ADOPTING A 'RANGE OF FACTORS' AND 'DIVISION OF SYSTEMS' APPROACH: ESTABLISHING PRINCIPLES FOR A CONSISTENT STANDARD OF PROOF TO ASSESS ILLEGALITY IN FOREIGN INVESTMENT DISPUTES

Hong-Lin Yu*

INTRODUCTION

The legality requirements underlying investors' claims over treaty protections have increasingly been subject to scrutiny.[1] Frequently, the arbitral tribunal is confronted with a host state's assertion that the investor engaged in corruption or bribery during the lifetime of an investment contract. This includes an array of misconduct such as administrative omissions, violations of the host state's laws, deceit, the misuse of the system of international investment protection, and the violation of good faith or transnational public policy.[2]

The attempt to tackle serious illegality, such as corruption and its impact on the residents of host states, has led the international community's joint efforts to clean up the corruptive practice in foreign investment activities. Kofi Annan has further stated that the 'international community is determined to prevent and control corruption which betrays the public trust, undermines the core values in the community, disrespect for the rule of law.'[3] By doing so, it will increase 'accountability, and transparency in promoting development and making the world a better place for all.'[4]

1 Aloysius Llamzon and Anthony C. Sinclair, 'Investor Wrongdoing in Investment Arbitration: Standards Governing Issues of Corruption, Fraud, Misrepresentation and Other Investor Misconduct'' in Albert Jan van den Berg (ed), *Legitimacy: Myths, Realities*, Challenges, ICCA Congress Series, Volume 18 (Kluwer Law International 2015) 451, 451

2 *Ibid*. 452

3 Kofi Annan, Foreword, United Nations Convention against Corruption (2003), iii, <https://www.unodc.org/documents/brussels/UN_Convention_Against_Corruption.pdf> accessed on 29 December 2019.

4 *Ibid.*

Dr Hong-Lin Yu, Reader in Law, University of Stirling, UK

The international community has introduced two Conventions in particular which combat corruption, the UN Convention against Corruption[5] and the OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions.[6] Around the same time as these were introduced, the Convention on the Fight Against Corruption Involving Officials of the European Communities or Officials of Member States of the European Union,[7] the Council of Europe Civil Law Convention on Corruption,[8] the Council of Europe Criminal Law Convention on Corruption, [9] the Inter-American Convention Against Corruption,[10] and then later the African Union Convention on Preventing and Combating Corruption,[11] were introduced at a regional level to address this issue.

Subsequently, domestic jurisdictions enacted anti-bribery legislation with potential extra-territorial effects on their home state investors. Taking the United Kingdom as an example, the Bribery Act 2010 contains provisions which are backed up with the imposition of domestic investigatory powers and criminal sanctions against bribery of foreign public officials carried out beyond its territory.[12] It requires the prosecution to meet the standard of 'beyond reasonable

[5] Article 1, United Nations Convention against Corruption (2003). <https://www.unodc.org/documents/brussels/UN_Convention_Against_Corruption.pdf> accessed on 29 December 2019.

[6] OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions, signed on 17 December 1997 and in force since 15 February 1999. <http://www.oecd.org/daf/anti-bribery/ConvCombatBribery_ENG.pdf> accessed on 29 December 2019.

[7] Convention on the Fight Against Corruption Involving Officials of the European Communities or Officials of Member States of the European Union (1997) Official Journal C 195 of 25 June 1997, <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=OJ:C:1997:195:TOC> accessed on 29 December 2019

[8] Civil Law Convention on Corruption (1999) ETS No.174 (Date of entry 01/11/2003), < https://www.coe.int/en/web/conventions/full-list/-/conventions/treaty/174> accessed on 29 December 2019

[9] Criminal Law Convention on Corruption (1999) ETS No.173 (Date of entry 01/07/2002), <https://www.coe.int/en/web/conventions/full-list/-/conventions/treaty/173> accessed on 29 December 2019

[10] Inter-American Convention Against Corruption, 29 March 1996, <http://www.oas.org/en/sla/dil/inter_american_treaties_B-58_against_Corruption.asp> accessed on 29 December 2019

[11] African Union Convention on Preventing and Combating Corruption (2003) (Date of Entry 05 August 2006; Date of last signature 26 December 2018), <https://au.int/en/treaties/african-union-convention-preventing-and-combating-corruption> accessed on 29 December 2019.

[12] s. 6(1), UK Bribery Act 2019

doubt' in order to discharge its burden of proof. Apart from the criminal actions, the United Kingdom also allows the Serious Fraud Office to pursue civil actions, applying the standard of the 'balance of probabilities', against those who have been alleged to commit bribery abroad in the context of foreign investment activities. Facing the allegation of corruptive practices in obtaining or maintaining foreign investment projects in arbitration proceedings, international investment tribunals are known for their application of the standard of the 'balance of probabilities' to decide whether any treaty claims tainted by the allegation of corruption fall outside of the treaty protection due to illegality. International tribunals have frequently justified the application of this standard of proof by asserting the private nature of their appointment and the lack of resources available to them.

