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Corruption in International Commercial Arbitration – Selected Issues

Michael Nueber

I. Introduction

Corruption is increasing worldwide. Parallel to this development the number of arbitrations in business-related disputes is increasing as well.¹⁾ Thus, it might not come as a surprise that arbitration proceedings ever more frequently involve issues of corruption.

Corruption in developing countries amounts to a sum of USD 20 to 40 billion per year, which is approximately 20% to 40% of the worldwide development aid spent yearly.²⁾ According to an official estimate from the World Bank the total damage that the affected states have to cope with due to corrupt conduct of their officials amounts to USD two to three thousand billion a year.³⁾

Developing countries are not the only ones that are affected by corruption. Sophisticated compliance-programs in international companies or rigorous (inter-)national anti-corruption legislation strongly indicate that corruption is an international phenomenon, which is tackled on different levels.⁴⁾

Arbitral tribunals have to deal with corruption cases on a regular basis. Cases of corruption might arise in both commercial and investment arbitrations. This contribution, however, focuses predominantly on corruption in international commercial arbitration. When confronted with corruption in its proceedings, one of the major questions an arbitral tribunal has to answer is how to determine the applicable law according to which it assesses the corrupt conduct. Other relevant and decisive issues concern the right of the arbitral tribunal to investigate into corruption cases *sua sponte*, the standard of proof as well as the burden of proof to be applied. Further, the potential obligation of the arbitral tribunal to report criminal conduct it becomes aware of in the course of its proceedings to state authorities might be an issue as well.⁵⁾

¹⁾ GARY B. BORN, *INTERNATIONAL ARBITRATION: LAW AND PRACTICE* 17 (2012).

²⁾ Michael Hwang & Kevin Lim, *Corruption in Arbitration – Law and Reality*, 1 Asian International Arbitration Journal Vol 8/1 (2012).

³⁾ 52 CorporAID Magazine, 24 (July/August 2014).

⁴⁾ Therefore, the prohibition of corruption forms part of international public policy, see III. E.

⁵⁾ Stephan Balthasar, *Schiedsverfahren im Spannungsfeld zwischen Privatautonomie*

This piece intends to give a brief and non-concluding outline about how to deal with cases of corruption in arbitral proceedings. Its main focus lies with the question of what law(s) an arbitral tribunal has to consider in order to deal with the civil law consequences of corrupt or illegal activity in its proceedings.

II. Selected Issues Regarding Corruption in International Commercial Arbitration

A. Introduction

Dealing with the relationship between international commercial arbitration and corruption has a long tradition among international legal scholars. However, arbitral tribunals have also dealt with corrupt activity in their proceedings for some time now. The most well-known ICC (International Chamber of Commerce)- award concerning this matter dates back to the year 1963. In the ICC Case No. 1110 Judge Lagergren – in his function as sole arbitrator – denied jurisdiction over a dispute about the payment of commissions out of an intermediary agreement which involved elements of bribery.⁶⁾ However, 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.

An arbitral tribunal might have to deal with cases of corruption in several ways. On the one hand, a contract in dispute could have been established through illegal activity, such as bribery. On the other hand, the contract in dispute can promote criminal activity, such as money laundering. In both cases a number of questions surface which should be answered by the arbitral tribunal.

B. Jurisdiction of the Arbitral Tribunal to Deal with Cases of Corruption

For some time, it was not entirely clear whether an arbitral tribunal was the competent venue to decide upon corruption cases. Open questions concerned the arbitrability of cases of corruption as well as the scope of the arbitration clause itself. Whereas the first issue could be resolved rather easily, the scope of the arbitration clause remained an open issue for some time. Currently, it seems to be commonly accepted by arbitral tribunals and legal scholars that an arbitral tribunal has the right to deal with allegations of bribery if one party explicitly premises its claims or defences on them, because it is the core duty of an arbitral tribunal to

und Compliance, in PRIVATAUTONOMIE UND IHRE GRENZEN IM WANDEL (Nueber & Przeczowska & Zwirchmayr ed., February 2015).

