's 'Declaration of Incorporating', its official mandate of activities, its State-derived rights, Board of Directors, decision-making process and its relationship with the Iraqi Ministry of Oil
- The court found "*It is beyond argument that SOMO is a separate juridical entity formed by the State for commercial or industrial purposes, with its own management and budget and accordingly ... there is a strong presumption that its separate corporate status should be respected.*"
- It concluded that:
 - "*this presumption has not been rebutted ... whilst the Ministry of Oil exercises a close overall supervisory function over the operations and affairs of SOMO, SOMO is not part of the Republic of Iraq but is an entity separate from the Iraqi state*"



The status of the arrested money

- When assessing whether a state's 'property' has been arrested, the definition of property is very wide, it includes:
 - *"all real and personal property and will embrace any right or interest, legal, equitable, or contractual in assets that might be held by any "emanation of the State" AIG Capital Partners Inc v Kazakhstan [2006]*
- However the court found that the assets arrested were being used commercially, and so SOMO could not claim sovereign immunity
 - *"the question is not whether the acts of SOMO in selling oil to [the buyer] and procuring the opening of the credits were authorised by the state, but whether these acts were of a sovereign character. In my view, these acts were manifestly of a commercial character of the sort that any private citizen can perform and were not done in the exercise of sovereign authority".*



The arrest of a debt pt.1

L/C opened by Shell

at the...

Federal Reserve Bank
New York

Payable to...



SOMO

The arrest of a debt pt.2

The Judge in *Taurus v SOMO* held that the debt was payable by the FRBNY to SOMO **and** the Central Bank of Iraq as joint promisees.

Taurus maintain that the amount is only payable to SOMO and that the CBI is acting only as the collecting bank. This is a critical point for both parties.

The controversy over this point was caused by the wording of the L/C which reads:

"[A] Provided all terms and conditions of this letter of credit are complied with, proceeds of this letter of credit will be irrevocably paid in to your account with Federal Reserve Bank New York, with reference to 'Iraq Oil Proceeds Account'.

[B] We hereby engage with the beneficiary and Central Bank of Iraq that documents drawn under and in compliance with the terms of this credit will be duly honored upon presentation as specified to Credit C.B.I. A/C with Federal Reserve Bank New York.

[C] Special instructions to Central Bank of Iraq: upon receipt of your authenticated Telex/Swift confirming that you have taken up documents in strict conformity with credit terms and conditions and couriered them to us, we undertake to effect payment at maturity as per your instructions, provided that such Telex/Swift is received at least 1 New York/London banking day prior to due date. Otherwise, payment will be made 1 New York/London banking day later.

[D] If our cover does not reach you in time to reimburse you for your payment under the credit on due date, we hereby undertake to compensate you for any loss of interest incurred by you due to this delay.

