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COMBATING CORRUPTION THROUGH INTERNATIONAL INVESTMENT TREATY LAW[1]

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ABSTRACT

Corruption plays an important role in investment arbitration. Parties to arbitral proceedings make allegations of bribery with increasing frequency. However, the lack of unambiguous guidelines on how to treat such allegations arguably has contributed to a shortage of affirmative decisions, even where further evidence might have been available to the arbitral tribunal. This is problematic, as the inflow of illicit moneys through investment projects can severely undermine anti-corruption efforts in the host state. This paper investigates options for integrating the strong legal regime of investment arbitration — which brings together foreign investors and host states as principal actors in transnational corruption — further into the fight against corruption. It is based upon an analysis of investment treaties, investment arbitration awards, subject literature and expert interviews. It is submitted that states should press for explicit anti-corruption provisions in investment treaties. The aim of these provisions must be to exclude corruption-tainted assets from the protections afforded by investment treaties. An anti-corruption Model Clause is proposed as a reference for drafters and negotiators of future investment treaties. The Model Clause makes access to arbitral procedures subject to the investor's compliance with international anti-corruption law.

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1 INTRODUCTION

The framework of international trade relations is undergoing major changes. The meaning of such notions as free trade and fair trade diverge widely[2] and the usefulness of investment protections as a whole is being questioned. However, the chances of achieving an anti-corruption consensus amongst the stakeholders appear much better, as corruption hurts honest investors and affected citizens alike. On the one hand, corruption causes citizens to lose trust in their representatives and burdens them with reduced quality in government services and heightened inequality. On the other hand, investors face corruption as an extra cost of operation. And where corruption is present, scrupulous investors suffer competitive disadvantages and elevated uncertainty, since rejecting a request for a bribe could result in the loss of an important contract to a competitor.

The relationship between foreign investment and corruption is a prominent feature in the history of numerous countries facing hardships currently. In many cases, foreign investments have helped to prop up corrupt, oppressive and kleptocratic regimes, have weakened state structures and have diminished any hope of achieving sustainable peace.[3] Accordingly, improvements in the fight against corruption would benefit all and it is in this fight that investment law can play a significant role, in that it "minimises dependence on public officials who are subject to capture by wealthy outsiders".[4] Most governments do not deploy investment law actively as a mechanism to achieve good governance and pursue anti-corruption objectives.[5] However, the need for action in this regard has become evident, not least against the backdrop of investment arbitration proceedings increasingly becoming venues for corruption-related disputes.[6]

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2 Pieth M (2016) *Wirtschaftsstrafrecht* Basel: Helbling Lichtenhahn Verlag at 14.

3 See, for example, McKindley J (17 March 1997) "Zairian Rebels' New Allies: Men Armed With Briefcases" *New York Times*, available at http://www.nytimes.com/1997/04/17/world/zairian-rebels-new-allies-men-armed-with-briefcases.html (visited 28 December 2017); Ross M (May/June 2008) "Blood Barrels – Why Oil Wealth Fuels Conflict" *Foreign Affairs*, available at https://www.foreignaffairs.com/articles/2008-05-03/blood-barrels (visited 28 December 2017). See also Collins D (2017) *An Introduction to International Investment Law* Cambridge: Cambridge University Press at 25 *et seq*.

4 Carrington P (2007) "Law and Transnational Corruption: The Need for Lincoln's Law Abroad" 70(4) *Law and Contemporary Problems* 109-138 at 109.

5 Gordon K (2008) *International investment Law: Understanding Concepts and Tracking Innovations* Paris: OECD at 138.

6 See, for example, Yeomans J (22 May 2017) "BSGR attacks 'unlawful' activities of Rio Tinto in Guinea as Simandou hearing opens" *The Telegraph,* available at http://www.telegraph.co.uk/business/2017/05/22/bsgr-attacks-unlawful-activities-rio-tinto-guinea-simandou-hearing/ (visited 28 December 2017).

This paper therefore investigates options for integrating the strong legal framework of investment law into the anti-corruption domain. The text is divided into three parts. In the first part — after a section on the methodology applied — §3 and §4 introduce the concepts of investment law and investment arbitration, as well as the occurrence of corruption in these areas. In the second part, an inquiry into available legal bases for the so-called corruption defence is undertaken. While §5 looks at legal principles and doctrine on which the defence has been based, §6 investigates examples of such legal bases found in investment treaties. In the final part, §7, the findings of the paper are rendered in a Model Clause.

2 METHODOLOGY

The paper is based largely on a quantitative analysis of investment treaty awards and international investment agreements as contained in reputable legal databases. For investment treaty awards, the following databases were used: Oxford University Press Investment Claims;[7] Thomson Reuters Westlaw International Materials;[8] and Investment Arbitration Reporter.[9] For investment agreements, reliance was placed on the United Nations Conference on Trade and Development (UNCTAD) International Investment Agreements Navigator.[10] The databases were searched with the following search terms: “corruption”, “corrupt” and “bribery”.

The large number of investment treaty awards that was produced by this search was examined and a group of 30 awards in which corruption played a significant role was extracted. The analysis then focused on criteria such as whether the investor or the host state alleged corruption, whether the corruption allegation was scrutinised by the arbitral tribunal, the success rate of corruption allegations and the predominant reasons for failed corruption allegations. The international investment agreements that were identified in the web-based search were analysed also for the rigour of their corruption provisions, as well as their applicability in a dispute resolution scenario.

