

Kyoto Seminar on International Investment Law

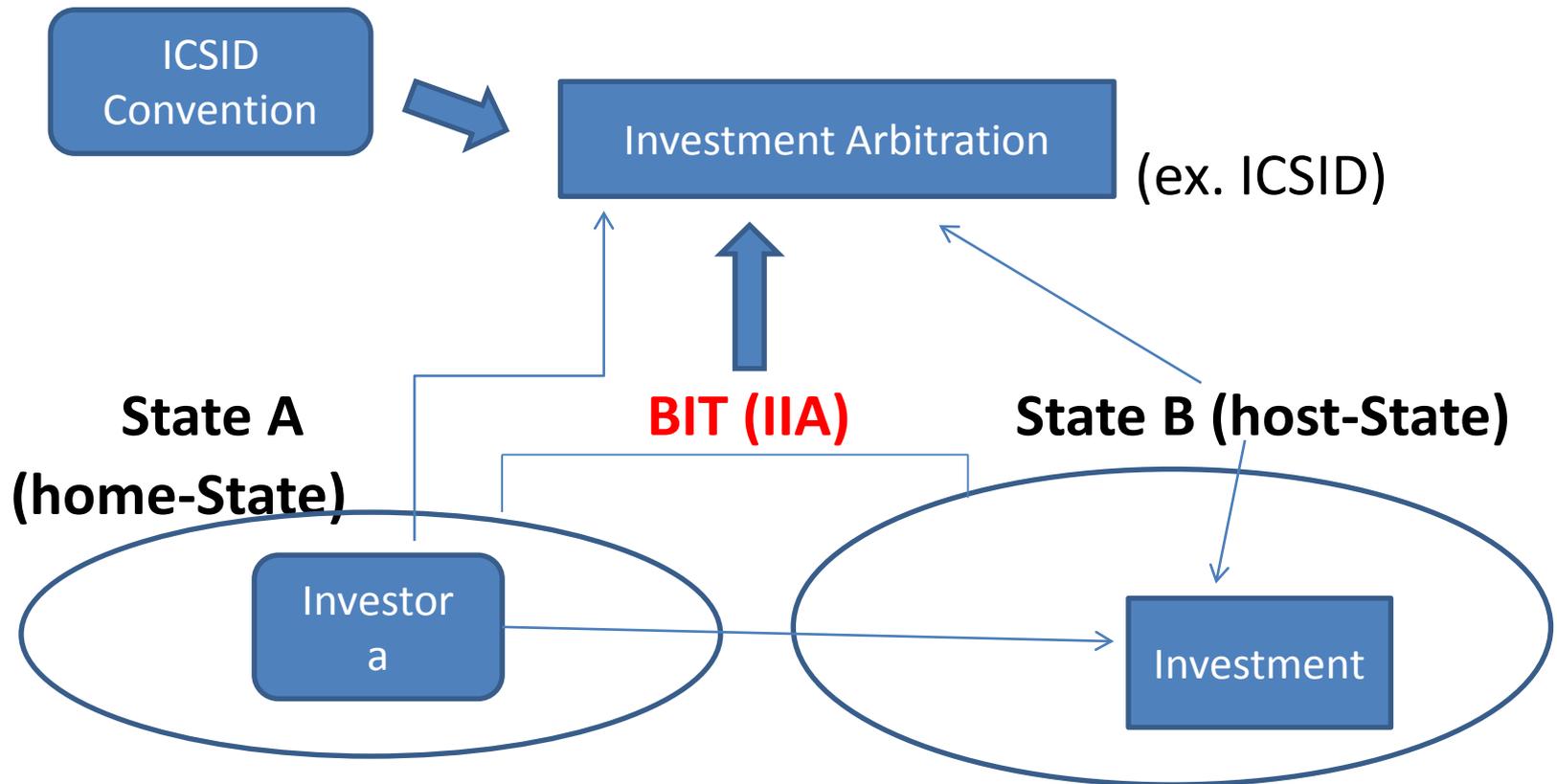
**Fight against Corruption  
and International Investment Law**

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# Introduction



# 1. Fight against corruption in international society

## 1. Domestic level

USA Foreign Corrupt Practices Act (FCPA) (1977)

## 2. International level

- **OECD Convention** on Combating Bribery of Foreign Public Officials in International Business Transactions (1997): obligation to criminalise the bribery of foreign public officials (Article 1 (1)), to punish the bribery (Article 3)
- OAS Inter-American Convention against Corruption (1996)
- The Council of Europe Criminal Law Convention on Corruption (1999)
- The African Union Convention on Combating Corruption (2003)
- **The UN Convention against Corruption** (2003)
- Committee on International Arbitration of **ILA** (2000)
  - ‘international consensus that corruption and bribery are **contrary to international public policy**’

## ▪ Evaluation

‘The international anti-corruption legal framework has been substantially strengthened in the past two decades, with impressive progress being made at both global and regional levels. Nevertheless, **the work is far from over**’.