With the extra-territorial effect of modern anti-bribery legislation, however, there is a real prospect of a foreign investor being made subject to criminal proceedings initiated by the Home State powers which instead apply the standard of 'beyond reasonable doubt' to determine whether the alleged corruptive practices actually took place and the appropriate sanctions against investors. The different standards potentially available to be applied to the same alleged illegality by the international investment tribunals and the domestic criminal courts could see foreign investors losing their treaty protections over the investment if they are to be found guilty of carrying out corruptive practice by the investment arbitral tribunals. Alternatively, with a not guilty verdict being delivered on the same charge by the criminal courts, investors would find no recourse to their already lost treaty protections which would have been available to them had the tribunal applied the same standard and reached the same conclusion as the one delivered by the domestic courts. Likewise, foreign investors may find themselves free from corruptive allegations made by the host state, enjoy treaty protections and receive

compensation paid by the host state, but later be found guilty by the Home state's criminal prosecutors. Further complicating the issue of standard of burden of proof, the claim of illegality can also impact on the admissibility of a claim in foreign investment arbitration. Such a potential conflict has attracted calls for a stricter standard of burden of proof in investment arbitration.

In 2016, the UK Supreme Court was invited to review the 'reliance principle' which had been delivered in *Tinsley v Milligan* back in 1994.[13] In *Patel v. Mirza*,[14] the Supreme Court applied two strands of argument to a defence of illegality in civil actions: 'range of factors' approach considering the policy of the relevant prohibitions, and a division between criminal and civil court systems demanding the different standards of burden of proof on illegality. The purpose of this article is to examine whether 'division of systems' and the 'range of factors approach' as applied in *Patel* can assist the interpretation of the standard of burden of proof and illegality defence arising from foreign investment disputes. To do so, the author will (1) explain the background of illegality in foreign investment law, (2) examine the link between the assertion of the lack of resources and the application of the 'balance of probabilities' standard by the investment tribunals, (3) investigate the nature of proceedings in the domestic context involving the same claims and (4) reflect upon the nature of proceedings upon the tribunal's practice in their application of 'balance of probabilities' in this matter. The article will conclude with a dismissal of the frequently cited ground regarding the tribunal's lack of resources justifying the application of the 'balance of probabilities' standard to illegality claims, but arguing that the application of the 'balance of probabilities' standard in foreign investment

[13] [1994]1 AC 340
[14] *Patel (Respondent) v Mirza (Appellant)* [2016] UKSC 42

arbitration should be based on the type of proceedings where illegality claims were raised, which dictates the application of the relevant standard of burden of proof.

THE ILLEGALITY DEFENCE IN FOREIGN INVESTMENT LAW IN GENERAL

The legality requirement touches on the issue of the admission of claims in foreign investment arbitration. Citing *Tokios Tokelės v. Ukraine*,[15] Polkinghorne and Volkmer[16] argued that the requirement that 'investments be made in compliance with the laws and regulations of the host state is a common requirement in modern BITs'.[17] They also pointed out that the issue of legality of investment covers corruption and bribery in respect of the admission of investments, investment carried out by circumventing the regulations of the host state[18] or admission due to misrepresentation.[19] Unfortunately, the words of 'any legal dispute arising directly out of an investment' provided in Article 25 of the ICSID Convention does not offer a clear guidance on this issue. Few treaties embody a direct or an explicit reference to the legality of an investment.

It is not unusual for investment arbitration tribunals to receive an illegality defence; that is, an allegation of corruptive practice engaged in between the investors and the public officials of the host state. The illegality defence raised by host states varies from serious corruption claims to illegality rooted in administrative errors arising from foreign investment activities.[20] A

[15] *Tokios Tokelės v. Ukraine,* ICSID Case No. ARB/02/18, Decision on Jurisdiction (29 Apr. 2004), < https://www.italaw.com/cases/1099> accessed on 29 December 2019
[16] Michael Polkinghorne and Sven Volkmer, 'The Legality Requirement in Investment Arbitration', (2017) 34(2) Journal of International Arbitration, 149 – 168; 150
[17] *Tokios Tokelės v. Ukraine* (n 15), para 84, < https://www.italaw.com/cases/1099> accessed on 29 December 2019
[18] *Fraport A.G. Frankfurt Airport Services Worldwide v. Republic of the Philippines*, ICSID Case No. ARB/03/25, Award (16 Aug. 2007)
[19] Polkinghorne and Volkmer (n 16), 151
[20] OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions (n 6)

failure to defend the allegation of illegal practice in accessing, obtaining and maintaining investment projects sees foreign investors being denied the protections offered by the multilateral or bilateral investment treaties the Home State is a party to. Such a potential impact on the property rights of the investors deserves a discussion of the standard of burden of proof applied to the issue of legality, as one tribunal pointed out that an economic transaction which may qualify factually and financially as an investment may still fall outside of the tribunal's jurisdiction due to illegality.[21] Furthermore, the difficulty in harnessing an effective system to counteract corruption in international investment arbitration has been stressed by Haugeneder and Liebscher,[22] even though the international community has expressed its intolerance of such a practice.

At one end of the scale of illegality is corruption and the investor's failure 'in accordance with the law of the host state' on the other end of the spectrum. Although corruption may allow foreign investors to operate under the concessionary rights initially, it will increase the costs and the risk of accessing and operating within the market and ultimately run the risk of being denied the treaty protections any legal investment is entitled to. Such a high level of costs and risk can discourage foreign investors from engaging in foreign investment within a particular host state which is renowned for corruptive practice. Equally, this would not be to the benefit of the host state whose main aim is to attract foreign investment into its country to improve or re-energise its economy.

