Chapter 3

Corruption Issues in the Jurisdictional Phase of Investment Arbitrations

An Arbitrator's Checklist

Hiroyuki Tezuka*

INTRODUCTION

Corruption issues — or, more broadly, issues of illegality — have become a hot topic in international arbitration. Likely because corruption issues are so multifaceted and go way beyond mere legal considerations, they have become the subject of increased legislative, jurisprudential and scholarly attention.

In particular, the field of investment arbitration has seen an increased focus on corruption and illegality issues, with host states discovering they can be used as a defensive weapon and investors using them to argue violations of substantive investment protections. When an allegation of corruption is brought forward by a host state, it quite often becomes a 'gateway issue' requiring an arbitral tribunal to consider how and whether to continue the arbitral proceedings at an early stage.

The problems and questions connected to such considerations shall be the focus of this article. However, this article does not set out to rehash the insightful findings and considerations that others have already made in the field.[1] Instead, the aim is to take a step back and come up with something of a 'checklist' of typical and recurring issues that arbitrators or arbitral tribunals will most likely be faced with when corruption charges are raised between parties in the early stages of arbitral proceedings. The so created framework will hopefully facilitate the resolution of complex issues connected to corruption charges in investment arbitrations.

I ANTI-CORRUPTION REGULATION — A GLOBAL TREND

Due to an increase in foreign investment, the number of cases where investors have been involved in corruption in foreign countries has significantly increased in recent times. For instance, in 2008, it was revealed that a Japanese company was involved in bribery in connection with highway construction work in Vietnam. This case attracted widespread public attention because the Japanese government provided a yen loan for the highway construction work in Vietnam as part of the Japanese Official Development Assistance (the 'ODA'). It was alleged that the Japanese company gave two officials of the Vietnamese authority overseeing the highway construction work US$60 million in December 2003 and US$22 million in August 2003 as a reward for being appointed to carry out the

* Partner, Nishimura & Asahi, Japan; Committee Vice Chairperson, Dispute Resolution and Arbitration, Inter-Pacific Bar Association

construction work. Several employees of the Japanese company, as well as the Vietnamese officials, were convicted in courts in their respective home countries. In the wake of this scandal, both countries launched a joint investigation task force and reformed the bidding process for yen-loan-financed projects in Vietnam under the Japanese ODA.[2]

As you may have noticed in the reference to the above case, Japan has a domestic law that prohibits Japanese nationals and entities from 'offering' bribes or corruptive payments to 'foreign' public officials. The regulation on bribery of foreign public officials was enacted by amending an existing law, the Unfair Competition Prevention Act, which came into effect on 1 January 2005.

In fact, this legislation was introduced in response to the OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions, which entered into force on 15 February 1999 (the 'OECD Convention'), and which 34 OECD member countries and four non-OECD member countries had ratified or acceded to as of 21 May 2014. The purpose of the OECD Convention is to eliminate corruption in international business transactions, including trade and investment, which raises serious moral and political concerns, undermines good governance and economic development, and distorts international competitive conditions. In order to achieve this purpose, the convention requires the contracting countries to establish domestic law declaring the 'offering' of bribes to 'foreign' public officials as a criminal offence thereunder.

As embodied by the OECD Convention, there is a global trend whereby domestic anti-bribery legislation prohibits nationals from 'offering' bribes to not only their own public officials but also to those of 'foreign' countries. It should be emphasized that in the global movement of anti-bribery legislation, the prevailing approach is to sanction the act of 'offering' bribes, rather than that of 'receiving' or 'requesting' them, with an aim to effectively eliminate corruption by regulating the 'offering' side.

In contrast to the matured discussion in the area of anti-bribery legislation, the discussion on how to deal with corruption at the investment arbitration stage is still developing. Nonetheless, as discussed below, the approach adopted in anti-bribery legislation may have an influence when considering possible approaches to dealing with the issue of corruption at the investment arbitration stage.

II CORRUPTION AND GATEWAY ISSUES

A. State v Investor Disputes — Investment Arbitration

Corruption frequently occurs in connection with foreign investment, especially where officials of host states have a significant influence on the administration regarding permissions or licenses necessary for investment by foreign investors. When a host state ruins or diminishes the value of an investment through unfair or arbitrary measures, one of the most effective remedies available for foreign investors is investment arbitration; more precisely, investment treaty arbitration where foreign investors are permitted to directly sue the host state in accordance with the applicable investment treaty. Nonetheless, despite the fact that host states or their officials enrich themselves through corruption, as discussed below, if a host

state may use the fact that a foreign investor is involved in the corruption as a defensive weapon and the admissibility of the foreign investor's claim is denied, a legitimate question arises: is it really fair that the host state, which is also tainted by the corruption, can be discharged from all responsibility regarding its alleged unfair or arbitrary measures? The aim of this article is to shed light on this question and to provide materials to facilitate discussions on this far-reaching question. Accordingly, in this article, the focus is on international investment arbitration, especially in the case a foreign investor sues the host state regarding its investment based on investment treaties, including the Convention on the Settlement of Investment Disputes between States and Nationals of Other States (the 'ICSID Convention').

B. The Scope of Corruption

As discussed below, if an investor is allegedly involved in corruption and the relevant investment treaty contains a certain type of admission clause (such as 'in accordance with the laws of the host state') in the definition of the investment, a standard tactic employed by host states is to argue that the case should be dismissed because the claimant's investment was not made 'in accordance with the laws of the host state' and, therefore, the dispute related to such investment should not be afforded any protection under the investment treaty, including under the investor-state dispute resolution clause.

As such, when an arbitrator is faced with this argument and decides to confirm to the necessary extent whether such corruption actually took place, the arbitrator may need to look into the definition of corruption under the host state's laws. In this regard, it should be emphasized that the definition of corruption may vary depending on the laws of host states, which may lead to the question of whether it is fair for outcomes to vary depending on the laws of the host state. One possible solution would be to rely on the concept of public policy to fill in the gaps. However, even if arbitrators may rely on the notion of public policy, it would be essential that arbitrators share the same understanding of 'corruption.'

