

## Article

# Analysing Obstacles and Challenges in Fighting Corruption in Cases of Illegal Investments

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**Abstract:** Due to existing shortcomings in the system, the suitability and effectiveness of the international investment arbitration regime in addressing corrupt practices in international transactions and investment projects has been frequently questioned. The current legal and regulatory regime presumes that there is a level playing field, i.e., that the parties to an arbitration have equal access to information regarding corrupt actions. However, in practice, bringing claims of corruption in international investment fora meets various obstacles such as evidentiary hurdles and the lack of a specific arbitrators' mandate. Hence, the focus of this article is on addressing gaps in the international investment arbitration regime dealing with corruption cases. There is increasing concern that the international legal and regulatory regime is inadequate and contains gaps that permit multinational firms to engage in illegal acts involving corruption. Against this backdrop, the main issue that arises is how the international community should respond. This article reviews the gaps in the international investment arbitration regime and then identifies two broad strategies to address the issue of accountability. The first strategy would be to build on and strengthen the existing international investment arbitration regime, which would imply its re-engineering. A second strategy would be to establish a regime providing a new forum and an avenue for dedicated international criminal investigators to be paired with dedicated anticorruption courts that would handle criminal complaints. The Anticorruption Protocol to the United Nations Convention against Corruption (APUNCAC) represents an example of the second strategy. The APUNCAC is a model convention that calls for the implementation of a system comprising dedicated international criminal investigators and dedicated anticorruption courts, in addition to a system where plaintiffs could pursue civil class actions and seek treble damages. The APUNCAC represents a more radical strategy for addressing corruption on the international level. In addition, the APUNCAC would also permit civil class actions seeking treble damages. Overall, the APUNCAC would offer claimants an opportunity to pursue their claims in a neutral forum.

**Keywords:** anti-corruption; international investment law; international arbitration; APUNCAC



**Citation:** Olmos Giupponi, Belen, and Hong-Lin Yu. 2022. Analysing Obstacles and Challenges in Fighting Corruption in Cases of Illegal Investments. *Laws* 11: 59. <https://doi.org/10.3390/laws11040059>

Academic Editor: Stuart S. Yeh

Received: 13 March 2022

Accepted: 7 July 2022

Published: 27 July 2022

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## 1. Introduction

Due to existing shortcomings in the system, the suitability and effectiveness of the international investment arbitration regime in addressing corrupt practices in international transactions and investment projects has been frequently questioned. The current legal and regulatory regime presumes that there is a level playing field, i.e., that the parties to an arbitration have equal access to information regarding corrupt actions. However, in practice, bringing claims of corruption in international investment fora meets various obstacles such as evidentiary hurdles and the lack of a specific arbitrators' mandate.

Hence, the focus of this article is on addressing gaps in the international investment arbitration regime dealing with corruption cases. There is increasing concern that the international legal and regulatory regime is inadequate and contains gaps that permit

multinational firms to engage in illegal acts involving corruption. Against this backdrop, the main issue that arises is how the international community should respond.

This article reviews the gaps in the international investment arbitration regime and then identifies two broad strategies to address the issue of accountability. The first strategy would be to build on and strengthen the existing international investment arbitration regime, which would imply its re-engineering. A second strategy would be to establish a regime providing a new forum and an avenue for dedicated international criminal investigators to be paired with dedicated anticorruption courts that would handle criminal complaints.

The Anticorruption Protocol to the United Nations Convention against Corruption (APUNCAC) represents an example of the second strategy. The APUNCAC is a model convention that calls for the implementation of a system comprising dedicated international criminal investigators and dedicated anticorruption courts, in addition to a system where plaintiffs could pursue civil class actions and seek treble damages. The APUNCAC represents a more radical strategy for addressing corruption on the international level. In addition, the APUNCAC would also permit civil class actions seeking treble damages. Overall, the APUNCAC would offer claimants an opportunity to pursue their claims in a neutral forum.

Section 1 of this article outlines the research question and the main topics covered by the analysis. Section 2 of this article sets the scene by describing the existing civil framework for addressing corrupt multinational practices and describes the obstacles in fighting corruption via the existing legal regime. A major issue is the legality of an investment. An economic transaction that may qualify factually and financially as an investment may still fall outside of the tribunal's jurisdiction due to its illegality.<sup>1</sup> Section 3, below, examines (1) the sources of the requirement that an investment must be 'in accordance with' the laws of the home State, (2) issues related to the stages where the alleged corruption and bribery occurred, and (3) how domestic legislation should be brought into consideration. Then, Section 3 explores the duties of due diligence and good faith in determining the legality of international investments and the degree to which they are 'in accordance with' the laws of the host State. Section 4 discusses the challenges in fighting corruption arising from the issues raised in Section 3. Section 5 evaluates the APUNCAC as a strategy for fighting corruption in view of the challenges posed by the existing legal regime regarding the task of successfully alleging and proving corruption in cases of illegal investments. Section 5 focuses on the APUNCAC as an alternative strategy involving the implementation of national systems of dedicated courts and procedures to vet the selection of prosecutors and judges to serve on those courts, with the objective of ensuring the independent prosecution and adjudication of charges of corruption.<sup>2</sup> Section 6 presents the conclusions, drawing on the analysis and suggesting alternatives for the future.

## 2. Setting the Scene: Corruption and International Investment Law

The existing international regime to fight illegal investments involves three layers. The first layer concerns the exclusion of illegal investments (as non-conforming with the host state's legislation) from the protection afforded under investment treaties. Illegal investments mean those that infringe the laws of the host state (which comprise not only investment legislation but, more broadly, any laws applicable to the development of the investment project such as anti-corruption, anti-bribery, and human rights laws). Following the criteria established in *Salini* (2001),<sup>3</sup> the need for the investment to be in

<sup>1</sup> *Fraport v. Republic of the Philippines* (n 3) para 306. Although the *Fraport* decision was later annulled by the ad hoc committee, the committee still rejected Fraport's argument concerning the tribunal's misinterpretation of the definition of investment Article 1(1) of the Germany–Philippines BIT. The second tribunal deciding after the annulment reached the same finding.

<sup>2</sup> APUNCAC, Articles 7 and 8.

<sup>3</sup> *Salini Costruttori S.p.A. and Italstrade S.p.A. v. Kingdom of Morocco* [I], ICSID Case No. ARB/00/4 <<https://www.italaw.com/cases/documents/959>> accessed on 18 December 2021.

conformity with the host state's law refers to its validity. This was further confirmed in *Inceysa v. El Salvador* (2003)<sup>4</sup> and *Fraport v Philippines* (2010)<sup>5</sup>, where the doctrine of unclean hands played a significant role in the interpretation of the legality of the investment. However, what remains controversial is the appropriate measures that should be adopted in consequence: the continuity of the investment and the avoidance of the investment through the review/revocation of licences for illegal investments. To ensure investors' accountability is addressed through an effective system, there is a trend in treaty-making shifting from the inclusion of an 'in accordance with domestic law' clause (such as the clause contained in the 1994 Bosnia and Herzegovina–Malaysia BIT) to the incorporation of specific 'anti-bribery and anti-corruption' provisions (such as the clause embodied in the 2016 Morocco–Nigeria BIT).

The second layer concerns the extraterritorial application of the anti-bribery legislation from the home country, e.g., the facilitation of payments abroad regulated under the OECD Convention on Bribery<sup>6</sup> and the UK Bribery Act 2010.<sup>7</sup> Questions regarding the effects and effectiveness of the legislation governing criminal offences committed abroad arise. In a parallel development, the EU is exporting its anti-corruption standards to non-EU countries via the inclusion of ad hoc clauses in trade agreements to prevent, detect, and combat corrupt practices and reinforce international co-operation and information sharing. Notably, free trade agreements concluded by the EU contain an anti-fraud clause providing for a temporary withdrawal of tariff preference to tackle serious customs fraud and the lack of cooperation. Nevertheless, the question posed is whether an appropriate level of homogeneity/consistency can be achieved through the extraterritorial application and export of EU standards.

Finally, to prevent money laundering and protect strategic sectors, such as critical infrastructure, water, health, defence, and food security, the screening of foreign investments is deployed through the proposed EU Screening Mechanism.<sup>8</sup> However, this requires a high level of international co-operation and significant peer pressure to ensure the success of this mechanism.

Three issues arise: (i) the obstacles and challenges caused by the lack of a definition of the legality requirements and their relationship with 'in accordance with the law of the host state', (ii) the obstacles and challenges faced by international investment tribunals in dealing with the extraterritorial effects of the home state's anti-corruption laws, and (iii) the challenges to be contemplated by the international investment community to achieve effectiveness and the efficiency of anti-corruption to promote integrity, accountability, and the proper management of public affairs and public property.<sup>9</sup>

A central question is the definition of 'corruption', as understood in the context of international investment law. The legality of the foreign investor's conduct has increasingly been subject to scrutiny (Llamzon and Sinclair 2015, p. 451). Frequently, the arbitral tribunal is confronted with the host state's assertion that the investor committed corruption or bribery during the lifetime of the investment contract. This can include an array of conduct such as the violation of the host state's laws, deceitful conduct, the misuse of the system of international investment protection, and the violation of good faith or transnational public policy.<sup>10</sup>

<sup>4</sup> *Inceysa Vallisoletana, S.L. v. Republic of El Salvador* (ICSID Case No. ARB/03/26), Award, 2 August 2006, para 238. [https://www.italaw.com/sites/default/files/case-documents/ita0424\\_0.pdf](https://www.italaw.com/sites/default/files/case-documents/ita0424_0.pdf) accessed on 18 December 2021.

<sup>5</sup> *Fraport A.G. Frankfurt Airport Services Worldwide v. Republic of the Philippines*, ICSID Case No. ARB/03/25, Award (16 August 2007), para 306 <<https://www.italaw.com/cases/456>> accessed on 29 May 2019.

<sup>6</sup> OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions, signed on 17 December 1997 and in force since 15 February 1999. <[http://www.oecd.org/daf/anti-bribery/ConvCombatBribery\\_ENG.pdf](http://www.oecd.org/daf/anti-bribery/ConvCombatBribery_ENG.pdf)> accessed on 18 December 2021.

<sup>7</sup> The Act received the Royal Assent on 8 April 2010.

<sup>8</sup> European Commission, *Foreign Direct Investment EU Screening Framework*, available at [https://trade.ec.europa.eu/doclib/docs/2019/february/tradoc\\_157683.pdf](https://trade.ec.europa.eu/doclib/docs/2019/february/tradoc_157683.pdf) accessed on 18 December 2021.

<sup>9</sup> Article 1, United Nations Convention against Corruption (2003).

<[https://www.unodc.org/documents/brussels/UN\\_Convention\\_Against\\_Corruption.pdf](https://www.unodc.org/documents/brussels/UN_Convention_Against_Corruption.pdf)> accessed on 18 December 2021.

<sup>10</sup> *Ibid.*, p. 452.