[21] *Fraport A.G. Frankfurt Airport Services Worldwide v. Republic of the Philippines* (n 18) para 306 <http://ita.law.uvic.ca.ezproxy-s2.stir.ac.uk/documents/FraportAward.pdf> accessed on 29 December 2019) para 306.

[22] Florian Haugeneder and Christoph Liebscher, 'Investment Arbitration - Corruption and Investment Arbitration: Substantive Standards and Proof', in Christian Klausegger, Peter Klein, et al. (eds), *Austrian Yearbook on International Arbitration* (Manz'sche Verlags- und Universitätsbuchhandlung 2009) 539, 544, 556, 557

Corruption in international investment is construed around the notion of illegal investment. A main obstacle for those faced with fighting against corruption is the lack of uniform definition of 'corruption' in the international community. This issue is mainly left to the interpretations of domestic jurisdictions; the 'domain réservé' as the *travaux préparatoires* for the United Nations Convention against Corruption[23] pointed out. Subparagraph (b) of the commentary on Article 7 of the Convention states:

> While the definition of corruption must be subject to national law, it should be understood to encompass the commission or omission of an act in the performance of or in connection with one's duties, in response to gifts, promises or incentives demanded or accepted, or the wrongful receipt of these once the act has been committed or omitted. [24]

The concept of 'domain réservé' is applied to illegality at both ends of the scale. Llamzon and Sinclair attempted to define corruption in comparison with other types of wrongdoing falling into the other end the scale of illegality. They highlighted the bilateral nature of corruption, frequently involving intermediaries. This placed corruption in a different form from other types of unilateral acts of wrongdoing.[25] They stated:

> Corruption is used almost uniformly to describe bribery between an investor's employee or intermediary and a public official of the host State. Fraud is often used in a generic sense and can further be subdivided into deceit (i.e., a form of fraud that involves the intent to deceive the host State to the investor's advantage) and to misrepresentation (which need not delve into whether there existed wilful intent to deceive). … the lack of good faith in the making of an investment and two of its manifestations – abuse of process and abuse of rights. International law and various domestic legal systems recognize 'good faith', broadly conceived, and to some extent the provenance of these terms can be traced to customary international law and general principles. They possess commonality in that they are framed in order to avoid misuse of the law.[26]

[23] Adopted by the General Assembly in its resolution 58/4 of 31 October 2003, < https://www.unodc.org/unodc/en/treaties/CAC/travaux-preparatoires.html> accessed on 29 December 2019
[24] *Ibid.* xiv
[25] Llamzon and Sinclair (n 1) 461
[26] *Ibid.* 453

In the case of corruption, it is noted in the definition of 'public officials' set out in Article 8 of the United Nations Convention against Corruption. The provision refers to 'in the domestic law and as applied in the criminal law of the State party in which the person performs that function.'[27] Similar reference to the domestic law is also noted in Article 2(a) of the Convention.[28] On the issue of burden of proof, the Convention requires the state parties to fulfil the burden for establishing the offences claimed which is applicable in the host state's domestic law. With domestic laws addressing corruption or bribery of the foreign public officials designed with extra-territorial effects, questions arise.

To prove illegality and determine whether an investment claim can be admitted, international tribunals are required to apply the appropriate standard of burden of proof. The next section will examine the practice and the debates over the lower standard of burden of proof applied by the international investment tribunals. The section will highlight the reasons given by the international tribunals to justify their decisions to apply the standard of balance of probabilities to an illegality defence which may undermine the investor's treaty protections.

AN 'ILLUSIVE' STANDARD OF BURDEN OF PROOF APPLIED BY INTERNATIONAL INVESTMENT TRIBUNALS

[27] Travaux préparatoires, adopted by the General Assembly in its resolution 58/4 of 31 October 2003, < https://www.unodc.org/unodc/en/treaties/CAC/travaux-preparatoires.html> accessed on 29 December 2019.
[28] Accordingly, "public official" means: (i) any person holding a legislative, executive, administrative or judicial office of a State Party, regardless length and pay (ii) any other person who performs a public function as defined in the domestic law of the State Party and as applied in the pertinent area of law of that State Party; (iii) any other person defined as a "public official" in the domestic law of a State Party.

In the case of ICSID arbitration, investment tribunals are given the procedural power and freedom to 'be the judge of the admissibility of any evidence adduced and of its probative value';[29] whereas the UNCITRAL Arbitration Rules designated such a choice to the parties' agreement dictating the tribunal's duty to determine the applicable law and the standard of burden of proof in order to discharge the evidential burden.[30] However, due to the lack of a direct link to a specific national procedural law or the place of arbitration in investment arbitration, there are inconsistent approaches to the standard of burden of proof in practice. In their applications of the bilateral investment treaty and the principles of public international law to determine treaty protections, arbitrators do not automatically consider the consequences of the applications of different standards of burden of proof and the requirements for meeting them as necessary. Consequently, one may see arbitrators applying no specific standard of proof,[31] a domestic standard under the host state law,[32] or an abstract generalised standard.[33] Kreindler[34] described the standard of proof, or indeed the lack of it, applied by international tribunals as 'illusive'.[35] Nevertheless, he also pointed out that offering precise evidential rules

[29] Rule 34(1), ICSID Arbitration Rule

[30] Article 19(1) of the UNCITRAL Model Law reads: "subject to the provisions of this Law, the parties are free to agree on the procedure to be followed by the arbitral tribunal in conducting the proceedings."