This analysis, along with an examination of the principal subject literature and interviews with two experts, enabled the identification of a series of problem areas and shortcomings which are documented in §5 and §6. The Model Clause in §7 expresses the findings of the study and encapsulates an attempted solution by the author. A draft of the Model Clause was presented at the 2017 OECD Anti-

7 Available at http://oxia.ouplaw.com/home/ic (visited 28 December 2017).
8 Available at https://legalresearch.westlaw.co.uk/ (visited 28 December 2017).
9 Available at https://www.iareporter.com/ (visited 28 December 2017).
10 Available at http://investmentpolicyhub.unctad.org/IIA (visited 28 December 2017).

Corruption & Integrity Forum in Paris and discussed with interested attendees.[11] Their feedback and reactions have been incorporated into this paper.

3 INTERNATIONAL INVESTMENT LAW AND INTERNATIONAL ANTI-CORRUPTION LAW

Foreign direct investment (FDI) is a critical component of the world's economy. Since many developing countries lack the technology, capital and other resources to develop their industries, FDI is seen as crucial to making markets more competitive in a globalised economy.[12] In order to make foreign investors feel more secure, governments of developing countries have entered into international investment agreements (IIAs).[13] Bilateral investment treaties (BITs) are in the foreground of such IIAs.[14] BITs — more than 2 300 of which are currently in force — typically offer investors protection against "arbitrary and discriminatory" treatment by the host state, a guarantee of "fair and equitable treatment" and protection against expropriation without adequate compensation.[15] Furthermore, in most BITs, host states consent to so-called investment arbitration, allowing individual foreign investors to claim directly the protections offered before an international tribunal against a state party to the treaty. Thereby, investors are enabled to bypass the host state's domestic legal system.[16]

Mainly since the early 1990s, investors have brought hundreds of arbitration claims against host states. The leading body for international investment arbitration is the International Centre for Settlement of Investment Disputes (ICSID), an arm of the World Bank created in 1965 to promote economic development.[17] ICSID arbitration is subject to the ICSID Convention which contains

11 The presentation is available at https://www.oecd.org/cleangovbiz/Integrity-Forum-2017-Mbiyavanga-international-investment-law-poster.pdf (visited 28 December 2017).

12 Moses M (2012) *The Principles and Practice of International Commercial Arbitration* (2ed) Cambridge: Cambridge University Press at 230.

13 Chaisse J & Bellak C (2011) "Do Bilateral Investment Treaties Promote Foreign Direct Investment? Preliminary Reflections on a New Methodology" 3(4) *Transnational Corporations Review* 3-10 at 4.

14 Moses (2012) at 239. See also Chaisse J (2015) "The Shifting Tectonics of International Investment Law — Structure and Dynamics of Rules and Arbitration on Foreign Investment in the Asia-Pacific Region" 47(3) *George Washington International Law Review* 563-683 at 565.

15 Llamzon A (2014) *Corruption in International Investment Arbitration* Oxford: Oxford University Press at 41.

16 Losco MA (2014) "Streamlining the Corruption Defence: A Proposed Framework for FCPA—ICSID Interaction" 63 *Duke Law Journal* 1201-1242 at 1205.

17 Scheuer C (2001) *The ICSID Convention: A Commentary* Cambridge: Cambridge University Press at 5.

a regime of jurisdictional limitations that may preclude access to the Centre.[18] Today, ICSID administers 70% of all known international investment dispute settlements and, as of December 2017, 161 states have signed the ICSID Convention.[19]

Parties wishing to arbitrate with ICSID must meet three jurisdictional criteria: firstly, one party must be a Contracting State and the other must be a national of another Contracting State, secondly, the state party must have consented in writing; and, lastly, the dispute must be a legal one and must arise out of an investment.[20]

This collective international effort to provide an investment-friendly environment in high-risk countries often is compromised by domestic struggles within the latter. Corruption in general and bribery in particular are primary concerns in this regard, as they have a particularly corrosive effect on the attractiveness of a domestic market to foreign investors.[21] These realisations, *inter alia,* have led to the emergence of international anti-corruption law. The major turning point in the regulation of bribery of foreign officials came in 1977, when the United States introduced the Foreign Corrupt Practices Act (FCPA). Nevertheless, until the 1990s, bribery was still considered very much a "necessary evil" and the FCPA was used only sparingly.[22] Since then, however, a great deal of energy has been put into the creation of an international, multilateral regime based on the example of the FCPA.[23] Pieth explains:

> Whereas the post-colonial world of the 'Cold War' made intensive use of bribery to foster and forge alliances and to continue to obtain access to natural resources in former colonies, with the opening of the East the

18 Tupman M (1986) "Case Studies in the Jurisdiction of the International Centre for Settlement of Investment Disputes" 35(4) *International &Comparative Law Quarterly* 813-838 at 813.

19 Available at https://icsid.worldbank.org/en/Pages/about/Database-of-Member-States.aspx (visited 28 December 2017).

20 Moses (2012) at 232.

21 Foreword to UNCAC by former UN Secretary-General Kofi Annan. See also ASEAN Business Outlook Survey (2017) at 14, available at https://www.uschamber.com/report/asean-business-outlook-survey-2017 (visited 28 December 2017). For an in-depth discussion of the phenomenology of corruption see Pieth (2016) at 166 *et seq*.