The difficulty in harnessing an effective system to counteract corruption in international investment arbitration has been stressed by Haugeneder and Liebscher (Haugeneder and Liebscher 2009, pp. 544, 556, 557). In turn, the international community has expressed intolerance of such a practice. The former Secretary General of the United Nations, Kofi Annan, stated that the ‘international community is determined to prevent and control corruption’.<sup>11</sup> Appropriately addressing these issues will increase the ‘accountability and transparency in promoting development and making the world a better place for all’.<sup>12</sup>

Internationally, treaties combating corruption include the UN Convention against Corruption (UNCAC)<sup>13</sup> and the OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions.<sup>14</sup> Further regional efforts have been made to introduce specific treaties such as the following: the Convention on the Fight Against Corruption Involving Officials of the European Communities or Officials of Member States of the European Union,<sup>15</sup> the Council of Europe Civil Law Convention on Corruption,<sup>16</sup> the Council of Europe Criminal Law Convention on Corruption,<sup>17</sup> the African Union Convention on Preventing and Combating Corruption,<sup>18</sup> and the Inter-American Convention Against Corruption.<sup>19</sup>

From an interdisciplinary perspective, corruption perception indexes such as those elaborated by Transparency International and the World Bank reveal a correlation between corruption and development, showing considerable differences across countries. Examples of corrupt practices, as reported by foreign investors, include ‘the solicitation of bribes to obtain foreign exchange, import, export, investment or production licences or to avoid paying tax, although for international investors that sort of extortion amounts to an extra tax’.<sup>20</sup> These extra costs dissuade potential foreign investment. In the extensive research conducted by Ades and di Tella, they found that corruption discourages investment, particularly so in an environment where the amount of red tape inherently detrimental to investment is low (Ades and Di Tella 1997, p. 501). In contrast, some economists have argued that corruption would enable business in heavily bureaucratic systems and semi-closed economies, while other authors have found a positive relationship between corruption and FDI, with corruption acting as a stimulus for FDI (Egger and Winner 2005, p. 949), but the results are inconclusive.<sup>21</sup>

Returning to the legal issues, corruption in the international investment arbitration is construed around the notion of illegal investment. A main obstacle faced in fighting corruption is the lack of a uniform definition of ‘corruption’ in the international community. For instance, the *travaux préparatoires* for the United Nations Convention against Corruption<sup>22</sup> expressed that the definition of corruption belongs to the ‘domaine réservé’. Subparagraph (b) of the commentary on Article 7 of the Convention states:

<sup>11</sup> Kofi Annan, Foreword, United Nations Convention against Corruption (2003), iii, <[https://www.unodc.org/documents/brussels/UN\\_Convention\\_Against\\_Corruption.pdf](https://www.unodc.org/documents/brussels/UN_Convention_Against_Corruption.pdf)> accessed on 18 December 2021.

<sup>12</sup> Ibid.

<sup>13</sup> United Nations Convention against Corruption (n 7).

<sup>14</sup> OECD Convention on Combating Bribery of Foreign Public Officials (n 4).

<sup>15</sup> Convention on the Fight Against Corruption Involving Officials of the European Communities or Officials of Member States of the European Union (1997) Official Journal C 195 of 25 June 1997, <<https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=OJ:C:1997:195:TOC>> accessed on 18 December 2021.

<sup>16</sup> Civil Law Convention on Corruption (1999) ETS No.174 (Date of entry 01/11/2003), <<https://www.coe.int/en/web/conventions/full-list/-/conventions/treaty/174>> accessed on 18 December 2021.

<sup>17</sup> Criminal Law Convention on Corruption (1999) ETS No.173 (Date of entry 01/07/2002), <<https://www.coe.int/en/web/conventions/full-list/-/conventions/treaty/173>> accessed on 18 December 2021.

<sup>18</sup> African Union Convention on Preventing and Combating Corruption (2003) (Date of Entry 05 August 2006; Date of last signature 26 December 2018), <<https://au.int/en/treaties/african-union-convention-preventing-and-combating-corruption>> accessed on 18 December 2021.

<sup>19</sup> Inter-American Convention Against Corruption, 29 March 1996, <[http://www.oas.org/en/sla/dil/inter\\_american\\_treaties\\_B-58\\_against\\_Corruption.asp](http://www.oas.org/en/sla/dil/inter_american_treaties_B-58_against_Corruption.asp)> accessed on 29 May 2019.

<sup>20</sup> See note 14.

<sup>21</sup> 1–10, with 10 meaning the least red tape; see [www.integrity-index.org](http://www.integrity-index.org) accessed on 18 December 2021.

<sup>22</sup> Adopted by the General Assembly in its resolution 58/4 of 31 October 2003, <<https://www.unodc.org/unodc/en/treaties/CAC/travaux-preparatoires.html>> accessed on 18 December 2021.

While the definition of corruption must be subject to national law, it should be understood to encompass the commission or omission of an act in the performance of or in connection with one's duties, in response to gifts, promises or incentives demanded or accepted, or the wrongful receipt of these once the act has been committed or omitted.<sup>23</sup>

Llamzon and Sinclair attempted to define corruption in comparison with other types of wrongdoing falling within the scope of illegality. They pointed out the bilateral nature of corruption, frequently involving intermediaries. This placed corruption in a different form from other types of unilateral acts of wrongdoing.<sup>24</sup> They stated:

Corruption is used almost uniformly to describe bribery between an investor's employee or intermediary and a public official of the host State. Fraud is often used in a generic sense and can further be subdivided into deceit (i.e., a form of fraud that involves the intent to deceive the host State to the investor's advantage) and to misrepresentation (which need not delve into whether there existed willful intent to deceive). . . . the lack of good faith in the making of an investment and two of its manifestations—abuse of process and abuse of rights. International law and various domestic legal systems recognize 'good faith', broadly conceived, and to some extent the provenance of these terms can be traced to customary international law and general principles. They possess commonality in that they are 'framed in order to avoid misuse of the law'.<sup>25</sup>

The concept of 'domaine réservé' is also noted in the definition of public officials, as set out in Article 8 of the Convention, which refers to an additional reference to the definition to be provided 'in the domestic law and as applied in the criminal law of the State Party in which the person performs that function'.<sup>26</sup> A similar reference to the domestic law is also noted in Article 2(a) of the Convention.<sup>27</sup> On the issue of the burden of proof, the Convention requires that the state parties fulfill the burden of establishing the offences claimed in the host state's domestic law. However, with many domestic laws addressing corruption or bribery to foreign public officials designed with extra-territorial effects, controversial questions arise.

### 3. The Definition of the Legality Requirement

In the international investment law context, the legality requirement touches on the central nerve system of foreign investment arbitration. Citing *Tokios Tokelès v. Ukraine*,<sup>28</sup> Polkinghorne and Volkmer (2017, p. 150) argued that 'investments be[ing] made in compliance with the laws and regulations of the host State is a common requirement in modern BITs'.<sup>29</sup> They also pointed out the issue of the legality of investment, which covers corruption and bribery with respect to the admission of investments, investments carried out by

<sup>23</sup> Ibid., p. xiv.

<sup>24</sup> Llamzon and Sinclair (n 8) 461.

<sup>25</sup> Ibid., p. 453.

<sup>26</sup> Travaux préparatoires (n 23).

<sup>27</sup> It reads: 'Public official' shall mean: (i) any person holding a legislative, executive, administrative or judicial office of a State Party, whether appointed or elected, whether permanent or temporary, whether paid or unpaid, irrespective of that person's seniority; (ii) any other person who performs a public function, including for a public agency or public enterprise, or provides a public service, as defined in the domestic law of the State Party and as applied in the pertinent area of law of that State Party; (iii) any other person defined as a 'public official' in the domestic law of a State Party. However, for the purpose of some specific measures contained in chapter II of this Convention, 'public official' may mean any person who performs a public function or provides a public service as defined in the domestic law of the State Party and as applied in the pertinent area of law of that State Party.

<sup>28</sup> *Tokios Tokelès v. Ukraine*, ICSID Case No. ARB/02/18, Decision on Jurisdiction (29 April 2004), <<https://www.italaw.com/cases/1099>> accessed on 18 December 2021.

<sup>29</sup> *Tokios Tokelès v. Ukraine*, ICSID Case No. ARB/02/18, Decision on Jurisdiction (29 April 2004), para 84, <<https://www.italaw.com/cases/1099>> accessed on 18 December 2021.



circumventing the regulations of the host state<sup>30</sup>, or admission due to misrepresentation (Polkinghorne and Volkmer 2017, p. 151).

Unfortunately, the words ‘any legal dispute arising directly out of an investment’ provided in Article 25 of the ICSID Convention does not offer clear guidance on this issue. The main difficulty related to the legality requirement is that the definition of ‘legality of investment’ may or may not be contained in bilateral investment treaties (BITs) and international investment agreements (IIAs). Few treaties embody a direct or explicit reference to the legality of an investment. From a broader perspective, comprehensive trade agreements (also incorporating an investment chapter) have paved the way to further regulate corruption in the context of international investment law. A new trend favouring the inclusion of anti-corruption provisions is emerging due to the proactive stance taken by the United Nations and the European Union in the regulation of corruption.<sup>31</sup>

Different models are thus observed. First, there are treaties linking the legality of the investment to compliance with the host state’s legislation, articulated around the requirement of ‘in accordance with host state’s law’ (Knahr 2007; Hepburn 2014). Second, there are treaties that, despite not including a specific clause, implicitly contain references to the legality of the investments. Third, treaties embodying specific anti-corruption clauses such as new provisions in international investment treaties can be observed.

The key question here is whether the legality requirement is linked to the admissibility of corruption claims under international investment law. This obstacle may still be present under a separate and autonomous system articulated around the idea of dedicated courts dealing with corruption cases. However, the main difference would be the possibility of relying on specific procedures to establish whether or not corruption has materialised in a specific case. In the next subsection, the question of the ‘illegality’ of the investment is examined in light of the scholarship and case law in international investment law.

### 3.1. ‘In Accordance with the Host State Law’ Requirement

In international investment arbitration, the legality requirement can be dealt with by the tribunal as a jurisdictional or merit issue. Regardless, the tribunals were frequently asked to examine the concept and practice of ‘in accordance with the laws of the host state’.

The importance of the laws and regulations of the host state is stressed by various commentators. Francioni highlighted that the extensive penetration of foreign investment guarantees into the areas of national regulation reserved to domestic jurisdiction can only be counter-balanced or met if the investor pursues ‘legitimate’ public policy objectives (Francioni 2010, p. 81). Dolzer and Schreuer spoke about how foreign investment may reach far into the ‘domaine réservé’ in domestic law against the concerns regarding the preservation of national sovereignty and the democratic legitimacy of the process of foreign investment (Dolzer and Schreuer 2008, p. 84). Kriebaum argues for the gravity of the violation of domestic regulations, setting a threshold by which an infringement is to be considered serious enough to invalidate the investment (Kriebaum 2010, pp. 307, 319).

Procedurally, the definition of ‘investment’ determines the tribunal’s jurisdiction to deal with the intended kind of investment agreed to under the BITs. Nevertheless, the fast pace of economic activity prompts contracting parties to BITs to develop BIT models that cover investments of all possible types. In some BITs, the inclusive definition of investment offers a link to the ‘domaine réservé’ of the host state’s laws. As discussed previously, not all BITs address the issue of legality requirements. Where appropriate, BITs usually prescribe and restrict treaty protections only to the specific types of legal investments that the host states would like to attract to provide economic and social benefits. Under these

<sup>30</sup> *Fraport v. Republic of the Philippines*, (n 3).

<sup>31</sup> United Nations Convention against Corruption (n 6); European Commission, *Anti-corruption provisions in EU free trade and investment agreements: Delivering on clean trade*, April 2018, available at [http://www.europarl.europa.eu/RegData/etudes/STUD/2018/603867/EXPO\\_STU\(2018\)603867\\_EN.pdf](http://www.europarl.europa.eu/RegData/etudes/STUD/2018/603867/EXPO_STU(2018)603867_EN.pdf) access on 18 December 2021.

circumstances, BITs may prescribe legality requirement that can appear in the definition of investment, the admission clause, or both.