[31] *World Duty Free Company Limited v. The Republic of Kenya* (ICSID Case No. ARB/00/7), Award of 4 October 2006, para. 166 (available at <http://ita.law.uvic.ca.ezproxy-s2.stir.ac.uk/documents/WDFv.KenyaAward.pdf>), *TSA Spectrum de Argentina, S.A. v. Argentine Republic* (ICSID Case No. ARB/05/5), Award of 19 December 2008, para. 175 (available at <http://italaw.com/documents/TSAAwardEng.pdf>), *Inceysa Vallisoletana S.L. v. Republic of El Salvador* (ICSID Case No. ARB/03/26), Award of 2 August 2006, paras. 245 et seq. (available at <http://ita.law.uvic.ca.ezproxy-s2.stir.ac.uk/documents/Inceysa_Vallisoletana_en_001.pdf>), *Wena Hotels Limited v. Arab Republic of Egypt* (ICSID Case No. ARB/98/4), Decision on Annulment of 5 February 2002, 41 International Legal Materials (2002) p. 943, paras. 59 et seq. accessed on 29 December 2019

[32] *SGS Société Generale de Surveillance S.A. v. Islamic Republic of Pakistan* (ICSID Case No. ARB/01/13), Decision on Objections to Jurisdiction of 6 August 2003 (available at <www.italaw.com/sites/default/files/casedocuments/ita0779.pdf>), *Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines* (n 18) para. 399 accessed on 29 December 2019

[33] *EDF (Services) Limited v. Romania* (ICSID Case No. ARB/05/13), Award of 8 October 2009, para 221, available at <www.italaw.com/sites/default/files/case-documents/ita0267.pdf> accessed on 29 December 2019

[34] Richard Kreindler, 'Practice and Procedure Regarding Proof: The Need for More Precision', in Albert Jan Van den Berg (ed), *Legitimacy: Myths, Realities, Challenges, ICCA Congress Series* Volume 18 (Kluwer Law International, 2015)156

[35] The word "illusive" was also used by Jennifer M. Smith and Sara Nadeau-Séguin, 'The Illusive Standard of Proof in International Commercial Arbitration', in Albert Jan van den Berg (ed), *Legitimacy: Myths, Realities, Challenges, ICCA Congress Series* Volume 18 (Kluwer Law International, 2015) 134, 134

in foreign investment arbitration is a 'bold' move for any international tribunal[36] as this will result in 'bifurcated' investment arbitration proceedings because 'such precision will often be lacking.'[37] He further highlighted that, in investment arbitration, 'the tribunal will often provide no texture whatsoever as to the burdens which need to be met to sustain that objection, either in the first round or in a rebuttal round, or then in oral argument.'[38] This includes the annulment proceedings under the ICSID Convention;[39] in particular the expectation of a petition to annul the award is probably present in any event, with or without precision on proof.

However, such an illusive standard can satisfy neither host states nor foreign investors; let alone reflect the increasing institutionalization, globalization and transparency of investment arbitration.[40] Due to the lack of precise evidential rules in investment arbitration, the application of both a higher standard of proof in some cases and a lower standard of proof in others are noted. In the case of corruption, Mourre[41] argued for a lower standard to be applied because of the hidden nature of corruptive activities. von Mehren and Salomon agreed that the degree of proof should be decided on the balance of probabilities and stated that: 'the degree or level of proof that must be achieved in practice in an international arbitration is not capable of precise definition, but it may be safely assumed that it is close to the balance of probabilities.'[42] Hwang and Lim also argued for a lesser degree to be applied because tribunals are only mandated to deal with civil disputes. They wrote: '[a] tribunal does not impose criminal sanctions, which renders it unnecessary and undesirable for it to proceed with the

[36] Kreindler (n 34) 168
[37] *Ibid*.
[38] *Ibid*. 169
[39] *Ibid*. 171
[40] *Ibid*. 158
[41] A. Mourre, 'Arbitration and Criminal Law: Reflections on the Duties of the Arbitrator' (2006) 22 (1) Arbitration International 102, 102 and 103
[42] George M. von Mehren and Claudia Salomon, 'Submitting Evidence in an International Arbitration: The Common Lawyer's Guide' (2003) 20 (3) J. Int'l Arb. 285, 290-291

same degree of caution as a criminal court would apply in ascertaining the facts before it.'[43] They further supported the arguments highlighting the difficulty faced by the tribunals in the lack of resources to carry out an effective criminal investigation. Therefore, 'given the difficulty in proving corruption, a criminal standard of proof would be almost impossible to satisfy and plays directly into the hands of unscrupulous parties, who can simply deny wrongdoing and exploit the high threshold of proof to avoid liability.'[44]

However, a couple of arbitral tribunals[45] have decided to apply a higher burden of proof due to the seriousness of such an allegation. Similar decisions are also noted in *Westinghouse*[46] where the tribunal required a higher standard of proof to be placed on the party alleging the corruptive practice carried out by the investor. The *Westinghouse* tribunal decided that a mere preponderance is not sufficient and that 'clear and convincing evidence'[47] of corruption must be present for the host state to rely on the exemptions. Similarly, the tribunal in *Hilmarton* imposed the Swiss standard of 'beyond reasonable doubt' in order to prove corruption.[48] This approach is supported by Schlaepfer[49] who has argued for a clear standard of proof to be set by the tribunal and maintains that it is the tribunal's duty to ensure that 'the parties understand what is expected from them and, if possible, accept it.' She asserts: 'it is most of the time

