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Fight against Corruption and Fraud
in Investor-State Dispute Settlement

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Introduction

- Anti-corruption regulation

 - Ex. The UN anti-corruption Convention (2004)

 - Ex. The OECD Anti-bribery Convention (1997)

 - obligation to criminalise in domestic law

 - no international court of anti-corruption

 - implementation by each State

 - expectation on function of **ISDS** as anti-corruption mechanism

- **ISDS** = to protect foreign investors and investments
 - Respondent: corrupt investments should not be protected under IIA and ISDS
 - ‘sanction’ imposed by ISDS?

- Analysis
 - I. **Anti-corruption mechanism** of ISDS
 - II. **Limits** of anti-corruption mechanism
 - ISDS = trans-border criminal institution?

I. Anti-corruption mechanism in ISDS

1. Application of the **legality clause** to exclude corrupt investments

- ‘Legality clause’ = investment shall be established **in accordance with the laws and regulations** of the host State.

Ex. *Metal-Tech* [2013]: ‘corruption is established to an extent sufficient **to violate Uzbekistan law** in connection with the establishment of the Claimant’s investment in Uzbekistan. [...] **the investment has not been “implemented in accordance with the laws and regulations** of the Contracting Party in whose territory the investment is made”’

→ denied jurisdiction

2. Applicability of **MFN clause** to the legality clause

- can we use MFN clause to transport a legality clause of other IIAs?

- negative answer

→ *Metal-Tech* [2013]: ‘a MFN clause cannot be used to import **a more favourable definition of investment** contained in another BIT. The reason is that the defined terms “investments” and “investors” are used in the MFN clause itself, so that the treatment assured to investments and investors by Article 3 necessarily refers to investments and investors as defined in Article 1 of the BIT’.

→ MFN clause can be applied only to an investment **already established in conformity with** the definition of ‘investment’ under the applicable IIA.

3. Implicit requirement of legality under IIA

- requirement of legality → **implicitly** provided in IIAs
 - *Plama* [2008]: the silence of IIA ‘does not mean [...] that the protections provided for by the ECT [Energy Charter Treaty] cover all kinds of investments, including those contrary to domestic or international law [...]. The Arbitral Tribunal concludes that the substantive protections of the ECT cannot apply to investments **that are made contrary to law**’.
 - *Phoenix Action* [2009]: ‘this condition - the conformity of the establishment of the investment with the national laws - is **implicit even when not expressly stated in the relevant BIT**’.
- legality requirement is **implicit** in IIAs

4. Application of general principles

- Tribunals apply **general principles**: ex. clean hands doctrine, principle of good faith, international public order

- ***Hamester*** [2010]: ‘[a]n investment will not be protected if it has been created **in violation of national or international principles of good faith**; by way of corruption, fraud, or deceitful conduct’.

- ***Inceysa*** [2006]: Tribunal applied ‘generally recognized rules and principles of International Law’

 - = general principles of law (Article 38 of the Statute of the ICJ).

 - **General principles of law**

 - (i) the principle of good faith;

 - (ii) the principle of *nemo auditur propriam turbitudinem allegans*
(no one can benefit from his own wrong);

 - (iii) international public policy;

 - (iv) the principle that prohibits unlawful enrichment

▪ *World Duty Free* [2006] (bribery case):

‘bribery is **contrary to the international public policy** of most, if not all, States or, to use another formula, to **transnational public policy**. Thus, claims based on contracts of corruption or on contracts obtained by corruption cannot be upheld by this Arbitral Tribunal’.

Statute of the ICJ Article 38

1. The Court, whose function is to decide **in accordance with international law** such disputes as are submitted to it, shall apply:

a. international conventions, whether general or particular, establishing rules expressly recognized by the contesting states;

b. international custom, as evidence of a general practice accepted as law;

c. **the general principles of law recognized by civilized nations;**

d. subject to the provisions of Article 59, judicial decisions and the teachings of the most highly qualified publicists of the various nations, as subsidiary means for the determination of rules of law.

2. This provision shall not prejudice the power of the Court to decide a case *ex aequo et bono*, if the parties agree thereto.

5. Content of the international public policy

- What is ‘international public order’?

 - *private* international law

 - but, not *public* international law?

• *Inceysa* [2006]: ‘international public policy’ consists of ‘a series of fundamental principles that constitute the very essence of the State, and its essential function is to preserve the values of the international legal system against actions contrary to it’.