Where BITs fail to provide clarity, the vagueness of the ‘*domaine réservé*’ of the host state’s laws raised in arbitration proceedings would have to rely on the interpretations given by the tribunal to set the boundaries on the sources and definition of the legality requirement. In the decisions made by the tribunals in the *Inceysa* and *Metal-Tech* cases, the tribunals limited their jurisdiction to investments that were in compliance with local laws and where the home states had consented to arbitration.<sup>32</sup> This corresponds with Cosar’s view that state consent to arbitration is conditional and depends on whether the investment disputes meet the definition of a legal investment (Cosar 2015, p. 540).

This approach was also taken up in *Achmea B.V. v Slovak Republic*.<sup>33</sup> The respondent objected to the tribunal’s jurisdiction *ratione materiae* because the investment was made in violation of the law of the Slovak Republic.<sup>34</sup> The tribunal ruled that Article 2 of the Treaty ‘did not purport to qualify the definition of an investment ... Article 1(a) of the Treaty, unlike provisions in certain other bilateral investment treaties, does not contain a requirement that investments be made ‘in accordance with the laws and regulations’ of the host State’.<sup>35</sup> Furthermore, it stated that ‘the Tribunal is not free to rewrite the Treaty: it must interpret and apply the text adopted by the Parties; and it cannot decide their dispute as *amiable compositeur* or *ex aequo et bono*’.<sup>36</sup>

Nevertheless, following the principle of good faith stipulated by Articles 31–33 of the Vienna Convention on the Law of Treaties, the tribunal decided that ‘it is in the view of the Tribunal entirely reasonable to interpret the terms of Article 1(a) without reading in a requirement that there must be no infraction of the host State’s law in the course of the making of the investment, if the investment is to be within the scope of the Treaty protection’.<sup>37</sup> Since the investor’s licence was not revoked, there was no illegality in this case. The tribunal suggested that a distinction between the compliance with laws that limit the scope of permissible investments and the compliance with each and every law of the host state must be made. It asserted: ‘it is in the view of the Tribunal entirely reasonable to interpret the terms of Article 1(a) without reading in a requirement that there must be no infraction of the host State’s law in the course of the making of the investment, if the investment is to be within the scope of the Treaty protection’.<sup>38</sup> The question is whether such a distinction is necessary since the accepted view is that foreign investments are only protected by the international law or the general principles of law when they are made in accordance with the legislation of the host state.

### 3.2. Is Legality an Implicit Requirement?

More often, BITs prefer to use vague language to ensure the flexibility in interpreting the provisions of the BITs during their lifetime. To impose the legality requirements, an indirect approach may have to be used. Such an indirect approach can be applied through the admission clause, the scope of protection clause, or an implied duty to comply with the law of the host state. In the case of an admission clause, the contracting parties may agree to have protection extended to an investment made before its entry into force by the

<sup>32</sup> *Metal-Tech Ltd. v. The Republic of Uzbekistan* (ICSID Case No. ARB/10/3), Award, 4. October 2013, 373; <https://www.italaw.com/sites/default/files/case-documents/italaw3012.pdf> (accessed on 6 July 2022); *Inceysa Vallisoletana* (n 2) para 238.

<sup>33</sup> *Achmea B.V. v Slovak Republic*, UNCITRAL, PCA Case No. 2008–13 (formerly *Eureko B.V. v. The Slovak Republic*). The case concerned the interpretations of the Agreement on Encouragement and Reciprocal Protection of Investments between the Kingdom of the Netherlands and the Czech and Slovak Republic, which was signed on 29 April 1991 and entered into force on 1 October 1992, <<https://www.italaw.com/sites/default/files/case-documents/italaw3206.pdf>> accessed on 18 December 2021.

<sup>34</sup> *Ibid.*, para 162.

<sup>35</sup> *Ibid.*, para 166.

<sup>36</sup> *Ibid.*, para 168.

<sup>37</sup> *Ibid.*, para 169.

<sup>38</sup> *Ibid.*, para 172.

investors in accordance with the laws of the host state.<sup>39</sup> The second source of the legality requirement may be found in the scope of the protection clause, where the host state declares its duty to protect the investment made by investors in accordance with its legislation.<sup>40</sup>

For instance, the legality requirement was discussed in *Fraport*<sup>41</sup>, where the illegality was claimed to take place during the procurement and subsequent negotiations of the concession agreement. This was against the Philippines Anti-Dummy Law. The tribunal placed an emphasis on legality by referring to ‘investment . . . accepted in accordance with the respective laws and regulations of either Contracting State’, as required by Article 1(1) of the BIT between Germany and the Philippines.<sup>42</sup> In this case, the Philippine Constitution and the BOT Law required that the project proponent of a public utility project involving foreign investment must be Filipino or a corporation registered with the SEC that is at least 60% Filipino-owned and at most 40% foreign-investor-owned. This requirement was also stressed in Article 2 of the Protocol of Agreement to the BIT.<sup>43</sup>

The operation of the investment was alleged to be in breach of the Anti-Dummy Law<sup>44</sup>, which imposed nationality restrictions on the employment of foreign nationals, executives, and members of management. In terms of the timing of the legality requirement, the tribunal’s analysis of the language of both Articles 1 and 2 of the BIT stressed that the compliance of the law of the host state at the ‘initiation of the investment’ provided grounds for the tribunal’s jurisdiction.<sup>45</sup> The tribunal stated:

If, at the time of the initiation of the investment, there has been compliance with the law of the host State, allegations by the host State of violations of its law in the course of the investment, as a justification for State action with respect to the investment, might be a defense to claimed *substantive* violations of the BIT, but could not deprive a tribunal acting under the authority of the BIT of its Jurisdiction.<sup>46</sup>

The efforts to extend the legality requirement may require the tribunal to look at the real intentions of the contracting parties from the *travaux préparatoires* and the actions taken by both states at the negotiation stage, as the *Inceysa* tribunal did.<sup>47</sup> In the absence of clear treaty language prescribing legality in the BITs, the tribunal used ‘general recognised rules and principles of international law’ to add its interpretation of the legality requirement. The tribunal pointed out that the investor’s deliberate misrepresentation of its financial status and experience contravened the good faith required in international law. Investments made in an illegal manner are viewed as in breach of international public policy, the good faith principle, unjustified enrichment, and non-profiting from illegal actions.

### 3.3. The Broader Perspective: Anti-Corruption Clauses in Trade and Investment Agreements

The proliferation of comprehensive Regional Trade Agreements (RTAs) including an investment chapter has brought in new anti-corruption provisions, which range from transparency clauses to tailor-made provisions aligned with the ‘Singapore agenda’ (WTO n.d.). The EU has advocated for an inclusion of topics with a bearing on corruption: investment, competition, and transparency in government procurement. Yet, reaching a consensus on a multilateral level has become increasingly difficult due to the reluctance of some states to implement ‘deep provisions’ into areas which may limit their sovereignty (Lejárraga 2014; Lamy 2015).

<sup>39</sup> For example, Article 2 of the Spain—El Salvador BIT.

<sup>40</sup> For example, Article 3 of the Spain—El Salvador BIT.

<sup>41</sup> *Fraport v. The Republic of The Philippines* (n 3).

<sup>42</sup> *Ibid.*, para 300.

<sup>43</sup> *Ibid.*, para 336.

<sup>44</sup> *Ibid.*, para 309.

<sup>45</sup> *Ibid.*, para 345.

<sup>46</sup> *Ibid.*

<sup>47</sup> *Inceysa Vallisoletana* (n 2) paras 192–96.



Contemporary RTAs address regulatory areas such as transparency and anti-corruption provisions alongside environmental and labour standards (Jenkins 2017). An unprecedented trend starting in 2000 reveals that more than 40% of RTAs concluded since 2000 incorporate anti-corruption and anti-bribery commitments.<sup>48</sup>

A clear example of an anti-corruption provision is found in DR-CAFTA, which regulates the matter in parallel with transparency (Article 18, Section B). Article 18.7 takes on the additional obligation of the state parties to eliminate bribery and corruption in international trade and investment. In turn, Article 18.8(1) refers to a series of corruption-related situations which shall be regulated by each party through necessary legislative or other measures ‘to establish that it is a criminal offense under its law, in matters affecting international trade or investment’. Nevertheless, Article 18.8(2) grants states parties a considerable margin to determine which procedures and penalties they should adopt to enforce criminal measures. Article 18.8(3) guarantees that enterprises are sanctioned for corruption-related conduct, even if they are not criminal.

Article 18.8 deals with Anti-Corruption Measures, setting forth three underlying activities that affect international trade or investment, which require necessary legislative (or other) measures including the definition of criminal offenses. These are: for public officials to materially gain from an act in exchange for an act or omission in the performance of a public function; for a person to bribe, either directly or indirectly, a public official for personal gain or advantage; for a person of one country to bribe a foreign official of another in order for the official to act or refrain from acting in relation to the performance of an official duty in order to obtain or retain a business or another improper advantage in the conduct of international business. Conspiring to undertake any of the aforementioned activities is also considered a criminal offence.

There is also a reference to appropriate penalties which should be put into effect to address these criminal measures. Furthermore, Article 18.8(4) incentivises the protection of whistle-blowers, protecting those who, in good faith, report acts of bribery or corruption. Finally, the state parties set forth to work jointly to encourage and support appropriate initiatives in relevant international fora (Art.18.9). Although having such provisions included in comprehensive RTAs would contribute to a more coherent approach, the main caveat is that no cases concerning these provisions have been settled so far.

#### 4. Main Challenges in Fighting Corruption in International Investment Law

Different challenges have been observed in fighting corruption from an international investment law viewpoint. Firstly, there are challenges that relate to procedural hurdles to effectively dealing with corruption in arbitral proceedings. Secondly, there are those substantive questions that emerge from the application of due diligence and the principle of good faith. Finally, arbitral tribunals are confronted with the challenges that arise from the extra-territorial effects of domestic legislation and the standard of proof required in corruption cases.

##### 4.1. Procedural Obstacles Encountered in Arbitral Proceedings

As discussed, the legality requirement can be dealt with by a tribunal as a jurisdictional or merit issue in international investment arbitration. The decision depends on the tribunal’s interpretation of the legality requirement or its consideration of procedural efficiency if the practice of corruption was raised by the host state at the proceedings for the resolution of a substantive issue. The challenge is a particularly acute one if the illegality alleged by the host state overlaps with the breach of substantive protections alleged by the investors. This is because, as an accepted universal rule in arbitration, the merit of an award is not subject to challenge by the losing party; hence, concerns with dealing with the legality requirement at the merit stage were expressed. Paulsson highlighted that the use of admissibility as grounds for the legality requirement may run the risk of

<sup>48</sup> Lejárraga (n 58) 15.

‘an unjustified extension of the scope for challenging awards’ on the basis of jurisdiction (Paulsson 2005, p. 601). Nevertheless, others suggested the application of the threshold of the ‘scale of illegality’ to deal with such an issue. In accordance with the scale of illegality, it was invoked that an obvious fault in illegality was seen as a jurisdictional issue<sup>49</sup>, whereas a minor breach would not exclude the investors’ access to the substantive provisions and protections and should be dealt with at the merit stage.