⁶⁾ ICC Award No. 1110, 47 Yearbook Commercial Arbitration (1996).

deal with and decide upon all issues submitted by the parties.⁷⁾ Several arbitral awards further corroborate this view. In the ICC Case No. 13384⁸⁾ an intermediary claimed his fee out of the agreement. In turn, the principal objected that the contract promoted illegal activity (bribery). In applying the rule just mentioned, the arbitral tribunal concluded that the dispute is covered by the arbitration agreement since one party explicitly premises his defence on the allegation of corruption.⁹⁾

Furthermore, some legal scholars advocate that arbitral tribunals should even be entitled to deal with corrupt activity that in the end leads to the nullity of the main contract. This view is predominantly based on the *doctrine of separability* which separates the legal status of the arbitration agreement from the main contract.¹⁰⁾ Other legal scholars advocate in favour of the parties' right to terminate the arbitration agreement extraordinarily if corrupt conduct emerges in the course of the arbitration proceedings.¹¹⁾

C. The Right of the Arbitral Tribunal to Investigate into Corruption *sua sponte*

However, even in the light of the above-mentioned arguments, it is more sophisticated to assess whether an arbitral tribunal is entitled to investigate into illegal conduct *sua sponte*. Some legal scholars advocate that an arbitral tribunal, which is investigating into corrupt conduct *sua sponte*, is acting *ultra petita*.¹²⁾

Other scholars, however, argue that an arbitral tribunal has the right to investigate into corrupt activity *sua sponte* since corrupt dealings can have an impact on the enforceability of the claims submitted to the tribunal.¹³⁾ Accordingly, such investigations by the arbitral tribunal should be relevant for the resolution of the dispute of the parties and therefore covered by the arbitration clause.¹⁴⁾ Of course, the prerequisites of due process – e.g. the right to be heard – have to be met by an arbitral tribunal which is investigating into corrupt activity *sua sponte*.¹⁵⁾ Indeed, this opinion seems to be reasonable in the light of the recent increase of corrupt

⁷⁾ Michael Hwang & Kevin Lim, *supra* note 2, at 9.

⁸⁾ Referred to by Stephan Balthasar, *supra* note 5, at footnote 6.

⁹⁾ Stephan Balthasar, *supra* note 5.

¹⁰⁾ GARY B. BORN, INTERNATIONAL COMMERCIAL ARBITRATION: LAW AND PRACTICE 50 (2012); RICHARD KREINDLER, COMPETENCE-COMPETENCE IN THE FACE OF ILLEGALITY IN CONTRACTS AND ARBITRATION AGREEMENTS 237 *et seqq.* (2013), who further (arguably) differs between the various types of nullity.

¹¹⁾ Stephan Balthasar, *supra* note 5.

¹²⁾ NIGEL BLACKABY & CONSTANTINE PARTASIDES & ALAN REDFERN & MARTIN HUNTER, REDFERN AND HUNTER ON INTERNATIONAL ARBITRATION 2.140 (5th ed., 2009).

¹³⁾ Michael Hwang & Kevin Lim, *supra* note 2, at 17; for the duty of an arbitrator to render an enforceable award *see* III.D.

¹⁴⁾ Michael Hwang & Kevin Lim, *supra* note 2, at 17.

¹⁵⁾ Michael Hwang & Kevin Lim, *supra* note 2, at 18.

activity worldwide. Furthermore, this view is supported by the fact that the prohibitions of bribery and money laundering form part of international public policy and must therefore be respected by arbitrators in the context of their duty to render an enforceable award.¹⁶⁾

D. The Burden and Standard of Proof

1. Burden of Proof

Corrupt activity is not easy to prove. A vast number of both commercial and investment arbitration cases deal with questions of proof in regard to corrupt activity.

Sometimes even the allocation of the burden of proof is in question before arbitral tribunals. Without going into much detail, some arbitral tribunals advocated in favour of a complete reverse of the burden of proof and simultaneously let *prima facie* evidence of the party alleging corruption suffice.¹⁷⁾ On the contrary, other scholars argue in favour of an individual solution, which is based on a case-by-case approach. They advocate that the concrete burden of proof predominantly depends on the applicable law and therefore has to be assessed on a case-by-case basis.¹⁸⁾

However, the shifting of the burden of proof from the party alleging corruption to the opposing party is unacceptable in the light of considerations of due process. Of course, corruption cases are highly complicated. Furthermore, by their very nature they have regularly been conducted in secrecy, so that it might seem justified to shift the burden of proof to the responding party. Nevertheless, it makes more sense to remain with the traditional burden of proof according to which the alleging party has to prove his position. In the light of the difficulty to prove allegations of corruption it seems, however, justified to lower the standard of proof.