From this perspective, it may be worthwhile referring to the definition of corruption in the public sector provided in Articles 15 (Bribery of national public officials) and 16 (Bribery of foreign public officials and officials of public international organizations) of the United Convention Against Corruption (the 'UNCAC'). Article 15 of the UNCAC provides as follows:

> Each State Party shall adopt such legislative and other measures as may be necessary to establish as criminal offences, when committed intentionally:
>
> (a) The promise, offering or giving, to a public official, directly or indirectly, of an undue advantage, for the official himself or herself or another person or entity, in order that the official act or refrain from acting in the exercise of his or her official duties:
>
> (b) The solicitation or acceptance by a public official, directly or indirectly, of an undue advantage, for the official himself or herself or another person or entity, in order that the official act or refrain from acting in the exercise of his or her official duties.

For the 'offering' side, the elements constituting 'corruption' or the 'offering of bribes' are (i) intentionally (ii) promising, offering or giving, (iii) to a

national or foreign public official, (iv) an undue advantage, (v) for the official himself or herself or another person or entity, (vi) in order that the official act or refrain from acting in the exercise of his or her official duties.

As of 12 November 2014, 147 states are parties to the UNCAC. In addition, similar conceptions of 'corruption' or the 'offering of bribes' have been adopted in other prevailing international and domestic anti-corruption legislation, such as the OECD Convention and the Foreign Corrupt Practices Act of 1977. Accordingly, the above definition can be deemed to represent international consensus on public sector corruption.

C. Gateway Issues

There are various possibilities regarding how corruption comes into play in the context of investment arbitration. If an investor or claimant alleges corruption, the claim is usually related to the substantive merits of the dispute; for instance, the investor may argue that the host state did not accord fair and equitable treatment to the investor because the investor refused to pay a bribe.

Of course, corruption may take place during the course of the proceedings themselves in connection with arbitrators and expert witnesses, among others. Also, it is possible that the defendant may argue that an arbitral award should be set aside because it upholds an investment established by corruption in the enforcement stage.

If corruption is to be a 'gateway issue,' it almost automatically means it has been raised by the respondent host state with the goal to end the proceedings. Therefore, this article focuses on the arbitrability of the dispute, the admissibility of the claim, or the jurisdiction of the arbitral tribunal in the investment arbitration. More precisely, this article addresses arbitrators who have to assume the difficult task of determining (i) whether a case should be dismissed because of the alleged corruption, (ii) which party should bear the burden of proof, (iii) the standard of proof, etc.

III A PROPOSED CHECKLIST

In order for arbitrators to properly handle this difficult task, a certain guideline or checklist would be of assistance. The following are the major items and concerns that should be discussed in the preparation of the checklist.

A. Introduction of Corruption Issues into Arbitral Proceedings

1. Corruption Charges by a Party

Corruption issues are generally introduced into arbitral proceedings when one party raises the complaint that another party has availed itself of corruption in its investment or business activities. This complaint is intended not merely to taint the other side, but is raised with an explicit procedural goal in mind. In the 'gateway' phase, typically, the party bringing the charges is the respondent host state with the goal to end the proceedings.

If one party clearly alleges corruption in the gateway phase, such complaint usually takes the form of a jurisdictional issue (see Section D.1. below); if that is the case, the arbitrator cannot disregard the allegation and needs to mainly address: (i) whether the corruption charge can be grounds for

dismissal, (ii) which party should bear the burden of proof regarding the corruption and (iii) the standard of proof (see Section C. below).

2. More Controversial: *Sua Sponte* Inquiry by an Arbitral Tribunal

Arbitrators may face a more difficult issue when neither party alleges corruption but there are signs raising the suspicion of corruption. For arbitrators to determine the desirable avenue to handle this challenging situation, the following two considerations should be taken into account:

(i) Should an enforceable award be rendered?

The concern here is the risk of an award being set aside or denied enforcement by courts on public policy grounds (*sua sponte*) if it is alleged that the arbitral award is for an investor tainted by corruption.

It should be noted, however, that the rules of enforcement depend on the arbitral regime selected by the investor. If an investor is bringing a claim under the ICSID Convention, Article 54(1) provides that each contracting state shall recognize and enforce the pecuniary obligations imposed by an award within its territories as if it were a final judgment of a court in that state. No additional review by local courts is allowed and enforcement of the award would currently be possible in 149 of the Convention's member states. Therefore, investment arbitration under the ICSID Convention generally does not entail these setting aside and enforcement issues.

On the other hand, if an investor chooses arbitration rules other than those under the ICSID Convention, the arbitral award would still be enforceable if the state in which enforcement is sought is a party to the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards of 1958 (the 'New York Convention'). Article 5(2)(b) of the New York Convention provides that an award may be set aside or denied enforcement on public policy grounds.

(ii) Should the arbitral award achieve justice or fairness?

Another concern is the risk of using arbitral awards as a means for parties of host states also tainted by corruption to reap unfair benefits. This may not necessarily be true if the criminal investigation and justice system of the host state functions well; however, it is obvious that this is not always the case.

If the answer to either of the above questions is 'yes,' a possible avenue may be to 'not ignore the signs,' and then, the next question would be what should the threshold be for arbitrators to get active. One possible approach could be for tribunals to only pursue the issue of corruption where there is some *prima facie* evidence of corruption, considering the risk that an arbitral award could also be set aside or denied enforcement if the arbitrator's investigation (and subsequently, any ruling based on the results of such investigation) is deemed *ultra vires* where neither party raises such issues. For example, under the Rules of Procedure for Arbitration Proceedings (the Arbitration Rules) of ICSID (the 'ICSID Arbitration Rules'), Article 50(1)(c)(iii) provides 'the Tribunal has manifestly exceeded its power' as one of the limited grounds for annulment of an award. However, it may not be appropriate to adhere to one threshold or rule. Rather, a more flexible and case-by-case approach may often be need. As discussed below, corruption issues usually entail the difficulty of proof; therefore, if a tribunal

routinely requires *prima facie* evidence, it is almost tantamount to the tribunal passing over the signs of corruption.