 - ‘international public policy’ = *private* international law, general principles of law (Article 38 of the ICJ Statute)

 - mixture of *private* and *public* international law

 - more close to ‘*transnational public policy*’ (constituted by international conventions, convergence of national laws, arbitral decisions, and scholarly opinion)

6. Summary of the anti-corruption mechanism in the ISDS

- illegal investment (ex. corrupt investment)
 - a) **legality clause** → application of legality clause
 - denial of jurisdiction *ratione materiae*
 - b) no legality clause
 - implicit legality clause
 - application of **general principles**
 - **international** public order
 - **transnational** public order

- Conclusion:
anti-corruption mechanism is effectively functioning in investment arbitration.

II. Limits of ISDS for functioning as anti-corruption mechanism

- **Unfairness**: respondent is also involved in corruption
- *WDF* [2006]: the then president of Kenya accepted a bribe and his country, Kenya, used this fact for denying the jurisdiction.

1. Requirement of examination at the merit phase

- denial of **jurisdiction** = no protection of (corrupt) investment
 - need a more flexible and balanced finding in **merits** phase
 - ex. bribe in the performance of investment
 - ≠ bribe at the establishment of investment

2. Involvement of the respondent in corrupt acts

- bribery is always based on the acts of **both** investor and host State
- Respondent is **estopped** from invoking the corruption defence

ex: *Fraport* [2007]: ‘[p]rinciples of fairness should require a tribunal to hold a government *estopped* from raising violations of its own law as a jurisdictional defense when it knowingly overlooked them and endorsed an investment which was not in compliance with its law’.

3. Causal link between corruption and investment

- the respondent has to prove **a causal link** between the alleged corrupt acts and the establishment of investment.

→ ex. *NIKO* [2013]: the tribunal admitted the existence of corruption, but ‘there is no link between the established acts of corruption and the conclusion of the agreements’.

- standard of ‘**decisiveness**’

→ *Hamester* [2010]: ‘[t]here is no conclusive evidence proving that Cocobad would not have entered into the joint-venture had it known that some of the figures were overstated. In other words, there is **no proof** that the alleged fraud was *decisive* in securing the JVA [joint venture agreement]’.

4. Burden of proof and standard of proof

- the **burden of proof** on the **respondent**

→ consequently, tribunals deny the proof of wrongful acts and a causal link between corruption and investment

Ex. *Hamester* [2010]: ‘having carefully considered all the evidence’, ‘the Respondent **has not fully discharged its burden of proof**’ to establish the fact that the joint venture agreement was procured by fraudulent behavior (over-statement of invoices).

→ burden of proof imposed on the respondent

→ limits the scope of anti-corruption mechanism of ISDS

→ in favour of the investors

5. Equal shares of proceedings costs by both parties

- normal cases [loser pay rule]: corruption → denial of jurisdiction → **claimant** is ordered to pay the fees of arbitration
- recent cases [equal pay rule]: corruption → denial of jurisdiction → **both parties** are ordered to pay the fees of arbitration

Ex. *Fraport* [2007]: the tribunal denied its jurisdiction *ratione materiae* → ‘there is **no successful party** on the merits in the traditional sense. Accordingly, the Tribunal [...] has formed the view that **each party** shall bear in full its **own legal costs** as well as **one half of the arbitration costs**, including the administration fees for the use of the Centre’.

- respondent **is involved** in the corruption
- it is fair to share the fees between the parties

6. Possibility of criminal punishment

a) ISDS is not criminal punishment system

→ ISDS = settlement of investment dispute between parties
(=**horizontal** system) ≠ criminal procedure (= **vertical** system)

b) Anti-corruption mechanism → contributes to **the rule of law**

Ex. *Metal-Tech* [2013]: ‘the outcome in cases of corruption often appears unsatisfactory because [...] it seems to give *unfair advantage to the defendant party*. **The idea, however, is not to punish one party at the cost of the other, but to ensure the promotion of the rule of law**, which entails that a court or tribunal cannot grant assistance to a party that has engaged in a corrupt act’.

Conclusions

I. Anti-corruption mechanism

- application of Legality clause (explicit or implicit)
- application of general principles
 - highly appreciated and expected

II. Limits of anti-corruption mechanism

- involvement of respondent → estoppel
- causal link, burden of proof (standard of decisiveness)
- equal share of arbitration fees
 - limited scope of anti-corruption mechanism
 - mitigated and balanced in the future

Thank you for your attention.
Grazie.

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