2. Standard of Proof

Arbitral tribunals, both in commercial and investment cases, apply a high standard of proof¹⁹⁾, when *e.g.* demanding “*clear and convincing evidence*”²⁰⁾ to prove allegations of bribery. Accordingly, tribunals requested parties to prove allegations of bribery “*beyond doubt*”²¹⁾ Furthermore, arbitral tribunals rejected alle-

¹⁶⁾ See in more detail III.E.

¹⁷⁾ ICC Award No. 6497, 71 Yearbook Commercial Arbitration (1999).

¹⁸⁾ Duncan Speller & Kenneth Beale, *Arbitration and bribery: open questions*, CDR Jan 30, 2012.

¹⁹⁾ Stephan Wilske & Todd J. Fox, *Corruption in International Arbitration and Problems with Standards of Proof* 496 in LIBER AMICORUM ERIC BERGSTEN (2011).

²⁰⁾ ICC Award No. 6401, *Westinghouse*.

²¹⁾ ICC Award No. 5622, *Hilmarton*.

gations of bribery which have been qualified as pure “*allusions not supported by evidence and based on suppositions*”²²). Hence, it is not sufficient in order to meet the standard of “*substantive evidence*” that one member of the arbitral tribunal is just suspicious of a party’s conduct.²³) Further prerequisites to prove corrupt activity applied by arbitral tribunals are a “*high degree of probability*”²⁴) or “*irrefutable evidence*”²⁵). In a very recent investment arbitration case, the tribunal concluded that the application of the high standard to prove bribery is not necessary if the facts regarding bribery emerged in the course of the arbitration.²⁶)

The ICSID-tribunal in *EDF v. Romania*²⁷) gives a concise overview of the predominant approach taken by international arbitral tribunals in order to prove corrupt activity:

“*There is a general consensus among international tribunals and commentators regarding the need for a high standard of proof of corruption. The evidence before the Tribunal concerning the alleged solicitation of a bribe is far from being clear and convincing.*”²⁸)

On the contrary, arbitral tribunals have sometimes considered circumstantial evidence sufficient to prove allegations of bribery.²⁹) Legal scholars, however, sometimes argue that arbitrators should not deviate from the “*traditional balance of probabilities standard*”³⁰), as used in state court proceedings in common law jurisdictions. These commentators advocate in favour of a mere preponderance of evidence to prove corrupt activity in arbitration proceedings.³¹)

In fact, it seems it would make sense to lower the standard of proof on a case-by-case basis, like the tribunal in *Metal-Tech v. Uzbekistan*³²) did. It is a fact that cases of corruption are hard to prove. Where it seems *reasonable* and *justified* an arbitral tribunal might lower the standard of proof for the alleging party.³³)

²²) *SPP v. Egypt*, ICSID Case No. ARB/84/3.

²³) ICC Award No. 7047, *Westacre*.

²⁴) ICC Award No. 6497.

²⁵) *African Holding Company of America v. Republic of Congo*, ICSID Case No. ARB/05/21.

²⁶) *Metal Tech v. Uzbekistan*, ICSID Case No. ARB/10/3; see also Deyan Draguiev, *Proving Corruption in Arbitration: Lessons to be learned from Metal-Tech v. Republic of Uzbekistan*, Kluwer Arbitration Blog, Feb 11, 2014.

²⁷) *EDF (Service) Limited v. Romania*, ICSID Case No. ARB/05/13.

²⁸) *EDF (Service) Limited v. Romania*, *supra* note 27.

²⁹) ICC Award No. 3961; ICC Award No. 8891.

³⁰) Speller & Beale, *supra* note 18.

³¹) ABDULHAY SAYED, CORRUPTION IN INTERNATIONAL TRADE AND COMMERCIAL ARBITRATION 104 (2004).