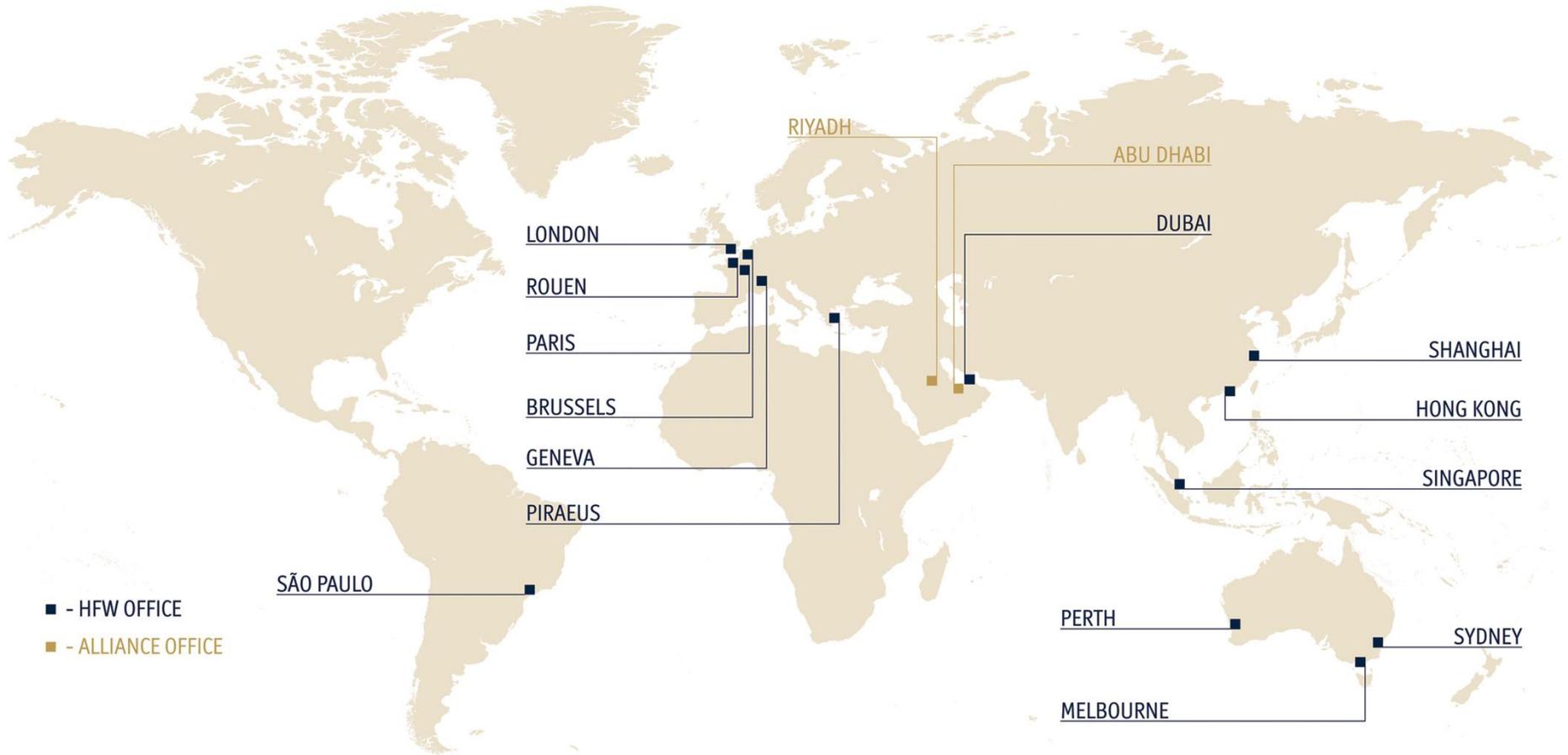
- The court rejected all of the sovereign immunity arguments that SOMO raised
- However, it found that the fact that the letter of credit stipulated that the money had to be paid into the CBI's New York account, meant that the CBI had an interest in the property arrested
 - As the property of a central bank enjoys sovereign immunity under s14(4) the court found that the orders had to be set aside
 - The court itself gave leave to appeal against this aspect of its decision, which will be heard by the Court of Appeal later this year
- The court recognised that the money was still owing to Taurus by unusually setting-off SOMO's costs against the amount of the Award and only allowing SOMO a very small percentage of its costs.

- Iraqi Kurdistan is a relatively stable region in the North West part of Iraq which produces large quantities of its own crude oil.
- Arguments have raged between the Kurdistan Regional Government ("KRG") in Erbil and the government in Baghdad as to who has the right to sell Kurdistan's oil.
- Until recently 2 million barrels of oil were in tanks, unused and without a buyer at the Turkish port of Ceyhan due to the arguments concerning who has the right to sell the oil: KOMO or SOMO?

- On 22 May 2014 a million barrels of the oil at Ceyhan was lifted onto the United Leadership.
- The vessel is currently anchored just off the coast of Morocco.
- SOMO, on behalf of the State of Iraq, have applied to the ICC to commence arbitration proceedings against the Turkish Ministry of Energy and BOTAS, Turkey's state owned pipeline company.
- It is believed that they are bringing proceedings under the Iraq-Turkey Pipeline Treaty ("ITPT").
- Presumably this will include an argument that SOMO holds the sovereign right to distribute the Iraqi oil (including that of Kurdistan) and that the Turkish Ministry and BOTAS have breached that right.
- What is certain is that once this is resolved, millions of barrels of oil will suddenly become available...

- Dealing with state-owned entities can bring particular difficulties because of the special rules that apply when states are involved in litigation
- They have an extra layer of protection against claims for their assets – however there are still ways in which they may have awards or judgments enforced against them
- The SOMO -v- Taurus judgment shows how it may be possible to arrest the funds of third parties owed under a sale contract or a letter of credit
- A state-owned entity will now be unable to claim sovereign immunity when, like SOMO, it is a separate entity with its own decision-making and engaged in buying and selling in the commercial marketplace

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