The issue of the scale of illegality is also linked to estoppel on the host state’s part. The challenge arising from the estoppel issue lies in the tribunal’s gatekeeping role in terms of jurisdiction and the likelihood of moving the disputes into the merit stage of the dispute resolution. Estoppel was discussed in *Mamidoil v Albania*<sup>50</sup>, where the issue of illegality was also raised by Albania. Albania alleged Mamidoil’s failure in obtaining the required permits for the investment.<sup>51</sup> The claimant replied by citing arguments from *Tokios Tokelés v. Ukraine*<sup>52</sup> and *Desert Line v. Yemen*<sup>53</sup>, where the tribunals held that minor errors and ‘a failure to observe the bureaucratic formalities of the domestic law’<sup>54</sup> did not breach the illegality requirement.<sup>55</sup>

The claimant alleged that formality defects, such as the failure to obtain a permit that would have been granted, are not sufficient to constitute illegality.<sup>56</sup> The tribunal confirmed its jurisdiction and decided to deal with the disputes at the merit stage because the host state required that the investor cure the violations. Although the tribunal agreed that a host state cannot be expected to consent to an arbitration for investments not made in accordance with the law of the host state, it can accept the jurisdiction of an arbitral tribunal when, in that state’s own appreciation, the illegality of the investment was susceptible to being cured, as that state’s legalization offers show. In such circumstances, the legal significance of the absence of permits is to be determined as a question of merit—namely, whether the respondent’s international responsibility is engaged in the face of the claimant’s violation of Albanian law rather than the tribunal’s jurisdiction.<sup>57</sup>

This led the tribunal in *Malicorp* to bring good faith<sup>58</sup> into its interpretation of the legality requirement by examining the parties’ performance prior to the illegality taking place.<sup>59</sup> Following the international practice, the tribunal decided to examine the issue at the second stage ‘from the standpoint of the merits, in relation to the validity of the investment’.<sup>60</sup> Considering the principle of autonomy of the arbitration agreement, the varied grounds of the invalidity of an investment, and the factual analysis of the case,<sup>61</sup> the arbitral tribunal stated: ‘[i]n order for an ICSID arbitral tribunal to be able to render an award against a State for breach of obligations concerning the protection of an investment,

<sup>49</sup> *Phoenix Action, Ltd. v. Czech Republic*, ICSID Case No. ARB/06/5, (Award, 15 April 2009), para 104, <<https://www.italaw.com/cases/850>> accessed on 18 December 2021.

<sup>50</sup> *Mamidoil Jetoil Greek Petroleum Products Societe S.A. v. Republic of Albania*, ICSID Case No. ARB/11/24 <<https://www.italaw.com/cases/3003>> accessed on 18 December 2021.

<sup>51</sup> *Ibid.*, para 208, 239.

<sup>52</sup> *Tokios Tokelés v. Ukraine* (n 30).

<sup>53</sup> *Desert Line Projects LLC v. The Republic of Yemen*, ICSID Case No. ARB/05/17. Award, para 104 <[https://www.italaw.com/sites/default/files/case-documents/ita0248\\_0.pdf](https://www.italaw.com/sites/default/files/case-documents/ita0248_0.pdf)> accessed on 18 December 2021.

<sup>54</sup> *Tokios Tokelés v. Ukraine*, ICSID Case No. ARB/02/18, para 297 <<https://www.italaw.com/sites/default/files/case-documents/ita0866.pdf>> accessed on 18 December 2021.

<sup>55</sup> *Desert Line Projects LLC v. The Republic of Yemen*, ICSID Case No. ARB/05/17. Award, para 117 <[https://www.italaw.com/sites/default/files/case-documents/ita0248\\_0.pdf](https://www.italaw.com/sites/default/files/case-documents/ita0248_0.pdf)> accessed on 18 December 2021.

<sup>56</sup> *Mamidoil v. Republic of Albania*, (n 65) para 304.

<sup>57</sup> *Ibid.*, para 492.

<sup>58</sup> *Malicorp Ltd. v. Egypt*, ICSID Case No. ARB/08/18, (Award 7 February 2011) para 118, <<https://www.italaw.com/cases/660>> accessed on 18 December 2021.

<sup>59</sup> *Franck Charles Arif v. Republic of Moldova*, ICSID Case No. ARB/11/23, Award (8 April 2013) para 376, where article 1(1) of the France–Moldova BIT expressly provided ‘in accordance with the legislation . . . , on the territory or maritime area of which the investment is made’.

<sup>60</sup> *Malicorp Ltd. v. Egypt* (n 73), para 117.

<sup>61</sup> *Ibid.*, para 119.

such investment must be valid. That is why the issue of the possible application of the principle of good faith is then considered as part of the issues on the merits'.<sup>62</sup>

Nevertheless, considering Paulsson's assertion regarding the undesirability of closing the door to the grounds for a challenge, confusion can arise from such an approach being taken by tribunals. In practice, the inclusion of 'in accordance with the law' in BITs has been argued as constituting a jurisdictional issue which requires the tribunal to grant a preliminary award before proceeding to the merit stage.<sup>63</sup> To illustrate this, the arbitral tribunal in *Phoenix* approached the legality requirement at the jurisdictional stage with its interpretation of the principle of good faith from the standpoint of Article 25 of the ICSID Convention. This approach was held as 'judicial common sense to deal with issues of jurisdiction at the outset of investment arbitrations'.<sup>64</sup> Cosar similarly suggested that, in practice, tribunals have generally accepted legality requirements as a jurisdictional impediment<sup>65</sup> which impacts the scope of the claims an investor may have.

The tribunals in *Mamidoil v Albania*,<sup>66</sup> *Tokios Tokelés v. Ukraine*<sup>67</sup>, and *Desert Line v. Yemen*<sup>68</sup> confirmed their respective jurisdictions and proceeded to the merit stage of the dispute resolution. Combining the principle of good faith in transnational public policy and the unclean hands doctrine, the legality requirement can be decided at the post-jurisdictional stage when both the investors and host state have access to the claims related to the substantive rights addressed by the tribunal. When the tribunal deals with the requirement of legality at the merit stage of the dispute resolution, the tribunal's decision virtually closes the door to any procedural challenges against the award under Article V of the New York Convention and Article 52 of the ICSID Convention.

#### 4.2. Exploring the Links between Due Diligence and the Fight against Corruption

Due diligence in international investment law is construed around the requirement under the definition of investment that it should be made 'in accordance with the law of the host state (De Brabandere 2015)'. In the case where BITs contain an express legality requirement, due diligence is subsumed by the legality requirement. Tailor-made provisions on due diligence are relatively new. However, due diligence associated with the host state's conduct and the effective implementation of FET, a growing trend in international arbitration, indicates that it is a two-way street imposing responsibilities upon foreign investors.

Early arbitration cases consider due diligence in relation to the legality requirement. The due diligence of the foreign investor is assessed against the nature of the domestic law processes and provisions infringed. Explicit legality was addressed in *Inceysa*, where the arbitral tribunal examined the requirement in light of the wording of the BIT between El Salvador and Spain.<sup>69</sup> Additionally, in terms of the threshold for the legality requirement, arbitral tribunals have determined that the breach of fundamental legal principles of the host state determines its seriousness, as discussed in *LESI & Alstadi v Algeria*. In a long string of cases, arbitral tribunals have looked into the seriousness of the breach and the lack of due diligence on the part of the investor, such as *Rumeli v Kazakhstan*, *Phoenix*, *Tokios & Tokeles*, *Hochtief v Argentina*<sup>70</sup>, and *Metalpar v Argentina*<sup>71</sup>, where the foreign investor's fault

<sup>62</sup> Ibid., para 117.

<sup>63</sup> *Inceysa Vallisoletana* (n 2) paras 142–45.

<sup>64</sup> See the respondent's submission in *Malicorp Ltd. v. Egypt* (n 73), para 98.

<sup>65</sup> Cosar (n 43) 540.

<sup>66</sup> *Mamidoil v. Republic of Albania* (n 63).

<sup>67</sup> *Tokios Tokelés v. Ukraine* (n 34).

<sup>68</sup> *Desert Line v. Yemen*, (n 70) para 104.

<sup>69</sup> *Inceysa Vallisoletana* (n 2) paras 46 and 47.

<sup>70</sup> *Hochtief AG v. The Argentine Republic*, ICSID Case No ARB/07/31 <<https://www.italaw.com/cases/538>> accessed on 18 December 2021.

<sup>71</sup> *Metalpar S.A. and Buen Aire S.A. v. The Argentine Republic*, ICSID Case No. ARB/03/5 <<https://www.italaw.com/cases/680>> accessed on 18 December 2021.

in fulfilling some legal requirements was viewed as a minor fault which did not exclude the investors from the protection available under the BIT.<sup>72</sup>

Arbitral tribunals have also confirmed their own competence in dealing with substantive issues in cases of due diligence exercised by host states by revoking a licence<sup>73</sup> in a case where the law was amended after the entry point of the investment.<sup>74</sup> Interestingly, in *Fraport*<sup>75</sup>, the plaintiff's claim of illegal investment alluded to an illegal secretive shareholder's agreement, invalidating the presumption favouring investors. In the tribunal's view, the arrangement for the profitability of the investment was not central to the definition of the investment<sup>76</sup>; references were made to good faith<sup>77</sup> but not due diligence. The question of estoppel was discussed but did not occur.<sup>78</sup>

A host state's lapse in addressing illegality may not amount to consent to illegality. This was addressed in a number of cases. In *Tecmed v Mexico* (a case relating to waste management), the arbitral tribunal decided that, though the host state could not be unaware of the illegality, the inherent procedures to close the gaming facilities, which took six months, did not amount to an estoppel. Consequently, it did not prevent the state from relying on 'in accordance with the law'.<sup>79</sup> By the application of the good faith principle, consent would not have been given had the host state been aware of the facts discussed. Cases involving misrepresentation include *Plama*, *Inceysa*, and *Desert Line v Yemen*, where the host state argued for no formal acceptance due to misrepresentation or fraud. Equally, the principle of estoppel was discussed in bribery cases such as *World Duty Free*.<sup>80</sup>

Clearly, the question of legitimate expectation poses a significant issue. For instance, in *Phoenix*<sup>81</sup>, the arbitral tribunal concluded that the legal modification of state law after investment should not lead to a limitation of the arbitral tribunal's jurisdiction.<sup>82</sup> In *Kardassopoulos*, the arbitral tribunal decided that Georgia had exceeded its own authority, arguing that foreign investors should be allowed to have a legitimate expectation if a state enterprise received a licence and operated for many years. In *SSP v Egypt*, *OKO Pankki v Estonia*, and *Swem Balt v Latvia*<sup>83</sup>, the host states were viewed to have given express or implied consent to illegal investment.

In *SAUR International SA v. Argentina*, the claimant alleged that when a BIT imposes a condition of legality on the investment, the violation of the legality requirement deprives the arbitral tribunal of jurisdiction. The claimant argued that the illegality must have been committed by the investor at the time of making the investment, citing *Fraport*, *Rumeli*, and *Saba Fakes* in support of this thesis.<sup>84</sup> In an evolution of the arbitral jurisprudence, in *Álvarez*,

<sup>72</sup> Ibid. Decision on Jurisdiction (27 April 2006) However, this view is different from the one held by the tribunal in *Alasdair Ross Anderson et al. v. Republic of Costa Rica*, ICSID Case No. ARB(AF)/07/3, Award (19 May 2010), 50 I.L.M. 23 (2011) para 57. The tribunal in *Anderson v Costa Rica* held that all regulatory requirements must be complied with in order to establish the true ownership of the investment, as the tribunal was required to establish its jurisdiction *ratione materiae*; see *Quiborax S.A., Non Metallic Minerals S.A., & Allan Fook Kaplún v. Plurinational State of Bolivia*, ICSID Case No. ARB/06/2, Award on Jurisdiction (27 September 2012), where the tribunal did not distinguish between minor and major non-compliance with the law of the host state, para 240. (The words 'any kind' of investment were used in Article 1(2) of the Bolivia–Chile BIT.)