³²) *Metal-Tech v. Uzbekistan*, *supra* note 26.

³³) See also Stephan Wilske & Lars Markert & Laura Bräuninger, *Pertinent Issues in Investment Arbitration against Romania: A Case Study in Challenges and Pitfalls of Investment Disputes in Central and Eastern Europe*, in AUSTRIAN YEARBOOK ON INTERNATIONAL ARBITRATION (Klaussegger et al. eds., 2015).

III. The Applicable Law

A. Introduction

After having established that an arbitral tribunal has jurisdiction to decide upon corrupt activity and how to (best) prove allegations of corruption in arbitration proceedings, in a next step an arbitral tribunal must examine which law(s) are applicable to the corrupt activity.

Since arbitration is first and foremost based on party autonomy, the same applies for the applicable law(s) to corrupt activity. Accordingly, the arbitral tribunal in determining the law(s) applicable to corrupt activity might first consider a parties' choice of law. Furthermore, the *lex arbitri*, the laws of the place of performance, the laws of the potential place(s) of enforcement, principles of international public policy and mandatory rules of law could be of relevance as well.³⁴⁾

B. The Choice of Law

If the parties made a contractual choice of law, questioning about the law applicable to allegations of corruption seems a bit out of place. Accordingly, some legal scholars argue that in the case of a parties' choice of law it should not really matter which law(s) the arbitral tribunal might additionally apply to the corrupt conduct in question.³⁵⁾ While it is true that e.g. bribery of government officials is prohibited by nearly all jurisdictions, there exist, however, further graduations in regard to the scope of the term "corruption". What is permitted in country A and considered as "lobbying" might be prohibited in country B and considered as bribery.

These considerations are most commonly relevant in the context of intermediary agreements. In the course of an intermediary agreement the principal concludes an agreement with the intermediary in the way that the intermediary is obliged to negotiate or obtain a government license or contract within a certain period of time. If the intermediary succeeds, it is common that he receives a certain percentage of the value of the contract he has procured. The intermediary agreement often contains a choice of law as well as an arbitration clause.

C. The Law of the Place of Performance (*lois de police*)

Arbitral tribunals frequently deal with disputes arising out of intermediary agreements. Besides questions of the standard and burden of proof, the law applicable to corrupt activity plays a major role in these proceedings. A question which

³⁴⁾ See Speller & Beale, *supra* note 18.

³⁵⁾ Michael Hwang & Kevin Lim, *supra* note 2, at 37.

often occurs is whether – despite a choice of law clause – the law of the place of performance of the intermediary agreement must be considered by the arbitral tribunal as well. In the typical constellation the parties of an intermediary agreement are from country A and country B and agree to the application of the laws of country C to the contract. In case of dispute, the arbitral tribunal has its seat in country D. However, the services out of the intermediary agreement have been rendered in country E. In addition, the intermediary agreement is illegal under the laws of country E, but not under the laws of countries C and D. How should the arbitral tribunal proceed? Is it the arbitral tribunal's duty to apply the mandatory laws of the place of performance (country E) as well?

In the well-known *Hilmarton* case, a sole-arbitrator had to deal with the situation that several laws had to be considered applicable to the alleged corrupt conduct. Subject to the proceedings was an intermediary agreement between a French company and an English intermediary according to which the English intermediary should procure the conclusion of a construction contract with the Algerian government.³⁶⁾ The intermediary contract was governed by Swiss law and provided for arbitration in Switzerland. Finally, the intermediary claimed for his fees out of the agreement. In turn, the principal denied paying the intermediary's fee because of the illegality of the intermediary agreement under Algerian law. The sole-arbitrator had to decide whether Algerian mandatory provisions (prohibition of intermediary agreements) apply to the allegations of bribery as well and override the parties' choice of law. Under Swiss law, intermediary agreements are absolutely legal. The sole-arbitrator finally decided that the violation of a foreign mandatory provision of law only then violates Swiss law if such violation qualifies as violation of Swiss morality in accordance with Art 20 para 1 of the Swiss *code des obligations*.³⁷⁾ He further confirms that the violation of mandatory Algerian law violates Swiss morality and therefore rejected the claim of the intermediary. Subsequently, the arbitral award was set-aside by the Swiss courts.³⁸⁾