B. Procedural Reaction to Introduction of Corruption Issues

1. Bifurcation of Jurisdictional Phase

If one party alleges corruption in the form of a jurisdictional issue, the arbitrator may decide to suspend the proceedings on the merits (for instance, Article 41(3) of the ICSID Arbitration Rules). In fact, it is not unusual, at least for investment arbitration under the ICSID Convention, for tribunals to grant an award-declining jurisdiction. According to statistics provided by the ICSID,[3] among the cases registered or administered by the ICSID as of 30 June 2014, 25% resulted in an award-declining jurisdiction. The unique feature of corruption issues in the jurisdictional phase is that there are still unsolved questions of whether it would be fair to deal with a corruption issue as grounds for declining jurisdiction and, if so, what is the appropriate approach.

2. Consideration of Special Procedural Directions

If neither party alleges corruption but there are signs indicating the possibility of corruption, as discussed in Section A.2. above, it raises the question regarding a *sua sponte* inquiry. From a procedural perspective, it should be noted that, at least for investment arbitration under the ICSID Convention, a tribunal might, on its own initiative, consider whether a dispute is within the jurisdiction of the ICSID Centre and within its own competence (Article 41(2) of the ICSID Arbitration Rules).

3. Reaction to Investigation Authority

Considering the global trend of tightening anti-corruption legislation, arbitrators may also need to consider whether they are allowed or obliged to report findings in arbitration proceedings. This consideration may even be important if a tribunal decides to proceed with a *sua sponte* inquiry.

Also, this issue cannot be discussed separately from confidentiality obligations under the applicable arbitration rules. In this regard, it should be noted that not necessarily all arbitration rules provide a specific provision regarding confidentiality obligations intended for arbitrators and exceptions to those confidentiality obligations. For instance, Rule 6(2) of the ICSID Arbitration Rules provides a confidentiality obligation intended for arbitrators as part of their declaration upon acceptance of an appointment. However, as shown below, it does not contain any exception to such duty:

> **Before or at the first session of the Tribunal, each arbitrator shall sign a declaration in the following form: "I shall keep confidential all information coming to my knowledge as a result of my participation in this proceeding, as well as the contents of any award made by the Tribunal.**

In contrast, the Arbitration Rules of the United Nations Commission on International Trade Law (the 'UNCITRAL Arbitration Rules'), another set of popular arbitration rules for investment arbitration, merely address the privacy of hearings and the confidentiality of awards (Articles 28(3) and 34(5)), but not confidentiality more generally. As such, in order for a checklist to properly address this issue, the following matters, at least, need to be deliberated: (i) whether the applicable arbitration rules provide any

confidentiality obligations intended for arbitrators, (ii) whether the arbitrators should be explicitly exempted from the confidentiality obligations if the competent authority requests disclosure of any information, and (iii) whether the arbitrators are allowed to, or furthermore, obliged to report the findings to the competent authority.

C. Assessing Proof of Corruption in Investment Arbitration

Assuming corruption charges have been made, or a suspicion of corrupt activities has arisen, how should an arbitrator assess corruption issues? The issue of dealing with proof of corruption has been subject to much debate, and a plurality of views exist. Examining all the relevant issues is not the purpose of this section. Instead, I simply propose that the following basic points should be on the arbitrators' checklist.

1. Proof by Admission

In *World Duty Free v Kenya*[4] and *Metal-Tech v Uzbekistan*,[5] the relevant tribunal found corruption by a party's admission. In *World Duty Free v Kenya*, the leading case on corruption in investment arbitration, claims were based on an ICSID arbitration clause in a contract governed by English law, and there was no applicable Bilateral Investment Treaty (BIT). The respondent, the host state, argued that the contract was procured by paying a bribe of US$2 million to the President of Kenya, and thus '[a]s a matter of Kenyan, English and International *ordre public*, the resulting Contract does not have the force of law.' The tribunal's fact-finding task was relatively straightforward since the claimant, World Duty Free, had attached a witness statement to a memorial where it openly described how its CEO had secured the conclusion of a concession contract by having handed over US$2 million in cash to the Kenyan President. Although he admitted contributing this US$2 million as a 'personal donation,' it argued that the personal donation 'was sanctioned by customary practices and was regarded as a matter of protocol by the Kenyan people,' and such donations were 'not only acceptable, but fashionable.' The tribunal found that, under the circumstances in that case, it had no doubt that the concealed payments made by the claimant's representative could not be considered 'a personal donation for public purposes,' and it considered that those payments must be regarded as a bribe made in order to ensure that the relevant agreement was concluded. Accordingly, the tribunal concluded that considering public policy both under English law and Kenyan law, and on the specific facts of the present case, 'the claimant is not legally entitled to maintain any of its pleaded claims in these proceedings on the ground of *ex turpi causa non oritur actio*' (from a dishonorable cause an action does not arise).

In *Metal-Tech Ltd. v Uzbekistan*, the claimant, an Israel-incorporated company that had entered into a joint venture with the Uzbek government in respect of a molybdenum production plant, brought a case alleging a breach of the Israel-Uzbekistan BIT. The claimant's Chairman and CEO testified at the hearing that *Metal-Tech* paid US$4 million pursuant to agreements with three alleged consultants, including a government official and the brother of the Uzbek Prime Minister. Interestingly, neither party had actually made corruption claims; however, the tribunal investigated the matter on its own initiative. The tribunal decided to order the parties to produce additional information and documents, pursuant to its powers

under Article 43 of the ICSID Convention. Accordingly, these admissions resulted from the tribunal's exercise of such *ex officio* powers to order the production of documents. In the end, the tribunal found that the payments made under consultancy agreements effectively amounted to corruption in violation of the Uzbek Criminal Code and the legality requirement of the BIT. The tribunal ultimately dismissed all the claims and counterclaims for lack of jurisdiction under the Israel-Uzbekistan BIT and the ICSID Conventions.