[43] Michael Hwang S.C. and Kevin Lim, 'Corruption in Arbitration – Law and Reality' (2012) 8 (1) Asian Int'l Arb. J. 1, 19
[44] *Ibid*.
[45] ICC Award No. 8891, published in JDI 2000, 1076
[46] *Westinghouse Int'l Projects Co., Westinghouse Elec. S.A. and Barns & Roe Enterprises, Inc. v. Nat'l Power Corp. and The Republic of the Philippines*, ICC Case No. 6401, Preliminary Award of 19 December 1991, paras. 31-35
[47] *Westinghouse Int'l Projects Co., Westinghouse Elec. S.A. and Barns & Roe Enterprises, Inc. v. Nat'l Power Corp. and The Republic of the Philippines*, ICC Case No. 6401, Preliminary Award of 19 December 1991, paras. 31-35
[48] *Hilmarton Ltd. v. Omnium de Traitement et de Valorisation S.A.*, ICC Case No. 5622 (1988), para. 23
[49] Anne-Véronique Schlaepfer, 'The Burden of Proof in International Arbitration', in Albert Jan Van den Berg (ed) *Legitimacy: Myths, Realities, Challenges, ICCA Congress Series* Volume 18 Kluwer Law International 2015) 127, 130

counterproductive for arbitral tribunals to impose self-made rules which have an impact on the parties' duty to prove their case, if the latter are not prepared to accept them.'[50]

Such conflicting views were noted by Smith and Nadeau-Séguin in their endorsement of Riddell and Plant's observation on the similar difficulties faced by both tribunals and the International Court of Justice, when they wrote: 'The difficulties have their root once again, in the contrasts of the common and civil legal traditions.'[51] Smith and Nadeau-Séguin further criticised the degree of proof in arbitration as 'a slippery subject'[52] where the fact-finding with the standard of proof is frequently lacking. This has resulted in a confusing and complex understanding of the nature of burden of proof in investment arbitration. As a result, different approaches to the standards of proof are prescribed, invoked and applied by the parties, legal counsels and arbitrators from differing legal backgrounds. Their natural tendency is to draw from their own legal culture,[53] expectations and backgrounds. This observation clearly corresponds with the long suspicion about the influence arbitrators' legal background and training may have on the standard of burden of proof applied.[54]

EXTRA-TERRITORIAL EFFECTS OF DOMESTIC ANTI-CORRUPTION LEGISLATION AND THE STANDARDS OF PROOF

The inconsistent approach in the standard of burden of proof can be further complicated by the concept of domain réservé and the extra-territorial effects contained in anti-bribery legislation. Because of the concept of domain réservé and the diversified legal backgrounds of arbitrators,

50 *Ibid*.
51 Anna Riddell and Brendan Plant, *Evidence Before the International Court of Justice* (BIICL 2009) 123
52 Smith and Nadeau-Séguin (n 35) 135
53 *Ibid*. 136
54 Durward V. Sandifer, *Evidence Before International Tribunals* (1939) 6

legal counsels and parties involved in international investment arbitration, it is essential to investigate how the standards of burden of proof required under domestic anti-bribery legislations would impact on the claim of illegality in foreign investment law.

Following the UN Convention Against Corruption[55] and the OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions, [56] domestic jurisdictions have grown increasingly intolerant of corruptive behaviours by their own nationals within and outwith their own territories. The legislation created by these jurisdictions, including the US Foreign Corrupt Practices Act 1977, China's Criminal Law of the People's Republic of China 1980 (amended in 1997), the Clean Companies Act 2015 in Brazil, the Anti-Bribery Act 2017 in Mexico, …and so on, prescribe an extra-territorial effect over their own nationals even though the illegal acts were carried out outside of their own jurisdictions.

Take the UK Bribery Act as an example: according to s 6(1) of the UK Bribery Act, 'A person ("P") who bribes a foreign public official ("F") is guilty of an offence if P's intention is to influence F in F's capacity as a foreign public official.'[57] As Jones and Taggart put succinctly:

> The offence of bribery is defined in the 2010 Act as a person who offers, promises or gives a financial or other advantage to a foreign official, with or without authority, intending by that to induce or reward the foreign official to perform improperly some relevant function or activity or to reward the official for their heaving done so, or knowing (or believing) that the acceptance of such advantage would per se constitute improper performance of such a function or activities.[58]

[55] The United Nations Convention against Corruption (n 5)
[56] OECD Convention (n 6)
[57] s 6(1), UK Bribery Act 2010.
[58] Timothy h. Jones and Ian Taggart *Criminal Law* (7th edn, W. Green 2018) 315. Also see Terence Anderson, David Schum, and William Twining *Analysis of Evidence* (2nd edn, CUP 2005) 290

The term 'foreign public official'[59] referred to above is defined in the Act as an individual who holds a legislative, administrative or judicial position of any kind,[60] exercising a public function for or on behalf of a country or territory outside the United Kingdom[61] or for any public agency or public enterprise of that country or territory (or subdivision) ,[62] or is an official or agent of a public international organisation.[63] Such descriptions correspond with the officials who are at the heart of the foreign investment framework. Accordingly, a UK investor who bribes a foreign public official of the host state would be caught by the intended extra–territorial effects under the Bribery Act. Consequently, he may be accused of carrying out a criminal offence if the investor's intention is to influence someone in his capacity as a foreign public official.[64] At the same time, such effects may also lead to the application of the Proceeds of Crimes Act 2002[65] and subject the accused to further civil proceedings.