22 Heimann F & Pieth M (2018) *Confronting Corruption* New York: Oxford University Press at 75.

23 Davis K (2013) "Does the Globalisation of Anti-Corruption Law Help Developing Countries?" in Rose-Ackerman S & Carrington P (eds) *Anti-Corruption Policy: Can International Actors Play a Constructive Role*? Durham: Carolina Academic Press at 170.

> rules of economic engagement changed and in particular G7 countries were no longer interested in a corruptive catch-as-catch-can.[24]

This international legal regime includes the Organisation for Economic Co-operation and Development Convention on Combating Bribery of Foreign Public Officials in International Business Transactions (OECD Convention) of 1997 and the United Nations Convention against Corruption (UNCAC) of 2003.

Generally, international anti-corruption conventions interact with FDI and investment law in at least three ways:[25] Firstly, they influence FDI via their effects on domestic and international laws and practices. Secondly, they provide a source of concepts, definitions and principles that can be integrated directly into the texts of BITs.[26] Thirdly, in rare cases they are used as guidance in decision-making by investment arbitration panels.

4 THE CORRUPTION DEFENCE IN INVESTMENT TREATY ARBITRATION

The usual setting in which investment arbitration takes place is that of an investor bringing a claim against a host state, for example, for loss of investment. However, by invoking the so-called corruption defence the host state can turn the tables and bring a counterclaim against the investor by alleging investment corruption, as a means of precluding the original claim and evading liability. The *raison d'être* of the corruption defence is that while arbitral tribunals are not tasked with punishing acts of corruption, they clearly "cannot grant assistance to a party that has engaged in a corrupt act".[27] This view enjoys a broad consensus and has been confirmed in various awards.[28]

The *Metal-Tech Ltd v Republic of Uzbekistan* Award is a good example of a successful corruption defence by a host state. In 2000, Metal-Tech entered into a

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24 Pieth M (2011) "Contractual Freedom v Public Policy Considerations in Arbitration" in Büchler A & Müller-Chen M (eds) *Private Law, National—Global—Comparative*, *Festschrift für Schwenzer* Bern: Stämpfli Verlag at 1379.

25 Gordon (2008) at 139.

26 See *Sistem Mühendislik Inşaat Sanayi ve Ticaret AŞ v Kyrgyz Republic* Award, ICSID Case No ARB(AF)/06/1, 9 September 2009 at para 41. The Tribunal relied directly on Art 1 of the OECD Convention as "a reasonable and useful definition" of bribery. See Betz K (2017) *Proving Bribery, Fraud and Money Laundering in International Arbitration* Cambridge: Cambridge University Press at 89 *et seq* for further comments.

27 *Metal-Tech Ltd v The Republic of Uzbekistan* Award, ICSID Case No ARB/10/3, 4 October 2013 at para 389.

28 See, for example, *International Thunderbird Gaming Corporation v The United Mexican States* Award, UNCITRAL Case, 26 January 2006 at para 112; *Inceysa Vallisoletana SL v Republic of El Salvador* Award, ICSID Case No ARB/03126, 2 August 2006 at para 250 (with regard to fraudulent activities).

joint venture (Uzmetal) with two state-owned enterprises (SOEs) of Uzbekistan to build and operate a modern plant in the country.[29] Metal-Tech concluded three "consulting agreements", worth USD 4.4 million, with individuals closely connected to the Uzbek Government.[30] In December 2006, both Uzbek SOEs filed domestic court proceedings which resulted in the liquidation and subsequent transfer of all of Uzmetal's assets to the Uzbek SOEs.[31] In January 2010, Metal-Tech filed a request for ICSID arbitration, claiming expropriation.[32] Uzbekistan's principal defence was that the Tribunal lacked jurisdiction because the claimant's investment was "made and operated" corruptly and in violation of the Uzbek law on bribery.[33] The Tribunal made findings of corrupt activities in respect of two of the three consulting agreements. Amongst other red flags, it was found that the contracting partners had no relevant experience or other qualifications for the services for which they were hired.[34] Since the applicable BIT only protected investments "implemented in accordance with the laws and regulations" of the host state, the claim raised by the investors was regarded as not covered by Uzbekistan's consent to arbitration contained in the BIT. Importantly, the claimants freely admitted to having made bribe payments, meaning that Uzbekistan did not have to prove corruption and the Tribunal did not have to consider and weigh additional evidence. Thereby, the Tribunal's decision was facilitated substantially.[35]

However, a look at investment law jurisprudence as a whole reveals that affirmative decisions on corruption defences are rarities. The number of publicly available investment arbitration awards in which corruption defences were approved by an arbitral tribunal can be counted on one hand still. And even where a corruption defence has been approved, it has been mostly in cases where the investors have presented evidence of their own wrongdoing, for example, by admitting to having paid a bribe.