2. Burden of Proof

Before discussing the issue of burden of proof, clarification is specifically required regarding the difference between burden of proof and standard of proof. Burden of proof stipulates what a party has to prove in order for its case to prevail; and standard of proof specifies how much evidence is needed to establish either an individual issue or a party's case as a whole.[6] Essentially, there are two points in relation to the generally accepted standard regarding the burden and standard of proof for ordinary allegations not involving corruption, fraud or illegality.[7] First, regarding burden of proof, each party must generally prove the facts relied upon to support its claim or defense.[8] Often, this is indicated as a maxim: he who asserts must prove (*onus probandi incumbit actori* or *actori incumbit probatio*). Second, regarding standard of proof, the standard for ordinary allegations is the 'preponderance of evidence' or the 'balance of probabilities,' which requires demonstrating that an allegation is more than likely true.[9]

The general rule concerning the burden of proof is expressly stated in article 27(1) of the UNCITRAL Arbitration Rules (as revised in 2010).[10] Interestingly enough, none of the other established arbitration rules contain provisions on the burden and standard of proof.[11] Neither the ICSID Convention[12] nor the ICSID Arbitration Rules are any exception to this trend. However, in ICSID cases the tribunals have also routinely required both parties to prove the facts that they allege.[13] Thus, the general principle of the burden of proof (i.e., that the burden of proof rests on the party who asserts a proposition) is widely supported and applied in arbitration practice, including in ICSID Arbitration.[14]

The next questions are how and in what situations should the tribunal reverse the burden of proof. Rules establishing presumptions of or shifting of the burden of proof under certain circumstances, or drawing inferences from a lack of proof are generally deemed to be part of the *lex causae*.[15] In most of the cases, the *lex causae*, the BIT for example, provides no rules for shifting the burden of proof or establishing presumptions. Therefore, the tribunal in *Metal-Tech* recognized that it has relative freedom in determining the standard necessary to sustain a determination of corruption.[16] Especially regarding proof of corruption, many commentators have contended that tribunals in investment treaty arbitration cases should also apply an approach of shifting burden of proof to allegations of corruption since corruption is difficult to prove. Further, if corruption is reasonably suspected, but nonetheless nearly impossible to 'prove,' then an appropriate method of making a finding may be to shift the burden of proof to the allegedly corrupt party to establish that the legal and good-faith requirements were actually met.[17] ICSID tribunals indeed have affirmed that the burden of proof *may* shift in various contexts, but, according to a recent article, no ICSID tribunal has yet taken this approach of shifting the burden of proof regarding alleged

corruption.[18] Accordingly, a tribunal should be cautious about shifting the burden of proof concerning allegations related to corruption as a 'gateway issue.' Usually, the host state brings as its defense an allegation that an investor's investment was corrupt as a 'gateway issue,' so that it can deny 'investment' protection due to tainted contracts. In such a case, it may not be difficult to prove that no facts exist indicating that the host state has acted corruptly. Thus, there seems to be no need to consider the balance of the difficulty of proving the corruption, and it would therefore be reasonable not to shift the burden of proof in this context.[19]

Further, generally speaking, shifting the principle of the burden of proof demands caution. In *Rompetrol*, under Rule 34 of the ICSID Arbitration Rules, the tribunal recognized that '[t]he overall effect of these provisions is that an ICSID tribunal is endowed with the independent power to determine, within the context provided by the circumstances of the dispute before it, whether particular evidence or kinds of evidence should be admitted or excluded, what weight (if any) should be given to particular items of evidence so admitted, whether it would like to see further evidence of any particular kind on any issue arising in the case, and so on and so forth.' The tribunal further showed its position that the provision '[no] doubt intends, among other things, that a given tribunal is specifically authorized to draw whatever inferences it deems appropriate from the failure of either party to produce evidence which that party might otherwise have been expected to produce.'

In this respect, the tribunal in *Metal-Tech* observed, in accordance with Rule 34(3) of the ICSID Arbitration Rules and Article 9(5) of the IBA Rules on Taking Evidence in International Arbitration (IBA Rules) (29 May 2010), that '[p]arties to an arbitration have a good faith obligation to cooperate in procedural matters,' including the production of evidence, and that a tribunal 'may draw appropriate inferences from a party's non-production of evidence ordered to be provided.' The tribunal in *Rompetrol* further confirmed that a party's failure to comply with directions relating to the production of evidence "may condition the circumstances under which a Tribunal may take particular factual allegations as 'proved' for the purpose of the arbitration."[20]

As explained above, the arbitral tribunal has the discretion to decide the probative value of evidence. Thus, it is often possible for the tribunal to reach the appropriate conclusion without shifting the burden of proof.

3. Standard of Proof

In *EDF v Romania,*[21] the tribunal rejected the claimant's (investor's) allegation that it had lost its investment when it had refused to pay a bribe of US$2.5 million, and the tribunal applied a high standard of proof to these allegations relating to corruption. The claimant alleged that it was the victim of a senior Romanian officials' demands for bribes, relying only on the testimony of its employees who had allegedly received bribe requests, in its attempt to prove the respondent's corruption. Consequently, the respondent's witness denials countered this allegation. The tribunal specifically expressed sympathy for the claimant's position that corruption is 'notoriously difficult to prove since, typically, there is little or no physical evidence.' However, the tribunal found that the 'seriousness of the accusation of corruption in the present case, considering that it involve[d] officials at the highest level of the Romanian

Government at the time, demands clear and convincing evidence.'[22] In the end, the tribunal concluded that '[t]he evidence before the Tribunal in the instant case concerning the alleged solicitation of a bribe is far from being clear and convincing.'

In *EDF v Romania* the tribunal further remarked that '[t]here is general consensus among international tribunals and commentators regarding the need for a high standard of proof of corruption.' In fact, international arbitrators tend to require clear proof of bribery before invalidating an alleged tainted agreement, despite any suspicions they may have. Several other ICSID tribunals similarly have concluded that clear and convincing evidence or another heightened standard of proof, even including the criminal standard of proof, beyond reasonable doubt, should apply to prove allegations of corruption, fraud or illegality.[23] For example, the tribunals use the standards of 'clear and convincing evidence' in *Rumeli*, 'irrefutable proof' in *African Holding*,[24] 'sufficient to exclude any reasonable doubt' in *Bayindir*[25] and 'any allegations of impropriety are particularly heavy' in *Saba Fakes*.[26]

Although these cases deal with commercial arbitration, the statistics regarding the arbitrator's approach in dealing with corruption issues indicate a dozen cases in which a 'high' standard of proof was applied (i.e., more than 50% of the cases), this serves as a useful reference in the context of investment arbitration.[27]