The potential cross-paths between civil and criminal proceedings are now a reality due to the extra-territorial effects on investors who will be subject to different standards of proof for the same allegation at different proceedings. The common understanding is that the standard of proof applied in criminal courts should be 'beyond reasonable doubt', despite it being a phrase which is impossible or at least dangerous to attempt to define.[66] In English law, evidence of a circumstantial nature will not meet the threshold. Accordingly, section 5.1 on the Burden and Standard of Proof in the Crown Court Compendium issued by the English Judicial College

[59] T.H. Jones and M.G.A. Christie *Criminal Law* (6th end W. Green 2012) 295; T.H. Jones and Ian Taggart *Criminal Law* (6th edn, W. Green 2015) 299
[60] s. 6(5)(a), UK Bribery Act 2010
[61] s. 6(5)(b)(i), UK Bribery Act 2010
[62] s. 6(5)(b)(ii), UK Bribery Act 2010
[63] s. 6(5)(c), UK Bribery Act 2010
[64] A foreign public official is defined as someone who holds a legislative, administrative or judicial position of any kind, whether appointed or elected, of a country or territory outside the United Kingdom or exercises a public function for the host state outside the United Kingdom or acted for any public agency or public enterprise of the host state or acted as an official or agent of a public international organisation.
[65] https://www.legislation.gov.uk/ukpga/2002/29/contents
[66] Fraser Davidson, *Evidence* (SULI Thomson & W. Green 2007), para 4.78

requires the prosecution to carry the burden of proving the defendant's guilt. The burden can only be discharged if the evidence allows the jury's conclusion 'making you sure of it. Nothing less than that will do.'[67] Lord Denning pointed out that 'proof beyond reasonable doubt does not mean proof beyond the shadow of a doubt' and 'a case is proven beyond reasonable doubt if the evidence is so strong against a man as to leave only a remote possibility in his favour and 'nothing short of that will suffice.'[68] In Scotland, in terms of criminal matters, Raitt[69] views the standard of proof beyond reasonable doubt as the logical and appropriate threshold to ensure the accused's entitlement to 'all protections and safeguards implicit in art 6 of the ECHR and the right to a fair trial.'[70]

Apart from criminal proceedings, in the cases involving corruption, the UK Serious Fraud Office may elect to pursue the accused in a civil action. In a civil recovery, the application of the UK Proceeds of Crime Act 2002[71] will observe a lower threshold of evidence rule – the balance of probabilities. This would see the 'admission of different types of evidence that would not be admissible at a criminal trial, including inferences from silence, previous behaviour, illegally obtained evidence, abuse of process, and hearsay evidence.'[72] Lord Denning wrote: 'That degree is well settled. It must carry a reasonable degree of probability, but not so high as is required in a criminal case. If the evidence is such that the tribunal can say: 'we think it more probable than not', the burden is discharged, but if the probabilities are

[67] Specimen Directions in Jury Trail, 2.1 <https://keithhotten.files.wordpress.com/2014/05/sdjt.pdf>; The Crown Court Compendium, June 2018 page 19-8 <https://www.judiciary.uk/wp-content/uploads/2018/06/crown-court-compendium-pt1-jury-and-trial-management-and-summing-up-june-2018-1.pdf > accessed on 29 December 2019

[68] *Miller v Minister of Pensions* [1947] 2 All ER 372, 373

[69] Fiona Raitt, *Evidence - Principles, Policy and Practice* (2nd edn W. Green 2013) 101

[70] *Ibid*. Also see *Inland Revenue v Ruffle* 1979 S.C. 371

[71] Part 5, the Proceeds of Crime Act 2002

[72] J Hendry and CP King, How Far Is Too Far? Theorising Non-Conviction-Based Asset Forfeiture, International (2015) 11 (4) Journal of Law in Context, 398, 399; Peter Alldridge, 'Proceeds of crime law since 2003 – two key areas' (2014) Criminal Law Review 171, 185

equal, it is not.'[73] Citing *Byrne v Ross*,[74] Raitt[75] similarly stated that '[d]espite the possibility of criminal penalties, proceedings for breach of interdict are civil proceedings within the meaning of s 1(1) of the Civil Evidence (Scotland) Act 1988 and corroboration is unnecessary.'