Whether and to what extent foreign mandatory provisions of law could be relevant in order to determine the applicable law in cases of corruption has been intensively discussed among legal scholars. However, the majority of legal scholars request for mandatory provisions of foreign law to be applied by an arbitral tribunal a close link to the dispute at hand. In addition, the values protected by the foreign state's mandatory provisions must at least be compatible with the values protected by the applicable law.³⁹⁾ Furthermore, Swiss courts developed a sophisticated judicature in order to answer under which circumstances foreign mandatory provisions of law can be relevant for proceedings in Switzerland. As a rule

³⁶⁾ ICC Award No. 5622, Yearbook Commercial Arbitration 105 *et seq.* (1994).

³⁷⁾ ABDULHAY SAYED, CORRUPTION IN INTERNATIONAL TRADE AND COMMERCIAL ARBITRATION 238 (2004).

³⁸⁾ Bundesgericht, April 17, 1990, Rev arb 315 (1993).

³⁹⁾ Alfred Siwy, *Mandatory Rules in International Commercial Arbitration*, AUSTRIAN YEARBOOK ON INTERNATIONAL ARBITRATION, 165, 169 (Klausegger et al. eds. 2012); different opinion Richard Kreindler, *supra* note 9, at 170.

thumb, a foreign mandatory provision of law can only then be relevant, if such mandatory provision of law also qualifies as Swiss fundamental legal principle.⁴⁰⁾ Accordingly, as already stated by the sole arbitrator in the *Hilmarton* case, a violation of foreign mandatory provisions of law must simultaneously violate Swiss morality.⁴¹⁾

Legal scholars argue that there is no primary duty of an arbitral tribunal to apply all mandatory provisions of foreign law. Some scholars even want to establish the tribunal's duty to apply mandatory provisions of foreign law only if their violation would offend *international public policy* as well.⁴²⁾ This, however, is a too narrow view, especially in regard to the enforceability of an arbitral award.⁴³⁾ The better approach relies on the *lex contractus* and examines whether the violation of a specific mandatory provision of foreign law violates provisions of the *lex contractus* as well.⁴⁴⁾

In order to determine what provisions can qualify as mandatory provisions of foreign law, an arbitral tribunal might consider a definition given by an international legal instrument. Article 9 para 1 Rome I Regulation on the Applicable Law to Contractual Obligations⁴⁵⁾ therefore stipulates:

“Overriding mandatory provisions are provisions the respect for which is regarded as crucial by a country for safeguarding its public interests, such as its political, social or economic organisation, to such an extent that they are applicable to any situation falling within their scope, irrespective of the law otherwise applicable to the contract under this Regulation.”

Article 9 para 3 of the Rome I Regulation further defines the nature of mandatory rules of the place of performance as rules that render the performance of the contract unlawful. In addition, the court in applying foreign mandatory provisions of law has to consider their nature and purpose as well as the consequences of their application or non-application. Although the Rome I Convention is not directly applicable to arbitration proceedings, it can serve as a guideline for arbitral tribunals to determine the applicable law in their proceedings⁴⁶⁾ and therefore these definitions can be of high value for arbitrators in order to determine what foreign provisions might qualify as mandatory rules and how to apply them properly.

As can be seen from the above, an arbitral tribunal should carefully consider what provisions of the place of performance of an intermediary agreement might

⁴⁰⁾ BGE Apr 17, 1990, ASA Bulletin 253 (1993).

⁴¹⁾ Matthias Scherer, *Beweisfragen bei Korruptionsfällen vor internationalen Schiedsgerichten*, 687 ASA Bulletin 19/4 (2001).

⁴²⁾ Richard Kreindler, *supra* note 9, at 176.

⁴³⁾ See III.D.

⁴⁴⁾ Stephan Balthasar, *supra* note 5.

⁴⁵⁾ Regulation (EC) No. 593/2008, June 17, 2008.

⁴⁶⁾ Michael Nueber, *Nochmals: Schiedsgerichtsbarkeit ist nicht vom Anwendungsbereich der ROM-I Verordnung erfasst*, 186 SchiedsVZ (2014).