According to the survey, the tribunal enumerated the following standards:

- 'direct or even circumstantial evidence'[28]
- 'with certainty'[29]
- 'were intended to bribe'[30]
- 'clear and convincing evidence'[31]
- 'allusions not supported by evidence and based on suppositions'[32]
- 'proof of traffic of influence'[33]
- 'direct or circumstantial evidence'[34]
- 'conclusive evidence' or 'a high degree of probability of bribery'[35]
- 'a mere suspicion by a member of the arbitral tribunal is entirely insufficient'[36]

These standards used in commercial arbitration relating to corruption reflect the prevailing arbitral practice of subjecting complainants in corruption cases to a high standard of proof. In a survey of arbitral case law on corruption, it was also concluded that in just one out of 25 cases, a *low* standard of proof was applied;[37] whereas in fourteen cases, a *high* standard of proof was applied.[38]

Turning to the requisite standard of proof that a party must satisfy to establish corruption, however, there is some criticism against adopting such a high standard of proof, and some opine that it should remain a balance of probabilities standard.[39] Arbitral tribunal, both in commercial and investment, deals with the consequences of corruption in matters of civil liability, not criminal. It should therefore be recognized that the higher standard of proof, beyond-reasonable-doubt, which exists in criminal law, does not apply. In arbitration, the tribunal does not impose criminal sanctions, therefore it is unnecessary and undesirable for it to proceed with

the same degree of caution as a criminal court would. More importantly, as stated above, given the difficulty in proving corruption, it would be almost impossible for investors to satisfy a criminal standard of proof. If the higher criminal threshold standard of proof applies in arbitration, unscrupulous host state parties can simply deny wrongdoing and enjoy the protection of such higher standard of proof.

Moreover, as a more serious problem, such trend could invite states to abuse ethics. In cases where a state is involved in a corruption case, often only the state is in a position to prove that a non-state entity successfully bribed a state official due to its control over its officials. It is of concern that this might create a rather perverse incentive for a state to benefit from its own omissions in allowing corruption. There is cynical logic that a state party advisor could recommend ensuring that a non-state party (such as an investor in investment arbitration) pay a bribe in violation of the laws of the host state.[40] Such bribery would then provide the host state with a type of insurance against such investor successfully bringing any arbitration claim. This is because the host state could rely on and be secured by the 'corruption objection to jurisdiction' defense.[41]

Currently, the theories and views regarding the standard of proof in corruption proceedings are complicated, and the issues seem to be far from being settled. Thus, the decisions of arbitral tribunals vary in many different ways, which demonstrates that as yet there is no general consensus regarding the standard of proof for allegations of corruption, fraud or illegality.[42]

In *Rompetrol*, the claimant, a Dutch company, argued that criminal investigations by the Romanian authorities regarding conduct by individual company officers breached the BIT's provisions on fair and equitable treatment (FET), physical protection, and security and non-impairment. In order to assess the evidence provided by the claimant, the tribunal decided to apply "the normal rule of the 'balance of probabilities' as the standard appropriate to the generality of the factual issues before it." The tribunal observed that it would 'where necessary adopt a more nuanced approach and would decide in each discrete instance whether an allegation of seriously wrongful conduct by a Romanian State official at either the administrative or policymaking level has been proved on the basis of the entire body of direct and indirect evidence before it.'[43]

This approach taken by the tribunal in *Rompetrol* seems to be one of the examples of keeping a good balance between the need for a sufficient standard of proof in corruption cases, and the possibility of abuse of too high a standard of proof. Such approach would be justified especially under the current trend where tribunals are increasingly willing to be involved in the procedure and decision-making processes surrounding party's allegations on corruption issues.[44] Finally, in respect of a gateway issue, the various issues and views regarding the burden of proof and the standard of proof should be taken into the consideration.

D. Assessing the Legal Consequences of Proven Corruption

The legal consequences sought by the party alleging the corruption are usually the termination of arbitral proceedings in the 'gateway phase.' An arbitrator can be guided by the following inquiries, which are to be on the checklist, and which often provide at least a sounds legal argumentation and arbitral examples for a consideration of categories of the legal consequences:

1. IIA with 'Illegality' Language in Investment Definition

In assessing the legal consequences of corruption that is proven in the 'gateway phase' of investment 'treaty' arbitration proceedings, it is important to see if the applicable investment treaty has language that could be read as requiring that the definition of the 'investment' to be protected under that investment treaty must be legal rather than illegal. The language of the definition of the protected 'investment' often includes the term 'in accordance with the applicable laws and regulations' of the host state. For example, Article 58(b) f. of the Japan-Indonesia EPA provides as follows:

> the term "investments" means every kind of asset invested by an investor, *in accordance with applicable laws and regulations*, including, though not exclusively.... (*emphasis added*)

The existence of such language might affect the jurisdiction of the arbitral tribunal if and when corruption is found to have existed, because such finding of proven corruption could lead to the conclusion that since the investment in question was **not** made 'in accordance with applicable laws and regulations' of the host state, such investment tainted by illegality could not satisfy the requirements for the 'investment' protected under the applicable investment treaty and therefore, the arbitral tribunal lacks jurisdiction to hear the case.

In fact, in *Metal-Tech*, where the applicable Israel-Uzbekistan BIT had a clause for definition of 'investment' (Article 1(1)), which reads:

> The term "investments" shall comprise any kind of assets, implemented in accordance with the laws and regulations of the Contracting Party in whose territory the investment is made, the Tribunal finds that this clause 'defines investments to mean only investments implemented in compliance with local law.'[45]

Where the relevant investment treaty has the language of the definition of the 'investment' protected thereunder which would read to include the legality requirement, one should further ask if that legality requirement needs to be satisfied only at the time of the establishment of the investment, or if corruption made at a later stage could also affect the legality of the investment.