It is submitted that, apart from arbitrators' lack of familiarity with the issue of corruption, it is a lack of procedural and substantive guidance that has contributed to the reluctance of tribunals to render affirmative decisions on

29 *Metal Tech v Uzbekistan* (2013) at paras 1, 7 & 13.
30 *Metal Tech v Uzbekistan* (2013) at paras 29 & 86. One of the consultants was the brother of the Prime Minister of Uzbekistan. See paras 90 & 226.
31 *Metal Tech v Uzbekistan* (2013) at paras 34 *et seq*.
32 *Metal Tech v Uzbekistan* (2013) at para 55.
33 *Metal Tech v Uzbekistan* (2013) at paras 110(i) & 110(ii).
34 *Metal Tech v Uzbekistan* (2013) at paras 311 *et seq* & paras 337 *et seq*.
35 *Metal Tech v Uzbekistan* (2013) at paras 240 *et seq.* See also Llamzon (2014) at 198.

corruption defences.[36] Some of the difficulties which tribunals have encountered are discussed in the next two sections.

5 DIFFERENT MEANS TO THE SAME END: THE CONCEPTS SUPPORTING CORRUPTION DEFENCES

In ICSID jurisprudence, three concepts are referred to most often in relation to corruption: firstly, the investor's obligation to invest "in accordance with host state law and regulations"; secondly, transnational public policy; and, thirdly, the doctrine of clean hands.

5.1 "In accordance with host state law" clauses

Investment agreements oftentimes stipulate that an investment must be made "in accordance with the host state's law and regulations". This is the so-called legality requirement. Accordingly, where an investor violates the laws or regulations of the host state, his dealings cannot be considered investments and arbitral tribunals will not have jurisdiction to render an award on the merits. By way of example, Article 1(1) of the India-Morocco BIT specifies that:

> The term 'investment' shall mean any kind of asset invested by investors on one Contracting Party in the territory of the other Contracting Party, in conformity with the laws and regulations of the latter.[37]

Even where no such phrasing is found in the text of a BIT, ICSID jurisprudence and subject literature generally recognise the legality requirement as an applicable international legal principle.[38]

However, it is unclear with which laws of the host state investors have to comply in order to enjoy treaty protections. ICSID case law reveals that not all types of violations of the domestic law of host states have led to an investment losing its BIT protections.[39] In *L.E.S.I-DIPENTA v Algeria*, the Tribunal held that the BIT's mention of conformity with laws only "seeks to exclude from protection all

36 For further comments, see §6.4 below.

37 Agreement between the Government of the Republic of India and the Government of the Kingdom of Morocco for the Promotion and Protection of Investments of 13 February 1999. See also Nadakavukaren K (2016) *International Investment Law 8* (2ed) Cheltenham: Edward Elgar Publishing at 125.

38 For example, *Fraport AG Frankfurt Airport Services Worldwide v The Republic of the Philippines* Award, ICSID Case No ARB/11/12, 10 December 2014 (cited as *Fraport v. Philippines II*) at para 332. See also Betz (2017) at 17 *et seq* for further references.

39 See Betz (2017) at 12; Grubenmann B (2010) *Der Begriff der Investition in Schiedsgerichtsverfahren in der ICSID-Schiedsgerichtsbarkeit*, Dissertation, Basel: University of Basel at 209 *et seq*.

investments made in violation of the fundamental principles".[40] In the same vein, several authors have argued that only "grave violations", such as conduct leading to civil judgments or criminal convictions, should have said consequences.[41]

Furthermore, reliance on national law to determine the BIT's scope of application seems problematic. Firstly, national criminal laws vary in quality. Conduct that is considered criminal in one country well may be allowed in another. Secondly, it is uncertain whether the legality principle imposes a continuous duty on the investor, or whether the provision concerns only the inception of the investment.[42] Thus, In *Fraport v Philippines I*, the Tribunal suggested that the "in accordance with" provision only applies to the initiation of the investment and that violations of the law of host states during the operation of an investment "might be a defence to claimed *substantive* violations of the BIT, but could not deprive a tribunal acting under the authority of the BIT of its jurisdiction".[43]

Lastly, determining the legality of an investment on the basis of national laws arguably encourages the abuse of national law-making powers. In this context, the dissenting arbitrator in *Fraport v Philippines I* noted the danger of states parties using "their legislative, executive and judicial powers to escape their responsibilities, including their obligation to arbitrate".[44] Of course, such a line of action would be contrary to the substantive provisions of BITs, for example, the requirement of fair and equitable treatment. However, a finding of corruption — even if based on domestic law — could preclude the Tribunal's jurisdiction to hear the case, and it never even would get to decide on violations of the treaty's substantive protections.[45]

40 *Consortium Groupement L.E.S.I.- DIPENTA v République Algérienne démocratique et populaire* Award, ICSID Case No ARB/03/08, 10 January 2005 at para 24(iii).
41 Betz (2017) at 18; Grubenmann (2010) at 211.
42 Losco (2014) at 1226.
43 *Fraport AG Frankfurt Airport Services Worldwide v The Republic of the Philippines* Award, ICSID Case No ARB/03/25,16 August 2007 (cited as *Fraport v Philippines I*) at para 345. Original emphasis.
44 *Fraport v Philippines I*, Dissenting opinion of Mr Bernardo M Cremades at §29.
45 *Fraport v Philippines I*, Dissenting opinion of Mr Bernardo M Cremades at §29.