In other words, the degree of cogency required for discharging the burden of proof in a civil case is a reasonable probability. The balance of probabilities requires evidence to be established as 'more probable than not', however 'if the probabilities are equal' or 'evenly balanced', the burden is not discharged.[76] It is suggested that proof on a balance of probabilities is a variable standard.[77] However, '[a] civil court, when considering a charge of fraud, will naturally require for itself a higher degree of probability than that which it would require when asking if negligence is established. It does not adopt so high a degree as a criminal court, even when it is considering a charge of a criminal nature, but still it does require a degree of probability which is commensurate with the occasion.'[78] Davidson agreed and stated: 'the party facing such a burden must prove that the odds in favour of the conclusion he is advancing are not worse than 51:49.'[79] Furthermore, an allegation of fraud in a civil court must be proven by a 'preponderance of the evidence' standard[80] or 'a preponderance of probability, but the degree of probability depends on the subject-matter. In proportion as the offence is grave, so ought the proof to be clear.'[81]

[73] *Miller v. Minister of Pensions* (n 68).
[74] 1993 SLT 307
[75] Raitt (n 69) 4.15-4.19
[76] *Ibid.*
[77] Mike Redmayne, 'Standards of Proof in Civil Litigation', (1999) 62(2) The Modern Law Review 167, 168; Fraser Davidson, *Evidence* (2007 SULI), para 4.78
[78] *Bater v Bater* [1951] P. 35, 37
[79] Davidson (n 66) 4.84
[80] Smith and Nadeau-Séguin (n 35) 137
[81] *Blyth v Blyth* [1966] AC 643, 669

In the context of foreign investment arbitration, the standard of burden of proof applied by an arbitral tribunal to an investment allegedly tainted by corruption has its own critical importance.[82] It is a common understanding that the tribunal's decision on the corruptive practice will have a determining factor on the investor's access to substantive treaty protections under a BIT. Unfortunately, most investment treaties, customary international law, and applicable procedural laws contain no provisions on the standard of proof[83] as discussed above. Hence, no uniform standard is established to prove illegality. Agreeing with Redfern,[84] Reed et al.,[85] and Scherer,[86] Cosar stated that 'international arbitration tribunals are not bound to adhere to strict judicial rules of evidence.'[87] She further claimed that such a level of flexibility allowing the tribunal to 'consider all relevant aspects stems from the wide discretionary power tribunals are granted on matters of evidence' and adds that 'such flexibility has been confirmed by awards; tribunals have generally found that claims of corruption may be proven solely by circumstantial evidence'.[88]

The lack of a precise defined standard of proof regarding corruption in foreign investment is a common practice according to Haugeneder and Liebscher.[89] They highlighted that 'the tribunal has "relative factual freedom" in determining which standard of certainty is necessary to prove an allegation of corruption.'[90] Little discussion has been carried out by the tribunals in practice

[82] Haugeneder Liebscher (n 22) 544, 556, 557
[83] Article 24(1) of the UNCITRAL Arbitration Rules mentioned that each party shall have the burden of proving the facts relied on to support his claim or defence. Nevertheless, no threshold is prescribed.
[84] Alan Redfern, 'The Practical Distinction Between the Burden of Proof and the Taking of Evidence – An English Perspective' (1994) 10 Arb. Int'l, 317, 321
[85] Lucy Reed, Jan Paulsson and Nigel Blackaby, *Guide to ICSID Arbitration*, (2nd edn. Kluwer Law International 2011) 142
[86] Matthias Scherer, 'Circumstantial Evidence in Corruption Cases Before International Arbitral Tribunals' (2002) 5 Int'l Arb. L. Rev. 29, 31.
[87] Utku Cosar, 'Claims of Corruption in Investment Treaty Arbitration: Proof, Legal Consequences and Sanctions', in Albert Jan van den Berg (ed), *Legitimacy: Myths, Realities, Challenges*, ICCA Congress Series, Volume18 (Kluwer Law International 2015) 531 - 556; 532
[88] *Ibid*. 534
[89] Haugeneder and Liebscher (n 22) 547
[90] *Ibid*. 547

on the different standards of proof which should be applied to determine the matter of corruption.[91] It has been said that the approach taken by the tribunal is to 'avoid basing a decision solely on the burden and standard of proof and [instead it] will try to establish the relevant facts with reasonable certainty irrespective of the burden and standard of proof.'[92] As a result, the standard of proof has rarely been discussed in arbitral awards as tribunals have used the 'sufficient evidence' adduced by the parties to determine the facts without having to refer to any specific rules of evidence.[93] They have even claimed that it is a widespread approach among the tribunals who hold the 'view that the evidentiary standards in different jurisdictions in practice lead to the same result.'[94] Partasides spoke of 'an adequate evidentiary'.[95] Cosar[96] argued for the practice of 'the balance of probabilities standard' which focuses on 'an overall assessment of the accumulated evidence', rather than 'evidence on its own' as highlighted in *Rompetrol*.[97]

Most literature and the investment tribunals themselves cite the lack of resources and the private nature of their appointment as the grounds for their application of 'proof of balance of probabilities' in the illegality defence. In practice, both tribunals in *Metal Tech*[98] and *Rompetrol*[99] held that 'corruption was established to an extent sufficient to prove a violation.' The standard of the balance of probabilities was 'sufficient' and applied to the generality of the factual issues and the need to adopt 'a more nuanced approach'.[100] Bearing such an approach