2. No IIA with Illegality Language

Where there is no language in the relevant investment treaty that would read to require legality of the investment, ICSID tribunals have taken different approaches in dealing with the legal effect of their finding of corruption at the gateway stage:

2.1 Implicit Reading of Legality Requirement Under Article 25(1) of the ICSID Convention

In *Phoenix Action v Czech Republic*, the ICSID tribunal found that 'States cannot be deemed to offer access to the ICSID dispute settlement mechanism to investments made in violation of their laws' and concluded 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.'[46] The *Phoenix Action* tribunal held:

> The purpose of the international mechanism of protection of investments through ICSID arbitration cannot be to protect investments made in violation of the laws of the host State or investments not made in good faith, obtained for example through misrepresentations, concealments or *corruption [emphasis added]*, or amounting to an abuse of the international ICSID arbitration system. In other words, the purpose of international protection is to protect legal and *bona fide* investments.[47]

> The tribunal thus found that the Claimant's principal had established Phoenix Action, an Israeli company, to simply "buy Czech companies he owned as a Czech citizen living in the Czech Republic, after the actions taken by the Czech Republic against these companies",[48] concluding that the "initiation of and pursuit of this arbitration is an abuse of the system of international ICSID investment arbitration",[49] and that therefore the tribunal lacked jurisdiction.

It should be noted, however, that other ICSID tribunals do not share the view that legality requirement is implicit in Article 25(1) of the ICSID Convention (*e.g., Metal-Tech*).[50]

2.2 General Principles of Public International Law

Other ICSID tribunals have dismissed claims on the ground of corruption, fraud or other illegality, not relying upon the theory that there is an implicit legality requirement under Article 25 of the ICSID Convention, but based upon general principles of international law and public policy. For example, the ICSID tribunal in *Plama v Bulgaria* found a fraudulent conduct by the investor in making its investment, violating the rules and principles of international law, including the principle of good faith, and held that granting the Claimant's investment the protections provided by the Energy Charter Treaty would be contrary to the principle of *memo audiur propriam turpiudinem allegrans* and 'contrary to the basic notion of international public policy — that a contract obtained by wrongful means (fraudulent misrepresentation) should not be enforced by a tribunal.'[51]

It should be noted that where the ICSID tribunals rely upon such general principles of public international law rather than the explicit legality requirement of the protected 'investment' under the applicable BIT or the implicit legality requirement read into Article 25 of the ICSID Convention, they may dismiss the claims not on the lack of jurisdiction under the applicable BIT or ICSID Convention but on the basis of the lack of admissibility of claims, or on the lack of the merit of the claims.[52]

2.3 Arbitrability Issue (Judge Lagergren's Approach)

In one of the most famous cases dealing with corruption in international arbitration in the early year (as early as 1963), Judge Lagergren sitting as a sole arbitrator in ICC Case No. 1110, denied jurisdiction over a dispute about the payment of commissions out of an intermediary agreement involving bribery.[53] While this case is so famous, it should be noted that this was a

commercial arbitration but not an investment treaty arbitration, and as is put by a recent article, 'currently it is commonly recognized by both arbitral case-law and scholarly writing that an arbitral tribunal has jurisdiction to decide upon cases of corruption. Furthermore, disputes involving corrupt activity are considered to be arbitrable as well.'[54]

3. 'Balancing' Approach

Given the discussions accumulated so far and past arbitral awards, it seems there is a clear tendency for arbitral tribunals to dismiss cases due to corruption if the corruption occurred in the course of investment activity with both parties' involvement. Nonetheless, the outcome of this approach is rather drastic: the investor is deprived of protection and, consequently, the host state avoids any potential liability. Therefore, if the 'clean hand' doctrine should be adopted, it may also be useful to leave room in the checklist for more of a 'balancing' approach involving a case-by-case assessment. One might think that applying such balancing approach would be more appropriate in the merits phase rather than the gateway phase, but further discussions on this issue are beyond the scope of this article.

E. Other 'Gateway Issues' regarding Corruption

If an arbitrator reaches the conclusion that a case should be dismissed due to corruption, one further issue remains: which party should bear the costs incurred in connection with the arbitration, including the legal fees? In this regard, tribunals may be afforded a wider range of discretion compared to jurisdiction, admissibility or arbitrability issues. For instance, Article 61(2) of the ICSID Convention, which establishes the discretion of tribunals in allocating ICSID arbitration costs and the costs incurred by the parties in connection with the arbitration (including legal fees),[55] provides as follows:

> the Tribunal shall, except as the parties otherwise agree, assess the expenses incurred by the parties in connection with the proceedings, and shall decide how and by whom those expenses, the fees and expenses of the members of the Tribunal and the charges for the use of the facilities of the Centre shall be paid.

In fact, in *Metal-Tech*, despite the tribunal dismissing the case because of corruption that both parties were allegedly involved in, the tribunal held that each party was to bear its own legal fees and expenses and equally share the costs of the proceeding, including the ICSID fees. In reaching this conclusion, the tribunal emphasized the fact that the state had also participated in creating the situation that led to the dismissal of the claim and, because of this participation, which is implicit in the very nature of corruption, it appeared fair that the parties share in the costs.[56]

It should also be noted that, in contrast, if a case is dismissed due to illegality solely on the investor or claimant side, tribunals tend to impose all the costs on the claimant. In *Phoenix,* where the investor made an investment 'for the sole purpose of bringing international litigation against the Czech Republic,' the tribunal ruled that such investment 'is not a *bona fide* transaction and cannot be a protected investment under the ICSID system'[57] and, therefore, ordered Phoenix Action to pay the full amount of the Czech Republic's fees and costs.

Therefore, the checklist may need to cover the issue of cost bearing, and, at least for this particular subject, arbitrators should be given more flexibility to reach more balanced conclusions even in cases that have to be dismissed due to a claimant's participation in corruption.

IV CONCLUSION

It is evident that a clear consensus or policy for tribunals in international investment arbitration that are charged with handling this difficult task is needed considering the fact that corruption frequently takes place in connection with foreign investment. One possible and reasonable solution would be to adopt the 'clean hand' doctrine in line with the global trend of anti-corruption legislation recognizing that 'offering' should be regulated. Nonetheless, in situations where cases are dismissed due to corruption, the investor is deprived of protection and, consequently, the host state avoids any potential liability. Considering this drastic outcome, nonetheless, a comprehensive and detailed discussion would be necessary, and the outcome of such discussion should be appropriately embodied in a policy or checklist for arbitrators.