5.2 Transnational public policy

There is a broad consensus in ICSID jurisprudence and legal literature that corruption runs contrary to transnational public policy. In the oft-referenced *World Duty Free v Kenya* arbitration,[46] the Tribunal held bribery to be "contrary to the international public policy of most, if not all, States or, to use another formula, to transnational public policy".[47]

Transnational public policy plays a crucial role in today's world of investment arbitration. It may be defined as "the general principles of morality accepted by civilised nations".[48] A violation of public policy may be grounds for setting aside a court award pursuant to Article V1(e) of the New York Convention of 1958. However, the notion of transnational public policy lacks sharp contours. In this connection, Meyer observes that:

> The exact definition of this concept, its legal functioning, its boundaries and even its existence are highly controversial.[49]

In the interests of predictability of legal procedures, applying precise rules with explicit objective provisions should be the main legal basis for any award and not the rather vague concept of transnational public policy.[50]

5.3 The clean hands doctrine

The clean hands doctrine embodies the maxim that "he who seeks equity must do equity", that is, the applicant has to bring its claim with clean hands. It derives from the more general principle of good faith.[51] However, whether the doctrine really exists is controversial. In *Guyana v Suriname*, the Tribunal indicated that "the use of the clean hands doctrine has been sparse, and its application in the instances in

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46 *World Duty Free Company v Republic of Kenya* Award, ICSID Case No Arb/00/7, 4 October 2006.

47 *World Duty Free v Kenya* (2006) at 157. See discussion in Betz (2017) at 21 & 75 *et seq*; Kreindler R (2010) "Corruption in International Investment Arbitration: Jurisdiction and the Unclean Hands Doctrine" in Hober K *et al* (eds) *Between East and West: Essays in Honour of Ulf Franke* Huntington: JurisNet Publishing at 309; Losco (2014) at 1223.

48 International Law Association (2000) *Report on the Sixty-Ninth Conference* London at 345.

49 Meyer O (2013) "The Formation of a Transnational Ordre Public against Corruption" in Rose-Ackerman S & Carrington P (eds) *Anti-Corruption Policy: Can International Actors Play a Constructive Role*? Durham: Carolina Academic at 231.

50 Betz (2017) at 32 *et seq*; Llamzon (2014) at 196.

51 See *Niko Resources (Bangladesh) Ltd v Bangladesh Petroleum Exploration & Production Company Limited ("Bapex") and Bangladesh Oil Gas and Mineral Corporation ("Petrobangla")* Award on Jurisdiction, ICSID Case No ARB/10/18, 19 August 2013 at para 476.

which it has been invoked has been inconsistent".[52] If the doctrine were accepted customary law or a general principle of law, Tribunals arguably would be able to apply it without a textual basis in the treaty.[53] However, several awards have negated the existence of the doctrine. For example, in the 2014 *Yukos v Russia* arbitration, the Tribunal stated that it was "not persuaded that the clean hands doctrine exists as a 'general principle of law recognised by civilised nations'".[54]

Nonetheless, in more recent times there appears to be a trend towards recognising the clean hands doctrine as a valid legal basis for corruption defences. Thus, the Tribunal in *Al-Warraq v Indonesia* (2014) applied the clean hands doctrine and declared the investor's claim inadmissible.[55] Furthermore, in the yet-to-be published *Spentex v Uzbekistan* (2016) arbitration, the Tribunal found corruption to be a violation of good faith, and hence that a claimant entering an arbitral procedure with "unclean hands" should not be heard.[56]

However, as there is no binding precedent in investment arbitration, it remains unclear whether future tribunals will continue the current trend of recognising the clean hands doctrine. Arguably, therefore, the smooth, universal and undisputed application of the doctrine would benefit significantly from explicit treaty-based empowerment.[57]

6 INVESTMENT TREATY DRAFTING: EMERGING TRENDS

The current inclination of host states to raise corruption as a defence cannot gloss over the fact that investment treaties were not designed originally to deal with this kind of counterclaim. The vast majority of older BITs are silent on corruption, providing no substantive framework for arbitrators to resolve corruption defences.[58] However, there is growing acknowledgment that investment treaties need to be "part of the equation" for reducing illicit financial flows.[59]

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52 *Guyana v Suriname* Award, Permanent Court of Arbitration, ICGJ 370 (PCA 2007), 17 September 2007 at para 418.

53 Burke-White W (2015) "Inter-Relationships between the Investment Law and Other International Legal Regimes" *E 15 Task Force on Investment Policy Think Piece* at 9.

54 *Yukos Universal Limited (Isle of Man) v Russian Federation* Award, PCA Case No AA 227, ICGJ 481 (PCA 2014), 18 July 2014 at para 1358. See also Betz (2017) at 295 *et seq*.

55 *Hesham Talaat M Al-Warraq v The Republic of Indonesia* Award, UNCITRAL Case, 15 December 2014 at para 646.

56 For further details, see Betz (2017) at 296. The case citation is *Spentex Netherlands, BV v Republic of Uzbekistan* Award, ICSID Case No ARB/13/26, 27 December 2016 (unpublished).

57 Burke-White (2015) at 9.

58 Llamzon (2014) at 62; Gordon (2008) at 135.

59 See Betz K & Pieth M (2016) "Globale Finanzflüsse und Nachhaltige Entwicklung" *Basel Institute on Governance Working Paper Series 21* at 10.

In the following, examples are presented of investment treaty language signifying that corruption has become an international policy issue. To begin with, Article 18.5 of the United States—Morocco Free Trade Agreement (FTA) of 2004 states that:

> 1. The Parties reaffirm their resolve to eliminate bribery and corruption in international trade and investment.
> 2. Each Party shall adopt or maintain the necessary legislative or other measures to establish that it is a criminal offence under its law, in matters affecting international trade or investment.