Jan Wouters, Cedric Ryngaert and Ann Sofie Cloots, ‘THE FIGHT AGAINST CORRUPTION IN INTERNATIONAL LAW’, Leuven Centre for Global Governance Studies, Working Paper No. 94 (July 2012).

- limited to domestic application (criminalisation by domestic law)
- no implementation mechanism on international level
- overlapping with investment: sectors most prone to corruption are public work, construction, real estate and property development, oil and gas, heavy machinery and mining
- negotiation with government officials is required

## Corruption Perceptions Index (2013) by Transparency International

	Rank	Score
Denmark	1/177	91/100
Switzerland	7/177	85/100
Japan	18/177	74/100

Iraq (171), Libya (172), South Sudan (173), Sudan (174),  
Afghanistan (175), North Korea (175), Somalia (175)

## II. Fight against corruption in ISDS

- there is no IIA provision directly prohibiting corruption
  - solution 1 = application of 'legality clause'
  - solution 2 = application of general principles

### 1. Use of 'legality clause'

- investment protected by IIA
  - = investment established 'in accordance with the laws and regulations' of the host State
- more than 100 States ratified the UN Convention against Corruption
  - obliged to criminalise corrupt acts by its own officials
  - investment established through corruption is illegal investment
  - can not be protected by IIA and ISDS

## 2. Cases of application of 'legality clause'

### ***Fraport v. Philippines* [2007]**

- Claimant invested in a Philippine company (PIATCO) which was a party to a concession contract for the construction and operation of an international airport terminal
- Respondent claimed that Fraport's investment violated **nationality restrictions**, provided in its Constitution and the Anti-Dummy Law relating to those restrictions, and did not fall within the scope of the BIT investments.

### **ICSID finding**

- (1) Fraport 'was consistently aware that the way it was structuring its investment in the Philippines was **in violation of the [Anti-Dummy Law]** and accordingly sought to keep those arrangements secret'.
- (2) BIT **Article 1(1)** defined 'investment' as 'any kind of asset **accepted in accordance with the respective laws and regulations** of either Contracting State'.
- (3) Fraport understood the Philippine legal prohibition [...] but it proceeded with the investment **by secretly violating Philippine law through the secret shareholder agreements**.
- (4) Fraport 'cannot claim to have made an investment 'in accordance with law'. [...] the Tribunal **lacks jurisdiction *ratione materiae***'.

# ***Metal-Tech Ltd. v. Uzbekistan***

**ICSID Case No. ARB/10/3, Award (4 October 2013)**

- to obtain the approval of project by the Government, claimant gave a bribe

## **ICSID finding**

- Article 1(1) of Israel-Uzbekistan BIT defines investments as ‘any kind of assets, **implemented in accordance with the laws and regulations** of the Contracting Party in whose territory the investment is made’.
  - **‘implemented’** means **‘established’** (not ‘operated’)
- ‘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”’.
- Corruption (bribery) = breach of Uzbekistani law
  - **no (establishment of) investment**
  - tribunal **denied jurisdiction** (lack of consent of host-State)

### 3. Application of general principles

- Basic idea

= exclusion of **illegitimate** investments and expectation

- Wälde:

‘[t]here is ample jurisprudence that a legitimate expectation [of investors protected under the NAFTA] can not be created if **deception, fraud or other illicit means were used** to obtain the governmental assurance or other rights obtained from the government in this way. There can be no international treaty protection for rights **obtained by illicit means**. In such cases, there may be an expectation, but **not a ‘legitimate’ one**’.

*International Thunderbird Gaming Corporation v. United Mexican States*, UNCITRAL, Award (26 January 2006), Separate Opinion of Prof. Wälde, 2005.

→ only **‘legitimate’** investment should/can be protected under IIA and ISDS

## 4. International public policy (*ordre public*)

- if there is no 'legality clause' in IIA

  - alternative way = **international public policy**

- **Lagergren Award [1963]**

  - 'there exists **a general principle of law** recognised by civilised nations that contracts which seriously violate [...] **international public policy** are **invalid** or at least **unenforceable** and that they cannot be sanctioned by courts or arbitrators'.

  - '**corruption** is an international evil; **it is contrary to good morals and to an international public policy common to the community of nations**'.

## ***World Duty Free Co. Ltd. v. Republic of Kenya***

**ICSID Case No. ARB/00/7, Award (4 October 2006)**

World Duty Free (WDF) concluded a contract in 1989 with Kenya for the construction, maintenance and operation of duty free complexes at Nairobi and Mombassa International Airports. At the moment of the conclusion of contract, WDF made a **'personal donation'** of 2 million US dollars to Mr. Daniel arap Moi, then President of Kenya.

### **ICISD Finding**

- (1) donation 'must be regarded as a **bribe** made in order to obtain the conclusion of the 1989 Agreement'.
- (2) 'bribery [...] is sanctioned by **criminal law** in most, if not all, countries', in **the international instruments** concerning corruption, as well as in **the international commercial arbitration cases**.
- (3) **bribery is contrary to the international public policy** of most, if not all, **States** or, to use another formula, **to transnational public policy'**
- (4) 'claims based on contracts of corruption or on contracts obtained by corruption cannot be upheld by this Arbitral Tribunal'.