NOTES

1 For example, the following articles thoroughly discuss various aspects of this issue:

Bishop, Doak and Stevens, Margrete, '*International Code of Ethics for Lawyers Practicing Before International Arbitral Tribunals*,' presented at the ICCA Conference (26 May 2010), available at **http://www.arbitration-icca.org/media/0/12763302939400/stevens_bishop_draft_code_of_ethics_in_ia.pdf.**

Fox, Todd and Wilske, Stephan, '*Corruption in International Arbitration and Problems with Standard of Proof*,' International Arbitration and International Commercial Law: Synergy, Convergence and Evolution — Liber Amicorum Eric Bergsten, 2011, p.489 *et seq*.

Raeschke-Kessler, Hilmar, '*Corruption in Foreign Investment — Contracts and Dispute Settlement Between Investors, States, and Agents*,' The Oxford Handbook of International Investment Law, 2008, pp.584-616.

Khawar, Qureshi, '*Too Hot to Handle?*,' New Law Journal, 2010, p.25 *et seq*.

Lamm, Carolyn; Greenwald, Brody and Young, Kristen, '*From World Duty Free to Metal-Tech: A Review of International Investment Treaty Arbitration Cases Involving Allegations of Corruption*,' ICSID Review, Vol. 29, 2014, pp.328-349.

Scherer, Matthias, '*Circumstantial Evidence in Corruption Cases Before International Arbitral Tribunals*,' International Arbitration Law Review, Vol. 5, 2002, p.29 *et seq*.

Toulson, Tom, '*Do Counsel Need An Ethical Code?*,' Global Arbitration Review, 2010, available at **http://www.globalarbitrationreview.com/news/article/28658.**

Wilske, Stephan, '*The Corruption Objection to Jurisdiction in Investment Arbitration: Does it Really Protect the Poor?*,' Poverty and the International Economic Legal System Duties to the World's Poor, 2013, pp.177-188 ('Wilske I').

Ross, Alison, '*Should "Clean Hands" Be a Factor in Investment Arbitration?*,' Global Arbitration Review, 2009, available at **http://www.globalarbitrationreview.com/news/article/19249.**

Wilske, Stephan, '*The Global Competition for the "Best" Place of Arbitration for International Arbitrations — A More or Less Biased Review of the Usual*

Suspects and Recent Newcomers,' Contemporary Asia Arbitration Journal, Vol. 1, 2008, p.21 *et seq*. ('Wilske II').

Wilske, Stephan et al., '*International Investment Treaty Arbitration and International Commercial Arbitration — Conceptual Difference or Only a "Status Thing"?,*' Contemporary Asia Arbitration Journal, Vol. 1, 2008, p.216 *et seq*.

Wilske, Stephan, '*Crisis? What Crisis? — The Development of International Arbitration in Tougher Times,*' Contemporary Asia Arbitration Journal, Vol. 2, 2009, p.187 *et seq*. ('Wilske III').

Wilske, Stephan, '*The Impact of the Financial Crisis on International Arbitration,*' Dispute Resolution Journal, Vol. 65, 2010, p.82 *et seq*. ('Wilske IV').

2 The final report issued by the joint task force is available at: **http://www.mofa.go.jp/mofaj/gaiko/oda/seisaku/f_boushi/01/pdfs/shiryo04.pdf** (Japanese)

3 Chart 8a: Disputes Decided by Arbitral Tribunals under the ICSID Convention and Additional Facility Rules — Findings, The ICSID Caseload — Statistics (Issue 2014-2), at 14, available at: https://icsid.worldbank.org/apps/ICSIDWEB/resources/Documents/ICSID%20Web%20Stats%202014-2%20(English).pdf

4 *World Duty Free Co. Ltd. v Kenya*, ICSID Case No. ARB/00/7, Award (4 October 2006).

5 *Metal-Tech Ltd. v Uzbekistan*, ICSID Case No. ARB/10/3, Award (4 October 2013).

6 *See, e.g., Rompetrol Group N.V. v Romania*, ICSID Case No. ARB/06/3, Award (6 May 2013) para.178.

7 *See, e.g.,* Lamm (n.1), p.331.

8 *See, e.g.,* Redfern, Alan, '*The Practical Distinction Between the Burden of Proof and the Taking of Evidence — An English Perspective,*' in The Standards and Burden of Proof in International Arbitration, Arbitration International, Vol. 10, 1994, pp.317, 320.

9 *See, e.g., Tokios Tokekes v Ukraine*, ICSID Case No. ARB/02/18, Award (26 July 2007) para 124; *Rompetrol* (n.6), para.183.

10 Arbitration Rules of the United Nations Commission on International Trade Law ('UNCITRAL Arbitration Rules') (2010) art. 27(1) ('Each party shall have the burden of proving the facts relied on to support its claim or defence').

11 Redfern (n.8), pp.317, 320.

12 The Convention on the Settlement of Investment Disputes Between States and Nationals of Other States.

13 *See, e.g., Asian Agricultural Products Ltd. (AAPL) v Republic of Sri Lanka*, ICSID Case No. ARB/87/3, Award (27 June 1990) para.56; *Rompetrol* (n.6), para.179; *Metal-Tech* (n.5), para.237.

14 Fox (n.1), p.489 *et seq*.

15 *Metal-Tech* (n.5), para.238.

16 *Ibid.*, para.238.

17 Lamm (n.1), p.336.

18 *Ibid.*, p.335.

19 In *Rompetrol* (n.6), the ICSID Tribunal rejected the concept of shifting the burden of proof because, in its view, 'the burden of proof is absolute' at para.178.

20 *Ibid.*, para.184. *See also* Lamm (n.1), p.337.

21 *EDF (Services) Ltd. v Romania*, ICSID Case No. ARB/05/13, Award (8 October 2009).

22 *Ibid.*, para.221.

23 Lamm (n.1), p.333.

24 *Rumeli Telekom AS and Telsim Mobil Telekomikasyon Hizmetleri AS v Republic of Kazakhstan*, ICSID Case No. ARB/05/16, Award (29 July 2008) para.709 (requiring clear and convincing evidence to prove alleged criminal conspiracy); *African Holding Company of America, Inc. and Société Africaine de Construction au Congo S.A.R.L. v La République démocratique du Congo*, ICSID Case No. ARB/05/21, Sentence sur les déclinatoires de compétence et la recevabilité (29 July 2008) para.52 (requiring irrefutable proof such as that resulting from criminal prosecution to prove corruption).