In a similar fashion, Article 8 of the Japan—Philippines BIT[60] of 2006 provides that:

> Each Party shall ensure that measures and efforts are undertaken to prevent and combat corruption regarding matters covered by this Agreement in accordance with laws and regulations.

Such programmatic provisions — further examples of which can be found in numerous other investment treaties — are directed primarily at national lawmakers. Therefore, they are not directly of use in dispute settlement. Such provisions may be useful reminders to the arbitral tribunal of the importance allocated to anti-corruption by the contracting parties. However, they do not give arbitrators adequate guidance for deciding a corruption defence.

The 2016 Morocco—Nigeria BIT,[61] as well as several model investment agreements, has gone a step further, to include a so-called carve-out clause aimed specifically at arbitration procedures. Generally speaking, carve-out clauses describe the scope of application of treaties. The effect of a carve-out clause is to limit such scope of application in order, for example, not to infringe upon non-economic and public policy interests. In the context of corruption, a carve-out clause would premise a tribunal's jurisdiction or an investment treaty's applicability upon the investor's compliance with anti-corruption law.[62]

The Morocco—Nigeria BIT is the only IIA identified in the preparation of this paper that contains an explicit clause on corruption which can be of direct use in dispute settlement. Article 17.2 of the Morocco—Nigeria BIT sets out the elements of the "corruption" offence. It reads:

60 Agreement between Japan and the Republic of the Philippines for an Economic Partnership.

61 Reciprocal Investment Promotion and Protection Agreement between the Government of the Kingdom of Morocco and the Government of the Federal Republic of Nigeria.

62 UNCTAD (2015) *World Investment Report 2015* Geneva: United Nations Publication at 133.

> Investors and their Investments shall not, prior to the establishment of an Investment or afterwards, offer, promise or give any undue pecuniary or other advantage, whether directly or through intermediaries, to a public official of the Host State, or a member of an official's family or business associate or other person in close proximity to an official, for that official or for a third party, in order that the official or third party act or refrain from acting in relation to the performance of official duties, in order to achieve any favour in relation to a proposed investment or any licences, permits, contracts or other rights in relations to an investment.

In the context of dispute resolution, paragraph 4 makes it clear that conduct violating Article 17 is deemed a "breach of domestic law of the Host State Party". If Article 17.4 is read with Article 1.3 of the treaty — which defines an investment as an "enterprise … in accordance with law of the Party in whose territory the investment is made" —it becomes apparent that any activity violating Article 17.2 cannot be considered an investment, and hence that an investment arbitration tribunal will not have jurisdiction to render an award on the merits.

A further example of a corruption carve-out clause is contained in the Southern African Development Community (SADC) Model BIT, which creates a "common obligation on corruption for investors" by stipulating that:

> Investors and their Investments shall not, prior to the establishment of an investment or afterwards, offer, promise or give any undue pecuniary or other advantage, whether directly or through intermediaries, to a public official of the Host State, or a member of an official's family or business associate or other person in close proximity to an official, for that official or for a third party, in order that the official or third party act or refrain from acting in relation to the performance of official duties, in order to achieve any favour in relation to a proposed investment or any licences, permits, contracts or other rights in relation to an Investment.[63]

What is more, the commentary attached to the model text indicates that investments which do not comply with the corruption obligation should be considered violations of the treaty and should no longer be considered covered investments. In such a case, all the dispute settlement rights of a bribing investor could be challenged. Notably, the language of both Article 17.2 of the Morocco—Nigeria BIT and Article 10.1 of the SADC Model Treaty is related closely to Article 1 of the OECD Convention.[64]

63 Article 10.1 of the 2011 Southern African Development Community Model Bilateral Investment Treaty and Commentary.

64 See §7 below.

Lastly, India's Model BIT[65] of 2015 contains the most explicit carve-out provision to be located during the preparation of this paper. Article 8.3 provides that:

> The Parties further agree that compliance with Articles 9, 10, 11 and 12 of this Chapter is compulsory and is fundamental to the operation of this Treaty. Investors and their Investments must comply with the obligations in Articles 9, 10, 11, and 12 to benefit from the provisions of this Treaty.

Article 9 goes on to prescribe an "obligation against corruption" in the following terms:

> 9.1 Investors and their Investments in the Host State shall not, either prior to or after the establishment of an Investment, offer, promise, or give any undue pecuniary advantage, gratification or gift whatsoever, whether directly or indirectly, to a public servant or official of the Host State as an inducement or reward for doing or forbearing to do any official act or obtain or maintain other improper advantage.
>
> 9.2 Except as otherwise allowed under the Law of the Host State, Investors and their Investments shall not engage any individual or firm to intercede, facilitate or in any way recommend to any public servant or official of the Host State, whether officially or unofficially, the award of a contract or a particular right under the Law of the Host State to such Investors and their Investments by mechanisms such as payment of any amount or promise of payment of any amount to any such individual or firm in respect of any such intercession, facilitation or recommendation.
>
> 9.3 Investors and their Investments shall not make illegal contributions to candidates for public office or to political parties or to other political organisations. Any political contributions and disclosures of those contributions must fully comply with the Host State's Law.
>
> 9.4 Investors and their Investments shall not be complicit in any act described in this Article, including inciting, aiding, abetting, conspiring to commit, or authorizing such acts.