## ***Inceysa v. El Salvador* [2006]**

- illegal contract concluded through **fraud**
- no 'legality clause'

### **ICSID Finding**

- 'generally recognized rules and principles of International Law' = '**general principles of law**' (Article 38 of the ICJ Statute)
  - (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**
- investment was illegally made, and 'it is not included within the scope of consent [of two States] and, consequently, the disputes arising from it are not subject to the **jurisdiction** of the Centre [=ICSID]'

## 5. Criticism on case-law

- denial of jurisdiction *ratione materiae* = all or nothing approach
  - more **flexible** solution is needed
  - ex. to limit the amount of **damages**
- Involvement of host-State in corrupt acts is **unpunished**
  - both the investor and the host-State should be responsible for corruption
  - corrupt host-State should be **estopped** from invoking corruption defense
- investor's actual corrupt act itself is **unpunished**  
(denial of jurisdiction ≠ punishment)
  - weakens investment protection and exacerbate domestic corruption while leaving its root causes untreated.
  - victims must be **the people of host-State**

# III. New trend of balancing interests by ISDS

- Detailed examination of corruption in recent cases.

1. **Causation**: *Hamester* [2010]

2. **Clean hands principle**: *NIKO* [2013]

## 1. Causation: *Hamester* [2010]

### ***Hamester v. Ghana*, ICSID Case No. ARB/07/24 (Award, June 18, 2010)**

- Ghana alleged that the investment contract for a cocoa production plant was procured by fraud (over-statement of invoices).
- German-Ghana BIT

### **ICSID finding**

#### ▪ **Distinction** between

- (1) legality as at the **initiation** of the investment → a **jurisdictional** issue
- (2) legality during the **performance** of the investment → a **merits** issue

#### ▪ **Causation**

‘There is no proof that the alleged fraud was **decisive** in securing the JVA [investment agreement]’.

#### ▪ **issue of equities**

‘The Tribunal sees the over-statement of invoices as an issue bearing upon **the balance of equities** between the two parties, rather than the existence itself of the contract or the investment’.

→ Tribunal dismissed the Respondent’s jurisdictional objections.

- **Result (Merits phase)**

  - No-attribution of acts and no violation of BIT.

    - The fraud issue was not discussed by the Tribunal.

- **Evaluation**

  - **Causation** (decisiveness of fraud) was examined in detail.

  - Different from *Inceysa* (→ contract by misrepresenting finances and qualifications → no jurisdiction)

  - more flexible solution

## 2. Clean hands principle: *NIKO* [2013]

### ***NIKO Resources Ltd. v. Bangladesh et al.* [2013] Decision on Jurisdiction**

- Agreement on the development of marginal/abandoned gas fields and the sale of gas from such fields.
- Claimant provided benefits to Mr Hossain (the then Bangladesh State Minister for Energy and Mineral Resources).
- Respondents did not allege the nullity of agreement, but application of **clean hands principle**.

### **ICSID finding**

- there is **no link of causation** between the established acts of corruption and the conclusion of agreements.
- Tribunal applies the **clean hands principle** as a **general principle of law**
  - three criteria formulated by **ITLOS Arbitral Tribunal** in *Guyana v. Surinam*

- Criteria

- (i) the breach must concern a **continuing** violation.

- A: the violation is not continuing, but consisted in two acts that have been completed long ago.

- (ii) the remedy sought must be “protection against continuance of that violation in the **future**”, not damage for **past** violations.

- A: remedy does not concern protection against past violation.

- (iii) there must be a relationship of **reciprocity** between the obligations considered.

- A: there is no relation of reciprocity between the relief sought and the acts in the past.

- Conclusion: Objections based on acts of corruption was dismissed.

- Differentiation of two cases

- ① If **link of causation** exists

- tribunal examines the nullity of agreement

- ② If **link of causation** does not exist

- no nullity of agreement

- apply other principles (ex. clean hands principle)

# Conclusions

- Applicable law (when IIA does not contain 'legality clause')
  - International public policy = transnational public policy
  - = general principle of law or general principle of international law
  - = principle of good faith, principle of clean hands
  - criteria are clarified by **case-law** (of ISDS and other tribunals)
  
- Two stages of examination
  1. Illegal or illegitimate investment at the time of **establishment**
    - **jurisdictional** issue
    - More detailed examination
    - a **link of causation** between corrupt acts and agreement.
    - whether corruption was **decisive** or not
  
  2. Illegal or illegitimate investment during **performance** → **merits** issue
    - but impacts on **compensation** is not yet certain
  
    - 'legality clause' in IIA should target both stages

▪ Several Issues unanswered

1. Corruption by government officials

→ regulated by clean hands principle?

2. Finding of no-jurisdiction benefits host-State?

→ Mr Cremades (Dissenting Opinion in Fraport):

The government party is equally responsible. The denial of jurisdiction damages not only the claimant, but also **the citizens** of the host State which need the investment and its benefits.