25 *Bayindir Insaat Turizm Ticaret ve Sanayi AS v Islamic Republic of Pakistan*, ICSID Case No. ARB/03/29, Award (27 August 2009) paras. 142-3 (requiring proof 'sufficient to exclude any reasonable doubt' to prove bad faith).

26 *Saba Fakes v Republic of Turkey*, ICSID Case No. ARB/07/20, Award (14 July 2010) para.131 (finding that the standard for 'any allegations of impropriety is particularly heavy').

27 Crivellaro, Antonio, '*Arbitration Case Law on Bribery: Issues of Arbitrability, Contract Validity, Merits and Evidence*,' TDM 3 (2005), Arbitration Money Laundering, Corruption and Fraud, Dossiers — ICC Institute of World Business Law.

28 Case No. 4 (Interim and Final Awards in ICC Case No. 4145 of 1983, 1984 and 1986), the arbitral tribunal ruled that, although the 'consultancy price was very high,' this element was not sufficient, alone, to prove corruption.

29 Case No. 6 (ICC Case No. 5622; Award of August 1982 (annulled) and Second Award of April 1992 (Hilmarton Matter))(Hilmarton Case, First Award), the arbitrator concluded that the evidence was not sufficient to establish 'with certainty' the existence of corruption. He decided, however, that the agreement was in violation of Swiss public policy and was hence invalid since the agent was appointed in patent violation of Algerian law forbidding intermediaries in administrative contracts.

30 Case No. 12 (ICC Case No. 6286 of 1991 (Partial Award)), the arbitral tribunal required clear proof that the amounts paid to the agent 'were intended' to bribe officials to trade on their influence to obtain favors. No such proof was provided, so bribery and corruption were deemed not to have been present.

31 Case No. 13 (ICC Case No. 6401 of 1990/1991 (Westinghouse)), (the Westinghouse/President Marcos Case), the arbitrators applied the standard of proof required in the three States (the Philippines, New Jersey and Pennsylvania) of the parties; that is, 'clear and convincing evidence' of bribery. Case No. 20 (Ad Hoc award of 28 July 1995), 21 (ICC Case No. 7664 of 1996), 22 (ICC Case No. 8113 of 1996), 24 (ICC Case No. 9333 of 1998) and 25 (Award of 4 May 1999 in an Ad-hoc UNCITRAL Arbitration), the arbitrators ruled that 'clear and convincing' evidence was needed in order to declare the agreement invalid because of corruption.

32 Case No. 14 (ICSID Case No. ARB/84/3 of May 1992), the arbitral tribunal stated that 'allusions not supported by evidence and based on suppositions' are not sufficient to prove corruption.

33 Case No. 16 (ICC Case of 31 March 1992), proof that the agent was hired to influence the employer's award was deemed lacking. The Paris Appeal Court confirmed that no proof of traffic of influence had been provided.

34 Case No. 17 (ICC Award of 1993), 'no direct or circumstantial evidence of bribery' was found.

35 Case No. 18 (ICC Case No. 6497 of 1994), several agency agreements were disputed, but 'conclusive evidence' of bribery was not found to have been provided in a vast majority of the agreements, notwithstanding the disproportion between the price paid to and the costs borne by the agent. A 'high degree of probability of bribery' was, however, found in relation to one of the agreements, in which the commission amounted to the 'extremely unusual' fee of 33.33%.

36 Case No. 19 (ICC Case No. 7407 of 1994), the majority of the arbitral tribunal ruled that 'a mere suspicion by a member of the arbitral tribunal is entirely insufficient' to prove the presence of corruption. The clause 'exonerating the agent from proving his actual services' was not considered a sufficient indication of an illicit intent.

37 Case No. 11 (ICC Case No. 6248 of 1990), a violation of fiduciary duty contrary to public international policy and to *bonos mores* under Swiss law.

38 Crivellaro (n.27), p.115; Hwang S.C., Michael and Lim, Kevin, '*Corruption in Arbitration — Law and Reality*,' Asian International Arbitration Journal, Vol. 8, 2012, p.15.

39 Hwang (n.38), p.19.

40 Fox (n.1), p.499.

41 Wilske II (n.1), pp.1, 15.

42 Lamm (n.1), p.334.

43 *Rompetrol* (n.6), para.183.

44 Kendra, Thomas and Bonini, Anna, '*Dealing with Corruption Allegations in International Investment Arbitration: Reaching a Procedural Consensus?*,' Journal of International Arbitration, Vol. 31, 2014, p.439.

45 *Metal-Tech* (n.5), para.373.

46 *Phoenix Action, Ltd. v The Czech Republic*, ICSID Case No. ARB/06/5, Award (15 April 2009) para. 101.

47 *Ibid.*, para.100.

48 *Ibid.*, para.137.

49 *Ibid.*, para.144.

50 *Metal-Tech* (n.5), para.127.

51 *Plama Consortium Limited v Republic of Bulgaria*, ICSID Case No. ARB/03/24, Award (27 August 2008) paras. 138-140, 143-145.

52 *See*, *World Duty Free* (n.4), para.179, dismissing the claims as inadmissible in ICSID arbitration based on contract; *see also Niko Resources (Bangladesh) Ltd. v People's Republic of Bangladesh*, ICSID Case Nos ARB/10/11 and ARB/10/18, Decision on Jurisdiction (19 August 2013) para.471, holding that the 'alleged or established lack of good faith of the investment does not justify the denial of jurisdiction but must be considered as part of the merits of the dispute.'

53 ICC Award No. 1110 of 1963, Year Book Commercial Arbitration, 1996, p.47.

54 Nueber, Michaeal, '*Corruption in International Commercial Arbitration — Selected Issues*,' Austrian Yearbook on International Arbitration, 2015, p.4.

55 *Metal-Tech* (n.5), para.421.

56 *Ibid.*, para.422.

57 *Phoenix* (n.46), paras. 134, 142.

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