In Article 8.3, the Indian Model BIT explicitly excludes any investor who does not comply with Article 9 from benefiting from the provisions of the treaty. While the provision makes extensive use of the language of Article 1 of the OECD Convention, it also explicitly outlaws facilitation payments, illegal political contributions, and complicity in any of the designated acts.

65 Model Text for the Indian Bilateral Investment Treaty of 2015.

6.1 Advantages of carve-out clauses

Carve-out clauses offer a number of benefits. Firstly, they represent a step toward levelling the playing field within the same market by ensuring that corrupt investors lose legal protection. This is particularly significant in the context of host states with relatively weak judicial systems, where otherwise there might be little motivation for foreign investors to maintain rule of law compliance.[66] Secondly, a BIT clause dedicated to anti-corruption will remind any tribunal deciding a dispute involving the BIT to examine suspicions of corruption thoroughly.

Thirdly, with the reliance on provisions and definitions in authoritative anti-corruption instruments such as the OECD Convention, the task of proving bribery can be facilitated. Significantly, the Tribunal in *Thunderbird v Mexico* acknowledged that due mainly to the influence of the international anti-corruption conventions, tribunals and courts have been open to the use presumptions rather than requiring fully-fledged and hard-to-obtain evidence.[67] Fourthly, the mere incorporation of a corruption carve-out clause represents a bold political statement by the parties to the investment treaty. It would emphasise that investment law and arbitration do not represent a "one-way-street favouring foreign investors".[68]

6.2 Likely challenges and objections to carve-out clauses

The greatest challenges to providing more explicit anti-corruption clauses in investment treaties are likely to be political ones.[69] This observation is rooted in the circumstance that, while a number of model investment treaties contain corruption carve-out clauses, the Morocco—Nigeria BIT was identified as the only investment agreement with legal force containing such a provision. The scarcity of best-standard anti-corruption norms outside of model agreements raises the suspicion that — rather than showing true anti-corruption commitment — model anti-corruption provisions are being used for political or tactical purposes, for example, as throw-away provisions during treaty negotiations.

A further challenge to the idea of including anti-corruption norms in BITs may come from those who consider investment arbitration to be the wrong forum

66 Burke-White (2015) at 9.

67 *Thunderbird v Mexico* (2006) at para 112.

68 Burke-White (2015) at 9.

69 Countries entering into investment agreements generally aim to establish a friendly environment for foreign investment. Where public policy concerns such as corruption enter the arena, however, conflicts of interests arise. For instance, export sector interest groups may lobby against the effective enforcement of anti-corruption norms due to fears of competitive disadvantages on the international market.

for corruption disputes.[70] The argument goes that rejecting jurisdiction due to corruption will incentivise host states to solicit bribes from investors. This relates to the structure of investment arbitration, where the investor almost always will be the claimant and the host state the respondent. Therefore, it is argued, the host state wins when proceedings are terminated for lack of jurisdiction.

However, it is submitted that where the tribunal concludes that corruption taints the investment to such an extent that jurisdiction must be negated, the host state should not be regarded as the winner. After all, the host state — understood as the totality of citizens living within the jurisdiction in question — does not benefit from such a finding. Rather, where jurisdiction is negated due to corruption, the public perception of the quality of the host state's administration declines considerably. The host state's reputation and prospects of attracting clean foreign investment are diminished, as henceforth honest investors likely will fear unlawful encroachment against their investments and might opt not to do business in the state in question.

Accordingly, not even in countries where the disjuncture between citizenry and administration is severe should one alter the conception of a host state representing the small ruling elite drawing an intermediate benefit from the closing of an arbitral procedure. Where a tribunal negates jurisdiction, this should be seen neither as a win for the host state nor as a punishment of the investor. Instead, it is the result of the obligations of arbitral tribunals towards the furtherance of global interests.

An additional argument against the inclusion of corruption clauses in investment agreements is that it would result in such agreements having to contain carve-out clauses for a wide range of issues, such as human rights, environmental protection and labour standards. However, unlike human rights and environmental protection, for example, corruption is an issue on which there is broad international consensus regarding subject matter and definition.[71] Furthermore, corruption is regulated by and criminalised under a relatively homogenous

70 See, for example, O'Toole L (2015) "Investment Arbitration: A Poor Forum for the International Fight against Corruption" *Yale Journal of International Law*, blog post, available at http://www.yjil.yale.edu/investment-arbitration-a-poor-forum-for-the-international-fight-against-corruption/ (visited 29 September 2017).

71 For example, the understanding of what constitutes torture differs significantly depending on the legal system studied. See Fernandez L & Muntingh L (2016) "The Criminalisation of Torture in South Africa" 60(1) *Journal of African Law* 83-109 at 89 *et seq*.

international legal framework.[72] Accordingly, it is justifiable to treat the issue of corruption differently from other public policy concerns.

7 MODEL CLAUSE

Building on the preceding discussion, this section proposes an anti-corruption Model Clause as a point of reference for treaty drafters. The Model Clause offers explicit guidance to arbitrators and counsel as to the objective requirements of and the remedy for a host state's corruption defence.

Model Clause — Bribery of Officials

1. Investments that, in whole or in part, have been procured, facilitated, established or operated in a manner violating Article 1 of the OECD Anti-Bribery Convention, shall not be subject to the provisions of this Treaty.
2. A Party may raise the violation of this Article as an objection to jurisdiction in any dispute under this Treaty.
3. The Parties reaffirm their conviction and commitment to eliminate bribery and other forms of corruption in international trade and investment.