<sup>73</sup> *Alex Genin, Eastern Credit Limited, Inc. and A.S. Baltoil v. The Republic of Estonia*, ICSID Case No. ARB/99/2 <<https://www.italaw.com/cases/484>> accessed on 18 December 2021.

<sup>74</sup> *International Thunderbird Gaming Corporation v. The United Mexican States*, UNCITRAL ARB/99/2 <<https://www.italaw.com/cases/571>> accessed on 18 December 2021.

<sup>75</sup> *Fraport* (n 3)

<sup>76</sup> Ibid., para 396.

<sup>77</sup> Ibid., paras 396–97.

<sup>78</sup> Ibid., paras 346–47, 387.

<sup>79</sup> *Técnicas Medioambientales Tecmed, S.A. v. The United Mexican States*, ICSID Case No. ARB (AF)/00/2 <<https://www.italaw.com/cases/1087>> accessed on 18 December 2021.

<sup>80</sup> *World Duty Free Company Limited v. The Republic of Kenya*, ICSID Case No. ARB/00/7. paras 184–85 <<https://www.italaw.com/documents/WDFvKenyaAward.pdf>> accessed on 18 December 2021.

<sup>81</sup> *Phoenix* (n 64).

<sup>82</sup> *Phoenix* (n 64) paras 102–4.

<sup>83</sup> *Swem Balt v Latvia*, UNCITRAL Case, 23 October 2000, paras 34, 35.

<sup>84</sup> *SAUR International SA v. Republic of Argentina*, ICSID Case No. ARB/04/4, para 241 <<https://www.italaw.com/cases/1456>> accessed on 18 December 2021.

the arguments revolved around the question of due diligence. The host state argued that the investment was illegal and that the claimants did not act with the ‘due diligence of a prudent and reasonable investor’.<sup>85</sup> The arbitral tribunal determined that the purchase of indigenous lands was plagued with irregularities.<sup>86</sup> Specifically, the investment took place in indigenous territory (Comarca Ngöbe-Buglé), which is protected by Article 127 of Panama’s constitution, is guaranteed as collective property, and is not subject to private property.<sup>87</sup> The arbitral tribunal established that legality was an implicit requirement and that the foreign investor had breached the requirement, thus precluding the possibility of being protected under the BIT.

#### 4.3. Is the Principle of Good Faith Enforceable?

In arbitration cases, the principle of good faith is also used to assess the claims of illegality. In *Inceysa*, the arbitral tribunal emphasised the exchange of notes between contracting states, as well as the various draft treaties prior to the final version. The arbitral tribunal relied on the principle of good faith to determine the jurisdiction of the centre.<sup>88</sup> Referring to *Amco*, the tribunal emphasised the need to interpret the relevant normative provisions in good faith, i.e., in an objective manner to determine whether or not a certain dispute falls within the jurisdiction of the centre.<sup>89</sup> Furthermore, the tribunal mentioned that the principle should be interpreted in a twofold manner:

- (i) [I]n the good faith with which the Arbitral Tribunal must act when making its jurisdictional analysis and (ii) said analysis must start from the premise that the consent of the parties was manifested in writing and given in good faith and, therefore, at the time they manifested their consent, the parties did so with the sincere intent for it to produce all of its effects under the circumstances agreed upon by them.<sup>90</sup>

The unclean hands doctrine has emerged in the consideration of the Fair and Equitable Standard.<sup>91</sup> In cases like *LESI and Alstadi v Algeria*,<sup>92</sup> arbitral tribunals have referred to the interpretation of the doctrine of unclean hands (Dumberry 2016) through indirect provisions on the promotion, admission, and protection of investments. The tribunal confirmed an implicit duty of legality and precluded investors from relying on treaty protections.

The *Inceysa* tribunal positioned the good faith principle as the ‘supreme principle, which governs legal relations in all... aspects and content’ of foreign investment.<sup>93</sup> The tribunal also stated that good faith requires the ‘absence of deceit and artifice’.<sup>94</sup> With regard to the coverage of the principle of good faith, it starts from the negotiation to the execution of instruments. In this sense, good faith is defined as ‘loyalty, truth and intent to maintain the equilibrium between the reciprocal performance of the parties’.<sup>95</sup> Following this analogy, good faith is viewed as a generally accepted rule or standard that requires parties to act within the scope of the legality requirement when entering into, and throughout, the duration of the legal relationship.<sup>96</sup> The falsification of documents related to an investment represents a breach of the good faith principle because the parties ‘would

<sup>85</sup> *Álvarez y Marín Corporación S.A. and others v. Republic of Panama*, ICSID Case No. ARB/15/14, para 95.

<sup>86</sup> *Ibid.*, para 229 and 318.

<sup>87</sup> *Ibid.*, para 319.

<sup>88</sup> *Inceysa Vallisoletana* (n 2) paras 179.

<sup>89</sup> *Inceysa Vallisoletana* (n 2) paras 180.

<sup>90</sup> *Inceysa Vallisoletana*, paras 181.

<sup>91</sup> Peter Muchlinski, ‘Caveat Investor’? The Relevance of the Conduct of the Investor under the Fair and Equitable Treatment Standard, 55 INT’L & COMP. L. Q. 527 (2006).

<sup>92</sup> *L.E.S.I. S.p.A. and ASTALDI S.p.A. v. République Algérienne Démocratique et Populaire*, ICSID Case No. ARB/05/3 <<https://www.italaw.com/cases/618>> accessed on 18 December 2021.

<sup>93</sup> *Inceysa Vallisoletana* (n 2) para 230.

<sup>94</sup> *Ibid.*, para 231.

<sup>95</sup> *Ibid.*

<sup>96</sup> *Ibid.*, para 233.



have never entered into the legal relation in question providing the accurate information were provided'.<sup>97</sup>

The tribunal used the words 'implicit confidence' to describe the essential requirement of good faith in a legal relationship involving foreign investment. The tribunal concluded that, in the absence of good faith, 'with which the parties must act when entering into the legal relation, and which is imposed as a generally accepted rule or standard'.<sup>98</sup> the tribunal would see the foreign investor's commitments as being breached. The tribunal drew a substantial link between misrepresentation and the breach of the principle of good faith. This involved Inceysa's attempt to present false financial information as part of the tender made by it to participate in the bid, false representations of its experience and capacity during the bidding process, and false representations of the experience of its team members. The tribunal ruled that 'by falsifying the facts, Inceysa violated the principle of good faith from the time it made its investment and, therefore, it did not make it in accordance with Salvadoran law' and that El Salvador would not have allowed Inceysa to make its investment had it known of the violations on Inceysa's part.<sup>99</sup> Consequently, the tribunal concluded that it did not have the competence and jurisdiction to hear the dispute because 'El Salvador gave its consent to the jurisdiction of the Centre, presupposing good faith behavior on the part of future investors'.<sup>100</sup>

Furthermore, considering the lack of good faith during the negotiations and the execution of the agreement on Inceysa's part, the tribunal upheld the maxim of '*Ex dolo malo non oritur actio*' (an action does not arise from fraud)<sup>101</sup> and ruled that Inceysa could not benefit from investment by means of its fraudulent acts, let alone the investment protection provided in the BIT. This was to ensure that justice was delivered by the tribunal, whose obligation is to see '[n]o legal system based on rational grounds allows the party that committed a chain of clearly illegal acts to benefit from them'.<sup>102</sup> Furthermore, the tribunal stated: 'the inclusion of the clause 'in accordance with law' in the agreements for reciprocal protection of investments follows international public policies designed to sanction illegal acts and their resulting effects'.<sup>103</sup>

Apart from the expressed 'in accordance with the law of the host state' provision(s),<sup>104</sup> the good faith principle in international law was again discussed in *Gustav F.W. Hamester v Ghana*,<sup>105</sup> where the tribunal ruled that a lack of good faith in the entry and operation of an investment on the investor's part would act as the second layer of exclusion or a tacit condition<sup>106</sup> leading to the investor being excluded from the protection provided by the BIT.<sup>107</sup> The tribunal ruled in *Gustav F.W. Hamester & Co KG v. Republic of Ghana*<sup>108</sup> that investors do not enjoy absolute protection. The tribunal stressed that the imposition of the compliance of laws and regulations is within the power of the host state, as 'States may specifically and expressly condition access of investors to a chosen dispute settlement mechanism, or the availability of substantive protection'.<sup>109</sup> In the absence of such an express provision, the performance of good faith in carrying out investment projects was also highlighted. Following *Phoenix*, the tribunal refused the investor's access to protections

<sup>97</sup> Ibid., para 232.

<sup>98</sup> Ibid., para 233.

<sup>99</sup> Ibid., para 237.

<sup>100</sup> Ibid., para 238.

<sup>101</sup> Ibid., para 240.

<sup>102</sup> Ibid., para 244.

<sup>103</sup> Ibid., para 247.

<sup>104</sup> *Gustav F.W. Hamester GmbH & Co. K.G. v. Republic of Ghana*, ICSID Case No. ARB/07/24, Award (18 June 2010) para 125 accessed on 18 December 2021.

<sup>105</sup> Ibid.

<sup>106</sup> *SAUR* (n 98) para 308; Polkinghorne and Volkmer (n 31) 157.

<sup>107</sup> *Gustav F.W. Hamester GmbH & Co. K.G. v. Republic of Ghana*, ICSID Case No. ARB/07/24, Award (18 June 2010), paras. 123–24 <<https://www.italaw.com/sites/default/files/case-documents/ita0396.pdf>> accessed on 18 December 2021.

<sup>108</sup> *Gustav Hamester* (n 121).

<sup>109</sup> Ibid.

under the ICSID dispute settlement mechanism, as the investment was not made in good faith.<sup>110</sup> While the Phoenix tribunal stressed the implicit link between the purpose of the investment protection through the ICSID Arbitration and the legality requirement by the laws of the host, it stated:

If a State, for example, restricts foreign investment in a sector of its economy and a foreign investor disregards such restriction, the investment concerned cannot be protected under the ICSID/BIT system. These are illegal investments according to the national law of the host State and cannot be protected through an ICSID arbitral process. And it is the Tribunal's view that 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.<sup>111</sup>

The *Gustav F.W. Hamester* tribunal further clarified the types of actions that could be viewed as a breach of the principle of good faith by the tribunals, involving illegal investments. The tribunal made a substantial link between the breach of the principle of good faith and a violation of the law of the host state by stating:

An 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; or if its creation itself constitutes a misuse of the system of international investment protection under the ICSID Convention. It will also not be protected if it is made in violation of the host State's law.<sup>112</sup>

The tribunal in *Desert Line Projects LLC v. The Republic of Yemen*<sup>113</sup> pointed out that compliance with the 'fundamental principles of the host State's law' is required. It further pointed out that 'according to its laws and regulations' is intended to ensure 'the legality of the investment by excluding investments made in breach of fundamental principles of the host State's law, e.g., by fraudulent misrepresentations or the dissimulation of true ownership'.<sup>114</sup>

The lack of specific wording such as 'conformity of a particular law' in BITs or the ECT does not mean that there is a scope for illegal investment. The investor's implicit duty to comply with the law of the host state was highlighted as an essential element in the integrity of foreign investment.<sup>115</sup> There was a legality requirement with a bona fide investment initiation<sup>116</sup> as a pre-condition for claiming the protections. By stating that a non-bona fide investment breaches both the BIT and Article 25 of the Washington Convention, the tribunal actually extended the application of good faith to Article 25 of the ICSID Convention.

