State Corruption in ICSID BIT Arbitration: Can it be Estopped?

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ICSID tribunals have refused to hear the merits of investment treaty claims if a corrupt act was involved in contract formation, even where that corruption involved state actors. Consequently, the arbitral system—which was designed to ensure the neutral and apolitical resolution of investment disputes, inadvertently incentivizes states to "promote a corruption scheme in order to establish in advance the [corruption defense]." In an article I wrote, published at 27 American Review of International Arbitration 311, I propose a practical 3-step approach to estopping states who are complicit in the corrupt act from asserting this defense in partial reliance on their own corruption. I discuss the basic arguments supporting this approach below.

1. **Claimants must distinguish the seminal ICC case that recognized the corruption defense in the context of international arbitration.**

In that case, ICC Case 1110 (1963), Judge Lagergren held that a contract between private parties in which they agreed to bribe a public official was non-arbitrable for lack of jurisdiction. Many subsequent tribunals have relied on this opinion as standing for the proposition that a successful corruption defense is a complete bar to an arbitral award. I believe that this is an overbroad interpretation of ICC Case 1110 for several reasons.

First, unlike BIT claims, Case 1110 involved a private contract which was drafted for an invalid purpose. BIT claims will always involve contracts where a government is a party, and will have a legitimate purpose—even where corruption is involved during contract formation. Second, BIT claims lack a key policy justification for completely barring claims subject to a corruption defense. As judge Lagergren pointed out, when corruption creeps into a contract, both parties accept the risk that they cannot recover if the other party breaches. In BIT arbitration, the state is almost always the defending against an investor's claim of breach. Consequently, and unlike in case 1110, when corruption creeps into a contract formed under a BIT, only the private investor accepts the risk that it cannot recover if the state breaches. This disproportionate allocation of risk cuts against the purpose of treaty-based investment arbitration.

2. **Litigants must analogize to existing ICSID jurisprudence recognizing the estoppel doctrine.**

The doctrine of estoppel is no stranger to ICSID tribunals. The *Fraport* tribunal pointed out that a tribunal should "hold a government estopped from raising violations of its own law as a jurisdictional defense when it knowingly overlooked them and endorsed an investment which was not in compliance with its law," and *Desert Line Projects* actually applied the doctrine to a jurisdictional

challenge. The *Waguih* case offers insight into when an ICSID tribunal might find that a state "knowingly overlooked" a material fact relating to the legality of contract formation under a BIT. There, the tribunal estopped Egypt from claiming ignorance of a fact that—if timely raised—would have been a jurisdictional bar to arbitration. Egypt was estopped because the Egyptian judiciary knew of the material fact. In reaching this conclusion, the tribunal stated as a general principle of international law that "the conduct of any State organ shall be considered an act of that State," even when such conduct is illegal or exceeds the authority of the state organ. Claimants could strengthen their argument by demonstrating some *ex post* knowledge of the corrupt act giving rise to a contract and plead some sort of theory of constructive knowledge or ratification. *Ionnis Kardassopoulos v. Georgia* seems to support such an argument. The policy justification for ruling in such a way is also apparent. Bruce Klaw argues compellingly that BITs hold great promise for serving as tools to hold states accountable to avoid and prevent the payment or receipt of bribes.

3. **Claimants must justify a departure from the results in *World Duty Free* and *Metal-Tech*.**

Both *World Duty Free* and *Metal-Tech* are much talked about ICSID decisions. *World Duty Free* was a contract-based claim where the ICSID refused to reach the merits because the contract was formed after bribes were paid to the Kenyan President. Metal-Tech was a BIT claim where the tribunal refused jurisdiction because pass-through "lobbyists" were used to pay bribes to Uzbek officials in order to get and keep the investment contract. To successfully estop a corrupt state's corruption defense, litigants must justify a departure from these results.

Claimants must argue that a facially enforceable contract that was formed after some corrupt acts is not *void ab initio*, but is merely voidable. This echoes the argument above relating to Case 1110, emphasizing the important difference between a contract made for an illegal purpose and a contract whose formation involved an illegal act. *World Duty Free* provides a vehicle for this argument in its heavy reliance on Lord Mustill's principles of avoidance.

Claimants also must argue that the acts of high-ranking government officials or a head of state should, under international law, impute knowledge to the state, as outlined in *Waguih*—even if the acts are is illegal or exceeds the official's authority.

Claimants also must *specifically plead* estoppel. While this may seem like an obvious exhortation, the *World Duty Free* decision dispensed with all of the claims that were plead (which did not include estoppel) and then declined to consider any other grounds for relief.

Finally, when faced with a clear-cut case involving corruption, a claimant must abandon attempts to legitimize the corrupt conduct. *Metal-Tech* serves as a cautionary tale for litigants who choose this path. There, the tribunal implied that it was presented with insufficient evidence of corruption, but — as discussed previously on this blog — relied on its *sua sponte* evidence gathering to find that corruption was present. To avoid this result, a claimant should, in clear cases, admit that the act leading to contract formation was illegal, and in so doing, implicate the defendant state's officials in the act. This places the defendant in the uncomfortable position of either (1) arguing that the act was lawful or (2) conceding that the act was unlawful but attempting to disclaim knowledge or responsibility in order to justify a corruption defense and rebut arguments in favor of estoppel. In this same vein, complainants should not shy away from supporting a high burden of for proving corruption. This is because the more apparent the corruption was, the harder it will likely be for a state to disclaim knowledge or responsibility for participating in or ratifying that act.

Conclusion

Given the right set of facts, and a careful litigation strategy, it seems that the time may have come for an ICSID tribunal to estop a corrupt government from relying on its own corruption as a defense to liability under the terms of a BIT. Such a result would remove the perverse incentive for states to support—or at least deliberately ignore—corruption in the context of international investment contracts and better align the practice and intent of international investment arbitration.

Of course, apportioning an award in a case involving corruption is the topic of an entirely separate conversation, potentially involving a "flexible approach" that includes restitutionary remedies and proprietary remedies….