Certain aspects of the Model Clause are considered in more detail below.

7.1 "Article 1 of the OECD Anti-Bribery Convention"

The Model Clause does not merely reiterate the content of Article 1 of the OECD Convention,[73] but expressly links itself to the Convention. Alternative provisions to consider for inclusion in the text of an anti-corruption clause are Article 16 of UNCAC, Article 4 of the AU Convention and Article VI(b) of the Inter-American Convention against Corruption.

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72 See §4 above.

73 The key paragraphs of Article 1 of the OECD Convention, headed "The Offence of Bribery of Foreign Public Officials", read as follows:

1. Each Party shall take such measures as may be necessary to establish that it is a criminal offence under its law for any person intentionally to offer, promise or give any undue pecuniary or other advantage, whether directly or through intermediaries, to a foreign public official, for that official or for a third party, in order that the official act or refrain from acting in relation to the performance of official duties, in order to obtain or retain business or other improper advantage in the conduct of international business.
2. Each Party shall take any measures necessary to establish that complicity in, including incitement, aiding and abetting, or authorisation of an act of bribery of a foreign public official shall be a criminal offence. Attempt and conspiracy to bribe a foreign public official shall be criminal offences to the same extent as attempt and conspiracy to bribe a public official of that Party.
3. The offences set out in paragraphs 1 and 2 above are hereinafter referred to as "bribery of a foreign public official".

The inclusion of Article 1 of the OECD Convention means that the tribunal is enabled — and at the same time obligated — to apply internationally used and highly developed provisions regarding bribery of foreign officials, along with definitions of relevant terms and the Convention's own commentary. This is of particular importance in the context of potential weaknesses in the host state's domestic bribery law.

7.2 "in whole or in part"

This formulation makes clear that the treaty's protections would be inapplicable to the whole investment, not just — if such a distinction can be made — to those parts tainted by bribery. For breaches of criminal law, such a consequence seems justified.[74]

7.3 "procured, facilitated, established or operated"

The Model Clause applies to investments "procured, facilitated, established or operated" by bribery. Accordingly, the Clause would be triggered by a breach at any point in the lifespan of an investment, as long as a causal link between the investment and the violation of Article 1 of the OECD Convention is established.

7.4 "objection to jurisdiction"

The Model Clause makes it clear that a finding of bribery nullifies jurisdiction. A look at ICSID jurisprudence reveals, however, that most tribunals have treated corruption allegations at the merits stage of proceedings.[75]

There are two plausible explanations for this observation. Firstly, tribunals may have preferred to avoid deciding a case on corruption arguments where other grounds for rejection of the investor's claim were available at the merits stage. As many arbitrators have a background in commercial or public law rather than criminal law, they might have opted to side-step the issue in cases where the investor would not have succeeded, regardless of the corrupt conduct. Secondly, a failure to make an affirmative finding of jurisdiction could be grounds for annulment of the award, pursuant to Article 52(1)(b) of the ICSID Convention.[76] Without adequate guidelines on how to reach a finding of corruption, arbitrators —

74 For breaches of administrative or civil law, other remedies should be pursued.

75 A survey conducted in preparation for this paper showed that in 15 of 18 awards featuring corruption defences by host states, tribunals looked into the allegation only at the merits stage. Whether the alleged corruption took place during the establishment or operation of an investment did not play a decisive role.

76 Nadakavukaren (2016) at 523.

somewhat justifiably — may have been reluctant to risk rendering a decision dismissing jurisdiction, which later might be open to annulment.

Be that as it may, it is suggested that those commentators are correct who argue that if corruption is seen as a merits issue, tribunals are more likely to compare the host state's perceived blameworthiness to the investor's criminal conduct.[77] As the Model Clause provides arbitrators with a framework to decide on corruption, there is no longer any justification for them to refrain from making affirmative decisions on corruption defences at the jurisdictional stage, where sufficient evidence is available.

8 CONCLUSION

Advocating explicit treaty-based justifications for the operation of a distinct corruption defence in investment arbitration is an important step towards safeguarding the integrity of investment law. The need to emphasise the inclusion of corruption carve-out clauses is supported by two key observations. Firstly, the legal principles that have been applied to corruption defences, namely, the legality principle, transnational public policy and the doctrine of clean hands, are inhibited by considerable uncertainties and shortcomings. In this regard, corruption carve-out clauses could lend much-needed guidance to tribunals. Secondly, and apart from one flagship treaty, parties to investment agreements are yet actually to include the best standard anti-corruption clauses found in various model treaties. The Model Clause presented in §7 above showcases what a bribery provision in future investment treaties could look like. By including such clauses in IIAs, the parties signal their commitment to calling a spade a spade and to confronting corruption in investment.

Interesting points for further research include the extension of carve-out clauses to address money laundering, as well as other forms of corruption, such as trading in influence and diversion of public funds. Furthermore, the obligations and options which arbitrators have after corruption has been alleged in a matter should be studied more thoroughly.

77 Yackee J (2011) "Investment Treaties and Investor Corruption: An Emerging Defence for Host States?" *Legal Studies Research Paper Series Paper No 1181* at 18, available at http://ssrn.com/abstract=1946341 (visited 26 December 2017).