Despite the lack of clear language in Article 1 of the Netherlands and Turkey BIT and in Article 25(1) of the ICSID Convention, in *Saba Fakes v Turkey*<sup>117</sup> and *Metal-Tech v. Uzbekistan*<sup>118</sup>, the tribunals extended the legality requirement to the issues of consent and whole protection. In *Phoenix*, the tribunal further underscored the imposition of good faith obligations within the system of foreign investment.<sup>119</sup> However, this extension should apply to the BIT but not to Article 25(1) of the ICSID Convention, as the tribunal was of the opinion that the imposition of the good faith requirement would significantly change the

<sup>110</sup> Ibid., para 123; *Phoenix* (n 64) para 106.

<sup>111</sup> *Phoenix* (n 64) para 106.

<sup>112</sup> *Gustav Hamester* (n 121) para 123.

<sup>113</sup> *Desert Line* (n 70).

<sup>114</sup> Ibid., para 104.

<sup>115</sup> *Phoenix* (n 62) para 101.

<sup>116</sup> Ibid., para 142.

<sup>117</sup> *Saba Fakes v. Republic of Turkey*, ICSID Case No. ARB/07/20, Award (14 July 2010) para 114. The investor's claim was dismissed due to a lack of legal title to the share certificates related to the investment in dispute.

<sup>118</sup> *Metal-Tech v. Republic of Uzbekistan* (n 40) para 127, See Article 1(1) of the Israel-Uzbekistan BIT.

<sup>119</sup> *Phoenix* (n 62) para 113.

intention of the provision.<sup>120</sup> It is worth noting that this view is different from the position taken in *Phoenix*<sup>121</sup> and *Aguas del Tunari S.A. v Bolivia*<sup>122</sup>, where the tribunals refused to incorporate the implicit requirement that the investment must meet the test of legality.

#### 4.4. Extra-Territorial Effects of Domestic Anti-Corruption Legislation and the Mandate of Arbitrators

Following the UN Convention Against Corruption<sup>123</sup> and the OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions,<sup>124</sup> domestic jurisdictions have become increasingly intolerant of the corrupt behaviour of their own nationals within and outside of their own jurisdictions. Such instruments prescribe an extraterritorial effect over its own nationals even though the illegal acts were carried out outside of its own jurisdiction. Taking the UK as an example, according to s. 6(1) of the UK Bribery Act, '[a] person ('P') who bribes a foreign public official ('F') is guilty of an offence if P's intention is to influence F in F's capacity as a foreign public official'.<sup>125</sup> Putting this provision in the context of foreign investment activities, a UK investor who bribes a foreign public official of the host state would be caught by the intended extraterritorial effect and be accused of being guilty of a criminal offence if the investor's intention is to influence the official in his capacity as a foreign public official.<sup>126</sup> In the case of the United Kingdom, such an effect would also lead to the application of the Proceed of Crimes Act 2002.<sup>127</sup> The potential crossing of paths between arbitration and criminal law became a reality due to the extraterritorial effect on investors and would cause a compatibility issue in domestic jurisdictions. An examination of the different standards of proof applied in criminal and arbitration systems as well as the arbitrator's mandate in foreign investment dispute resolutions is required.

In criminal evidential/procedural laws, it is widely accepted that the standard of proof should be 'beyond reasonable doubt'. Davidson suggested that 'beyond reasonable doubt' is a phrase that is impossible or at least dangerous to attempt to define.<sup>128</sup> By way of example, similarly to England, the 2.1 Burden and Standard of Proof in the English Judicial Studies Board requires the prosecution to carry the burden of proving the defendant's guilt. The burden can only be discharged if the evidence allows the jury to 'mak[e] you sure of it. Nothing less than that will do'.<sup>129</sup> Evidence of a circumstantial nature will not meet the threshold.

<sup>120</sup> *Saba Fakes v. Turkey* (n 132) para 113.

<sup>121</sup> Other cases include: *Salini* (n 1) where the host stat's claim of corruption was rejected; *Plama Consortium Limited v. Republic of Bulgaria*, ICSID Case No. ARB/03/24 <https://www.italaw.com/cases/857> accessed on 6 July 2022; *Gas Natural SDG, S.A. v. The Argentine Republic*, ICSID Case No. ARB/03/10, <https://www.italaw.com/cases/documents/477> (accessed on 6 July 2022); *Bayindir Insaat Turizm Ticaret Ve Sanayi A.S. v. Islamic Republic of Pakistan*, ICSID Case No. ARB/03/29 <https://www.italaw.com/cases/131> (accessed on 6 July 2022); *Mytilineos Holdings SA v. The State Union of Serbia & Montenegro and Republic of Serbia*, <https://www.italaw.com/cases/documents/726> accessed on 6 July 2022; L.E.S.I. (n 106); *Saipem S.p.A. v. The People's Republic of Bangladesh*, ICSID Case No. ARB/05/07 <https://www.italaw.com/cases/951>; *Desert Line* (n 68) *David Minnotte & Robert Lewis v. Republic of Poland*, ICSID Case No. ARB (AF)/10/1 <https://www.italaw.com/cases/707> (accessed on 6 July 2022); *Yaung Chi Oo Trading Pte. Ltd. v. Government of the Union of Myanmar*, ASEAN I.D. Case No. ARB/01/1 <https://www.italaw.com/cases/documents/1174> (accessed on 29 May 2019).

<sup>122</sup> *Aguas del Tunari, S.A. v. Republic of Bolivia*, ICSID Case No. ARB/02/3 <[https://www.iisd.org/pdf/2005/AdT\\_Decision-en.pdf](https://www.iisd.org/pdf/2005/AdT_Decision-en.pdf)> (accessed on 18 December 2021).

<sup>123</sup> United Nations Convention against Corruption (n 6).

<sup>124</sup> OECD (n 4).

<sup>125</sup> UK Bribery Act, s 6(1).

<sup>126</sup> A foreign public official is defined as someone who holds a legislative, administrative, or judicial position of any kind, whether appointed or elected, of a country or territory outside the United Kingdom or exercises a public function for the host state outside the United Kingdom or has acted for any public agency or public enterprise of the host state or as an official or agent of a public international organisation.

<sup>127</sup> Available at <https://www.legislation.gov.uk/ukpga/2002/29/contents> accessed on 18 December 2021.

<sup>128</sup> Fraser Davidson, *Evidence* (2007 SULI), para 4.78.

<sup>129</sup> Specimen Directions in Jury Trial, 2.1 <<https://keithhotten.files.wordpress.com/2014/05/sdjt.pdf>>; The Crown Court Compendium, June 2018 page 18–19 <https://www.judiciary.uk/wp-content/uploads/2018/06/crown-court-compendium-pt1-jury-and-trial-management-and-summing-up-june-2018-1.pdf> accessed on 18 December 2021.

Interestingly, in cases involving corruption, the UK Serious Fraud Office may elect to pursue the accused in a civil action. In a civil recovery, the application of the UK Proceeds of Crime Act 2002<sup>130</sup> may see the application of a lower threshold of evidential rule—the balance of probability. This would lead to the ‘admission of different types of evidence that would not be admissible at a criminal trial, including inferences from silence, previous behaviour, illegally obtained evidence and abuse of process, and hearsay evidence’. (Hendry and King 2015, p. 399; Alldridge 2014, p. 185) Lord Denning pointed out that ‘proof beyond reasonable doubt does not mean proof beyond the shadow of a doubt’ and that ‘a case is proven beyond reasonable doubt if the evidence is so strong against a man as to leave only a remote possibility in his favour and nothing short of that will suffice’.<sup>131</sup>

He also stated that to discharge a burden of proof in a civil case, the degree required is a reasonable probability. Furthermore, the balance of probability requires evidence to be ‘more probable than not’. However, ‘if the probabilities are equal’ or ‘evenly balance[d]’, the burden is not discharged.<sup>132</sup> It is suggested that proof on a balance of probabilities is a variable standard.<sup>133</sup> However, ‘[a] civil court, when considering a charge of fraud, will naturally require for itself a higher degree of probability than that which it would require when asking if negligence is established. It does not adopt so high a degree as a criminal court, even when it is considering a charge of a criminal nature, but still it does require a degree of probability which is commensurate with the occasion’.<sup>134</sup> Furthermore, an allegation of fraud in a civil court must be proven by ‘a preponderance of probability, but the degree of probability depends on the subject-matter. In proportion as the offence is grave, so out the proof to be clear’.<sup>135</sup>

In the context of foreign investment disputes, the standard of proof applied by an arbitral tribunal to an investment allegedly tainted by corruption has its own critical importance.<sup>136</sup> It is a common understanding that the tribunal’s decision to ascertain the corruptive practice will have a determining effect on the investor’s access to the substantive protections provided under the relevant BITs. Unfortunately, most investment treaties, customary international laws, and applicable procedural laws contain no provisions on the standard of proof.<sup>137</sup> No uniform standard is established to prove corruption. Citing Redfern (1994), Reed et al. (2011), and Scherer (2002), Cosar stated that ‘international arbitration tribunals are not bound to adhere to strict judicial rules of evidence’.<sup>138</sup> She further claimed that such a level of flexibility allowing the tribunal to ‘consider all relevant aspects stems from the wide discretionary power tribunals are granted on matters of evidence’ and that ‘such flexibility has been confirmed by awards; tribunals have generally found that claims of corruption may be proven solely by circumstantial evidence’.<sup>139</sup>

The loosely defined standard of proof of corruption in foreign investment is a common practice according to Haugeneder and Liebscher. They highlighted that the tribunal has ‘relative factual freedom’ in determining which standard of certainty is necessary to prove an allegation of corruption.<sup>140</sup> Little discussion was carried out by the tribunals in practice on the different standards of proof which should be applied to determine the matter of corruption.<sup>141</sup> Accordingly, the approach taken by the tribunal is to ‘avoid basing a decision

<sup>130</sup> Part 5 of the Proceeds of Crime Act 2002.

<sup>131</sup> *Miller v Minister of Pensions* [1947] 2 All ER 372, 373.

<sup>132</sup> Ibid.

<sup>133</sup> (Redmayne 1999, p. 168); Fraser Davidson, Evidence (2007 SULI), para 4.78.

<sup>134</sup> *Bater v Bater* [1951] P. 35, 37.

<sup>135</sup> *Blyth v Blyth* [1966] AC 643, 669.

<sup>136</sup> Haugeneder and Liebscher, (n 12) 546.

<sup>137</sup> Article 24(1) of the UNCITRAL Arbitration Rules mentioned that each party shall have the burden of proving the facts relied on to support his claim or defense. Nevertheless, no threshold is prescribed.

<sup>138</sup> Cosar (n 43) 532.

<sup>139</sup> Cosar (n 43) 534.

<sup>140</sup> Haugeneder and Liebscher (n 12) 547.

<sup>141</sup> Ibid., p. 546; Cosar (n 43) 534.

solely on the burden and standard of proof and will try to establish the relevant facts with reasonable certainty irrespective of the burden and standard of proof'.<sup>142</sup> Tribunals used the 'sufficient evidence' adduced by the parties to determine the facts without having to refer to the rules of evidence.<sup>143</sup> As a result, the standard of proof was rarely discussed in arbitral awards. They even claimed that it is a widespread practice among the tribunals to 'view that the evidentiary standards in different jurisdictions in practice lead to the same result'.<sup>144</sup> Partasides spoke of 'an adequate evidentiary' (Partasides 2010). Cosar<sup>145</sup> argued for the practice of 'the balance of probabilities standard', which focuses on 'an overall assessment of the accumulated evidence', rather than on 'evidence on its own', as highlighted in *Rompetrol*.<sup>146</sup>

In practice, both the tribunals in *Metal Tech*<sup>147</sup> and *Rompetrol*<sup>148</sup> held that 'corruption was established to an extent sufficient to prove a violation'. The standard of the balance of probabilities was applied to the generality of the factual issues and the need to adopt 'a more nuanced approach'.<sup>149</sup> Bearing such an approach in mind, the rule requires the tribunal to undertake an active role in taking a formal note of 'any reasons' given by a party for its failure to comply<sup>150</sup> and produce evidence in order to cooperate within the dispute resolution process. Accordingly, the view is that a failure on the party's part would prompt an automatic response from the tribunal, who should readily draw adverse inferences from such a failure. Furthermore, 'a tribunal may take particular factual allegations as 'proved' for the purpose of the arbitration'.<sup>151</sup>

The question that arises is whether the tribunal should apply the standard of 'beyond reasonable doubt' or that of 'proof on a balance of probabilities' in the context of the extra-territorial effect on the investor's corruptive practices committed abroad. In *BSG Resources Limited v. Guinea*<sup>152</sup>, the arbitral tribunal referred to the impossibility of adopting the standard of 'beyond reasonable doubt' in arbitration. In this case, after the introduction of the Mining Code 2011, the Technical Committee concluded its investigation by stating that BRGR Guinea had allegedly obtained the concessionary rights by corruption and other unlawful means in an ICSID arbitration.<sup>153</sup> Guinea relied on the 'in accordance with the law of the host state' principle. Hence, 'such corrupt practices nullify the mining titles and the mining agreement held by VGB'<sup>154</sup> because BSGR did not follow the law in reaching a deal with Vale.<sup>155</sup> Responding to BSGR's claim regarding the unjustified withdrawal<sup>156</sup> of BSGR's investments,<sup>157</sup> Guinea alleged a corruptive practice conducted by BSGR.

On the issue of the standard of proof, in a separate LCIA Arbitration, the tribunal had found that BSGR made fraudulent misrepresentations and false statements about the group's shareholding structure and false statements during the due diligence process about

<sup>142</sup> Ibid., pp. 539–64, 546.

<sup>143</sup> Ibid.

<sup>144</sup> Ibid.

<sup>145</sup> Cosar (n 43) 538.

<sup>146</sup> *The Rompetrol Group N.V. v. Romania* (ICSID Case No. ARB/06/3), 6 May 2013, para 223; <https://www.italaw.com/cases/920> accessed on 18 December 2021.

<sup>147</sup> *Metal-Tech Ltd. v. Uzbekistan* (n 135) para 372. In this award, the tribunal looked at the evidence of the number of payments, the qualifications of the consultants, and the relationship with the government.

<sup>148</sup> *Rompetrol* (n 168) para 186.

<sup>149</sup> Ibid., para 183.

<sup>150</sup> Ibid., para 185.

<sup>151</sup> Ibid., para 184.

<sup>152</sup> *BSG Resources Limited v. The Republic of Guinea* ICSID Case No. ARB/14/22 <<https://www.italaw.com/sites/default/files/case-documents/italaw7735.pdf>> accessed on 18 December 2021.

<sup>153</sup> Ibid., p. 5.

<sup>154</sup> Ibid., para 136.

<sup>155</sup> Ibid., para 136; VGB-Vale BSGR Sarl was formed by Vale S.A. (with 51% of shares in BSGR Guernsey) and BSGR (with 51% of shares in BSGR Guernsey).

<sup>156</sup> *BSG Resources Limited v. The Republic of Guinea* ICSID CASE No. ARB/14/22; <<https://www.italaw.com/sites/default/files/case-documents/italaw7378.pdf>> accessed on 18 December 2021, para 162.

<sup>157</sup> This includes the terminations of Zogota Mining Concession, Blocks 1 and 2 Permits and the Base Convention for the investment, paras 146–48.



Vale's use of the relevant consultants and agents. The tribunal established that limited inquiry should be conducted into the episodes of allegations of bribery, as investigating private corruption by local businessmen and 'the nature of payments is not the tribunal's task assigned by the parties'.<sup>158</sup> The tribunal also highlighted that, without full coercive powers, it would be extremely difficult for the tribunal to establish the genuine practice of corruption satisfactorily.<sup>159</sup>

The BSGR tribunal's comments on lacking full coercive power seem to correspond with the observation made by Haugeneder and Liebscher, who criticised the imposition of an unduly high standard of proof in arbitration because:

Establishing corruption is, as a matter of fact, difficult. The evidence is usually not readily available. The opposing party will usually not cooperate to establish the facts, even if the production of evidence is ordered by the arbitral tribunal. Putting an additional burden on the party alleging corruption may unduly disadvantage this party and endanger the equality of the parties. Arbitral tribunals applying such higher standards may, however, simply have expressed their view that there are no lower standards for the establishment of corruption, even if corruption is difficult to prove.<sup>160</sup>

They further argued for effect civil remedies, which are sufficient to address public policy concerns and the civil consequences of corruption.

More recently, the Petrobras case seems to suggest that corruption can be cured by the subsequent agreement which fulfilled the legality requirement. On 20 May 2019, the District Court Southern District of Texas Houston Division upheld the *Vantage v. Petrobras* award favouring Vantage against Petrobras on the basis of insufficient evidence of bribery and corruption.<sup>161</sup> Being governed by English law, the contract between the parties contained a 'compliance with law' clause<sup>162</sup> requiring Vantage to comply with all applicable laws, including all the applicable laws in each of the countries, in connection with the services performed.<sup>163</sup> The contract prescribed English law as the applicable law.<sup>164</sup>

On the issues of bribery and corruption, Petrobras (the respondent) alleged that Vantage violated Good Oil and Gas Field Practices by failing to monitor fluid volumes and hence breached the contract.<sup>165</sup> It also asserted misrepresentation, illegal information, and a failure in carrying out a background check, and these constituted breaches of the non-bribery and non-operational requirements.<sup>166</sup> Petrobras further asserted that illegal payments were made or offered to its officials with the claimant's knowledge for the purpose of inducing the contract.

<sup>158</sup> Ibid.

<sup>159</sup> Global Arbitration Review <https://www.cleargottlieb.com/-/media/files/award-in-guinean-bribery-dispute-made-public-pdf.pdf> accessed on 18 December 2021. Although the LCIA tribunal concluded that there was insufficient evidence for the alleged bribery, the allegation did spark criminal investigations in the US, Switzerland, and Israel, one of which leading to the agent receiving a two-year custodial sentence in the US for obstruction of justice.

<sup>160</sup> Haugeneder and Liebscher (n 12) 547. They also raised the possibility of the violation of due process if the alleged corruptive practice was laid to rest on the basis of diplomatic reasons.

<sup>161</sup> *Vantage Deepwater Company and Vantage Deepwater Drilling, Inc. v. Petrobras America, Inc., Petrobras Venezuela Investments & Services, bv, and Petroleo Brasileiro S.A.—Petrobras* United States District Court Southern District of Texas Houston Division, Civil Action No. 18-cv-2246; <https://globalarbitrationreview.com/article/1193157/petrobras-award-upheld-despite-bribery-claims> accessed on 18 December 2021

<sup>162</sup> Clause 10.15 reads: 'Contractor acknowledges and agrees that it will be transporting the Drilling Unit between the Countries and conducting Drilling Operations in each of the Countries. Contractor shall comply with all Applicable Law, including all Applicable Law in each of the Countries, in connection with the Services performed by Contractor'.

<sup>163</sup> *Vantage Deepwater Drilling* (n 183) page 13.

<sup>164</sup> Ibid., p. 16.

<sup>165</sup> Ibid., p. 50.

<sup>166</sup> Ibid., p. 50, award para 229.

Vantage (the claimant) claimed that Petrobras had failed to meet the burden of proof for the assertions of bribery and corruption.<sup>167</sup> The tribunal was required to determine the consequences of Petrobras's repeated ratifications of the novations. Vantage claimed that a contract with defects is not void, as claimed by Petrobras, but rather voidable at Petrobras's discretion. Petrobras's decision to ignore the defects and ratify the subsequent novations led to estoppel.<sup>168</sup> Hence, repeated ratification, waiver, and estoppel defeated Petrobras's contractual defences.<sup>169</sup>

The tribunal sided with the claimant<sup>170</sup>, stressing that no convincing evidence showed that Vantage was aware of the bribery<sup>171</sup> and that Petrobras failed to present sufficient evidence to prove bribery and corruption in this case.<sup>172</sup> The tribunal ruled that it did not need to look into these assertions because 'such alleged breaches were waived or ratified by Petrobras entering into the Second Novation and Third Novation'.<sup>173</sup> This is because the tribunal agreed with the claimant's view and ruled that a contract procured by bribery called for a wider category of contracts. Such a category demands that contracts be voidable, not void.<sup>174</sup> Petrobras's decision to ratify the subsequent novations means that 'the anti-waiver clauses can be waived by a party's silence and inaction over a lengthy period of time'.<sup>175</sup> The tribunal concluded that, without sufficient evidence and the estoppel, Petrobras did not satisfy its burden in proving its allegation about Vantage's commission of bribery and corruption.<sup>176</sup>

## 5. The APUNCAC as an Innovative Response to Dealing with Corruption Cases

The preceding analysis suggests that the existing regime to fight corruption in international investments is inadequate to effectively address the procedural and substantive challenges posed by the cases brought before the investment tribunals. As examined in the previous section, the current international investment arbitration system does not offer a consistent approach to interpreting and dealing with cases of corruption. First, the assessment of the illegal nature of an investment generates uncertainty in those cases, in which it is not crystal clear whether an investment meets the definition of a 'legal' investment. Second, civil law and criminal law systems clash when it comes to determining the applicable standard of proof. Third, complexities arise in terms of the relationship between international investment law and criminal law concerning the applicability of criminal law in international investment arbitration cases (Betz 2017).

Typically, the cumulative effect of these procedural and substantive hurdles is that the system does not efficiently deal with allegations of corruption. When an investor brings a treaty claim and is accused of corruption in the making or performance of its investment, the investor's claim would be subject to dismissal. This raises problems for both parties involved in an investment arbitration. For the foreign investor, the host state may raise corruption allegations based on presumptions or no direct evidence (*indicia*). For the host state, it might be difficult for an arbitral tribunal to find corruption to prove a case. These difficulties suggest a need for reform of the international investment arbitration system. There is a lacuna in relation to applicable standards of proof since most investment treaties remain silent on the applicable standard. Discretion regarding the standard of proof to be applied generates uncertainty and inconsistent decisions. Hence, arbitrators tend to rely on the law of the arbitral seat to assess the fulfilment of jurisdictional conditions regarding charges

<sup>167</sup> Ibid., p. 54, award para 252.

<sup>168</sup> Ibid., page 55, Claimants' Summary of Claims and Defenses, at p. 5. award para 257–58.

<sup>169</sup> Ibid., page 56, para 267; Claimants' Summary of Claims and Defenses, at p. 5.

<sup>170</sup> Ibid., page 53, award para 247.

<sup>171</sup> Ibid., page 59 para 286.

<sup>172</sup> Ibid., page 60 para 292.

<sup>173</sup> Ibid., page 60 para 358.

<sup>174</sup> Ibid., page 73 para 372.

<sup>175</sup> Ibid., page 73 para 374.

<sup>176</sup> Ibid., page 42 para 173.

of corruption. Proposals have ranged from increasing state responsibility to strengthening investor accountability, with mid-range solutions offering a combination of both (Orta and Loviscek 2019; Yeh 2020). Another possibility is to introduce specific corruption provisions into investment treaties or to add joint interpretative statements to existing treaties.

The implementation of the reforms would require a consensus around the need to establish clear standards of proof regarding allegations of corruption in international investment cases. This would increase legal certainty when handling corruption claims in international investment law. Other proposals that are promoted outside the international investment arbitration realm, such as the one for the establishment of a specific anti-corruption system under the APUNCAC, could increase the robustness of the system.

Cross-fertilization and regime interactions may foster the emergence of a fit-for-purpose system. In other words, the application of specific norms designed to prevent and fight against corruption could help to fill in the gaps by including clauses introducing references to the ILC Articles of State Responsibility and international instruments such as the OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions and the UN Convention Against Corruption.

In relation to the UN Convention Against Corruption, the preceding analysis suggests that there is a need for a different strategy in the international investment arbitration realm. In this vein, the Conference of the States Parties to the United Nations Convention Against Corruption has emphasised the importance of international investments in minimising the opportunities for corruption and the transfer of proceeds of crime in this context (Resolution 8/9 adopted in 2019).<sup>177</sup> The APUNCAC represents a structured alternative strategy to address the weaknesses in the existing regime, as it seeks to increase fairness, predictability, and legitimacy.

Pursuant to the APUNCAC, the following new UN agencies (with the status of organs) would be implemented to fight corruption: the International Commission Against Corruption (ICAC); the Anti-Money Laundering Debarment Office; the Financial Crimes Enforcement Network (FINCEN); and the Office of Personnel Management (OPM). Additionally, in each state party, there would be a Conflicts of Interest Board and a Fair Political Practices Commission. This system would contribute to establishing a more robust framework for dealing with cases of corruption in international investment law, as arbitral tribunals may rely on the findings and reports issued by these bodies.

One of the main innovations introduced by the APUNCAC is the appointment of independent inspectors who would undertake the investigation of alleged charges of corruption. The ICAC would employ duly qualified inspectors of the utmost integrity to conduct investigations following the procedures set out by the APUNCAC. The inspectors would be independent and would not seek nor act on instructions from any source.<sup>178</sup> Specific procedures are established in Article 7 of the APUNCAC. The standing to put forward a request is defined in broad terms as '[a]ny individual may submit a request for an investigation to the ICAC'.<sup>179</sup> The establishment of such investigators will add impartiality and certainty to the existing international investment arbitration system. Although they will continue to be separate systems, it is foreseeable that there will be a scope for cross-fertilization and interaction between them. The effective implementation of the APUNCAC will lead to a consistent practice in terms of fighting corruption.

Certainly, the effective articulation of the APUNCAC system has implications for the international investment system. This is better understood in terms of the roles of the various bodies endowed with the power to investigate and adjudicate cases. Clearly, states need to play their part in ratifying and implementing the treaty for it to become operative. To delve into more detail, from an investigation standpoint, when examining the admissibility of a complaint, the ICAC would verify that: (i) the accused is a national

<sup>177</sup> Eighth session of the Conference of the States Parties to the United Nations Convention against Corruption, held in Abu Dhabi, from 16 to 20 December 2019. Available at <https://www.unodc.org/unodc/en/corruption/COSP/session8-resolutions.html> accessed 21 December 2021.

<sup>178</sup> Ibid.

<sup>179</sup> Ibid.

of a state that is a party to the APUNCAC, (ii) the alleged crime(s) occurred within the territory of a state that is a party to the APUNCAC, or (iii) the alleged conduct occurred outside the territory of the state party but has or is intended to have a substantial effect within its territory.

The ICAC may also elevate the priority of investigations with regard to individuals whose cooperation may be of assistance in high priority investigations through deferred prosecution agreements, non-prosecution agreements, or other types of agreements. The ICAC would designate a United Nations Inspector who would lead the investigation and supervise every aspect of the investigation. The inspectors would be vested with the capacity to conduct inspections and investigations. After the assignment to an investigation, each inspector would submit reports to the ICAC every 30 days until the investigation is completed and the case is handed over to the appropriate prosecuting authority.<sup>180</sup> Transparency International would play a significant role in the whole process. The state that assumes responsibility for prosecution would provide Transparency International with updates regarding the disposition of each case every 30 days until a case is dismissed by the appropriate prosecuting authority or court or a final verdict is reached by the appropriate court. Upon the dismissal of a case or upon a final verdict, the state that assumes responsibility for prosecution would provide Transparency International with a final report, to be published online.<sup>181</sup>

This body of investigators will be able to conduct independent investigations and refer cases to dedicated anticorruption courts. Each state party would establish dedicated anticorruption courts to deal with corruption cases. The courts would be served by prosecutors who specialise in the adjudication and resolution of charges of corruption.<sup>182</sup> The UN Commission on Crime Prevention and Criminal Justice would ensure that dedicated courts and prosecutors have regular and adequate funding to perform their responsibilities. Additionally, they would conduct periodic reviews to assess the performance of the dedicated courts and prosecutors and redirect funding based upon those evaluations.<sup>183</sup> These courts and prosecutors would prioritise charges submitted by UN Inspectors or their surrogates.<sup>184</sup> The courts would receive and swiftly adjudicate each case.<sup>185</sup>

The APUNCAC also provides for the establishment of national judicial councils by the state parties, which are vested with the responsibilities of nominating judges and prosecutors of the utmost integrity to serve on dedicated courts, ensure adequate staffing, and develop and implement streamlined adjudication procedures.<sup>186</sup>

Overall, the new system would be specialised, establishing bodies and procedures tailored to the prompt investigation and adjudication of corruption cases. This could facilitate inquiries involving corruption in international investments. However, the new system may take time until it becomes fully operational.

The APUNCAC system poses questions about how it would align with the existing system of arbitration when questions are raised about the legality of an investment. There is a need to examine the system of international investment law to achieve greater certainty and clarity.

The APUNCAC could be considered a harbinger of a new model to fight corruption on the international level. The international investment law system and international

<sup>180</sup> Ibid., p. 12. When the case is handed over to the prosecuting authority, copies of the final report shall be submitted to: (a) the Commission; (b) the complainant; (c) the appropriate prosecuting authority; (d) the appropriate court; and (e) Transparency International.

<sup>181</sup> Ibid., p. 13.

<sup>182</sup> Article 8.1.

<sup>183</sup> Article 8.2.

<sup>184</sup> The system also includes FINCEN, the Chief Debarment Officer, the Commission on Crime Prevention and Criminal Justice, a State Party Conflicts of Interest Board, and a State Party Fair Political Practices Commission. A monitor appointed pursuant to paragraph one of Article 11, a monitor appointed pursuant to paragraph 16 of Article 58, or an attorney general or public prosecutor shall ensure the swift resolution of resulting cases and shall not tolerate delays that pervert the course of justice.

<sup>185</sup> Article 8.3.

<sup>186</sup> Article 8.4.

investment arbitration would be strengthened by the APUNCAC. However, coordination would be key to ensuring proper articulation between international investment tribunals and investigations by UN inspectors and decisions by the APUNCAC's dedicated anticorruption courts. Arbitrators would have a duty to report probable cases of corruption to the anti-corruption courts. This may require splitting the proceedings and may create further hurdles and delays in investment arbitrations.

In particular, one of the main advantages of the new system is that, for corruption claims brought before investment arbitration, tribunals will be able to rely on a stronger court with a clearer understanding of corruption cases, backed by real investigative powers. The reports issued by investigators could then be authoritatively incorporated by arbitration investment tribunals. The systems are not formally interrelated; investment tribunals will continue to operate as a separate jurisdiction. Though there is no appeal possible from the investment arbitration tribunal to the anti-corruption court, the emerging system and case law will lead to a more consistent approach to corruption in international investments.

If the APUNCAC is adopted and implemented, arbitral tribunals would be able to draw upon the information gathered by UN inspectors in the course of their investigations and decisions by the APUNCAC courts. The APUNCAC would reinforce a robust set of norms that would help to combat corruption and at the same time contribute greater certainty and legitimacy to international investment arbitrations.

## 6. Conclusions: The Way Forward

The use of international investment law mechanisms to address corruption has been based on a reactive approach articulated around the notion of 'illegal investments'. However, the way this has been defined varies from one arbitral tribunal to the next. Procedural and substantive discrepancies persist across jurisdictions. In certain jurisdictions, there is a strong emphasis on the requirement that investments must be 'in accordance with the host state law'. However, establishing that this requirement was violated, for the purpose of fighting corruption and winning an arbitration against a multinational corporation, is difficult. Procedurally, the hurdles in establishing a uniform standard of proof, together with the nature of the arbitrator's mandate and the lack of compelling evidentiary power, exacerbate the difficulties in establishing a coherent approach. Even if there is evidence of corruption, cases are caught in a procedural trap.

Anti-corruption clauses advance the cause of good governance on the international level. This raises questions about the ways that international investment law could be deployed to fight corruption. This, in turn, entails grappling with the definition of anti-corruption clauses and their effects. Although the inclusion of specific provisions represents progress, states are still reluctant to fully agree on the so-called 'deep provisions', i.e., full-fledged clauses dealing with corruption in investment treaties. The main problems observed at present are related to the constrained mandate of the arbitral tribunal in dealing with corruption and the challenges in successfully proving corruption in cases of illegal investments.

These weaknesses could be addressed by the creation of a permanent investment court, as suggested by some states and the UNCITRAL.<sup>187</sup> The system would gain certainty and consistency. This attempt to strengthen the existing regime would require an overhaul of the current system.

In contrast, the APUNCAC would establish specialised investigators and dedicated anticorruption courts. Procedures would be implemented to vet the selection of prosecutors and judges to serve on those courts and establish accountability. This would address concerns related to judicial competence, independence, and neutrality. In addition, the APUNCAC contains provisions to address conflicts of interest and corruption in domestic electoral systems, as well as provisions designed to fight systemic corruption that results in

<sup>187</sup> UNCITRAL, Working Group III: Investor-State Dispute Settlement Reform, available at [https://uncitral.un.org/en/working\\_groups/3/investor-state](https://uncitral.un.org/en/working_groups/3/investor-state) accessed on 18 December 2021.



the capture of government regulators. These measures may offer advantages in dealing with corruption in cases of illegal investments involving large, well-resourced multinational corporations that are able to hire the best legal counsel to defend their interests. The APUNCAC would entail a new, more vigorous approach to investigating and settling disputes concerning allegations of corruption. Corruption cases could be dealt with more effectively and efficiently. A combination of both strategies might be needed to fight corruption, but the combination may offer greater consistency and certainty.

**Author Contributions:** Conceptualization, B.O.G. and H.-L.Y.; methodology, B.O.G. and H.-L.Y.; software, B.O.G. and H.-L.Y.; validation, B.O.G. and H.-L.Y.; formal analysis, B.O.G. and H.-L.Y.; investigation, B.O.G. and H.-L.Y.; resources, B.O.G. and H.-L.Y.; data curation, B.O.G. and H.-L.Y.; writing—original draft preparation, B.O.G. and H.-L.Y.; writing—review and editing, B.O.G.; visualization, B.O.G. and H.-L.Y.; supervision, B.O.G. and H.-L.Y.; project administration, B.O.G. and H.-L.Y.; funding acquisition, B.O.G. and H.-L.Y. All authors have read and agreed to the published version of the manuscript.

**Funding:** This research received no external funding.

**Institutional Review Board Statement:** Not applicable.

**Informed Consent Statement:** Not applicable.

**Data Availability Statement:** Not applicable.

**Conflicts of Interest:** The authors declare no conflict of interest.

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