[91] *Ibid*. 534
[92] Cosar (n 87) 546
[93] *Ibid.*
[94] *Ibid*.
[95] Constantine Partasides, 'Proving Corruption in International Arbitration: A Balanced Standard for the Real World', (2010) 25 ICSID Review— Foreign Investment Law Journal 47, 60.
[96] Cosar (n 87) 538
[97] *The Rompetrol Group N.V. v. Romania* (ICSID Case No. ARB/06/3), 6 May 2013, para 223; <https://www.italaw.com/cases/920> Accessed on 29 December 2019
[98] *Metal-Tech Ltd. v. Republic of Uzbekistan* para 372. In this award, the tribunal looked at evidence of amount of payments, qualifications of consultants and the relationship with the Government
[99] The *Rompetrol* (n 97) para 186
[100] *Ibid.* para 183

in mind, the tribunal in *Rompetrol* stated that the rule requires the tribunal to undertake an active role in taking a formal note of 'any reasons' given by a party for its failure to comply[101] and to produce evidence in order to cooperate within the dispute resolution process. Accordingly, the view is that a failure on the party's part would prompt an automatic response from the tribunal who should readily draw adverse inferences from such failure; furthermore, 'a tribunal may take particular factual allegations as "proved" for the purpose of the arbitration.'[102]

Nevertheless, the application of 'beyond reasonable doubt' was dismissed by the tribunal in the recent case of *BSG Resources Limited v. Guinea*.[103] Responding to BSGR's claim on unjustified withdrawal[104] of BSGR's investments,[105] Guinea alleged corruptive practice conducted by BSGR. The illegality defence presented by Guinea argued that, in accordance with the law of the host state, 'such corrupt practices nullify the mining titles and the mining agreement held by VGB'[106] because BSGR did not follow the law in reaching a deal with Vale.[107]

In this case, the arbitral tribunal referred to the impossibility of adopting the standard of 'beyond reasonable doubt' and the lack of resources available to the tribunal to investigate the Technical Committee's conclusion in an ICSID arbitration, which indicated that BSGR Guinea

[101] *Ibid.* para 185
[102] *Ibid*. para 184
[103] *BSG Resources Limited v. The Republic of Guinea* ICSID Case No. ARB/14/22 <https://www.italaw.com/sites/default/files/case-documents/italaw7735.pdf> accessed on 29 December 2019
[104] *Ibid.* para 162
[105] This includes the terminations of Zogota Mining Concession, Blocks 1 and 2 Permits and the Base Convention for the investment, paras 146-148
[106] *BSG Resources Limited v. The Republic of Guinea* (n 103) para 136;
[107] *Ibid.* VBG-Vale BSGR Sarl was formed by Vale S.A. (with 51% of shares in BSGR Guernsey) and BSGR (with 51% of shares in BSGR Guernsey)

had allegedly obtained the concessionary rights by corruption and other unlawful means.[108] In a separate LCIA arbitration, although the tribunal had found that BSGR made fraudulent misrepresentations and false statements about the group's shareholding structure and during the due diligence process on Vale's use of the relevant consultants and agents, the tribunal stated that 'limited' inquiry should be conducted into the episodes of allegations of bribery as investigating private corruption by local businessmen and 'the nature of payments is not the tribunal's task assigned by the parties.' The tribunal also highlighted that, without full coercive power, it would be extremely difficult for the tribunal to establish the practice of corruption.[109]

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

> Establishing corruption is, as a matter of fact, difficult. The evidence is usually not readily available. The opposing party will usually not cooperate to establish the facts, even if the production of evidence is ordered by the arbitral tribunal. Putting an additional burden on the party alleging corruption may unduly disadvantage this party and endanger the equality of the parties. Arbitral tribunals applying such higher standards may, however, simply have expressed their view that there are no lower standards for the establishment of corruption, even if corruption is difficult to prove.[110]

They further argued for effective civil remedies which would be sufficient to address public policy concerns and the civil consequences of corruption.

More recently, the Petrobras case seems to suggest that corruption can be cured by a subsequent agreement which fulfils the legality requirement. On 20 May 2019, the District Court Southern

[108] *Ibid.* para 5

[109] Global Arbitration Review <https://www.clearygottlieb.com/-/media/files/award-in-guinean-bribery-dispute-made-public-pdf.pdf> accessed on 29 December 2019. Although the LCIA tribunal concluded that there was insufficient evidence of the alleged bribery, the allegation did spark criminal investigations in the US, Switzerland and Israel where one saw the agent receiving a two-year custodial sentence in the US for obstruction of justice.

[110] Haugeneder and Liebscher (n 22) 547. They also raised the possibility of violation of due process if the alleged corruptive practice was laid down to rest on the basis of diplomatic reasons.

District of Texas Houston Division upheld the award favouring Vantage against Petrobras on the basis of insufficient evidence of bribery and corruption.[111] Being governed by English law, the contract between the parties contains a 'compliance with law' clause[112] that required Vantage to comply with all applicable law, including all applicable law in each of the countries, in connection with the services performed.[113] The contract prescribed English law as the applicable law.[114]

Alongside the allegation made against Vantage on its breach of contract based on the breach of Good Oil and Gas Field Practice[115] Petrobras also asserted misrepresentation, illegal information, and failure in carrying out background checks, which all constituted breaches of non-bribery and non-operational requirements.[116] Petrobras further asserted that illegal payment had been made or offered to its officials with the claimant's knowledge for the purpose of inducing the contract.

Vantage (the claimant) claimed that Petrobras had failed to meet the burden of proof for the assertions of bribery and corruption.[117] The tribunal sided with the claimant[118] and stressed that no convincing evidence showed that Vantage was aware of the bribery[119] and that Petrobras

111 *Vantage Deepwater Company and Vantage Deepwater Drilling, Inc. v. Petrobras America, Inc., Petrobras Venezuela Investments & Services, bv, and Petroleo Brasileiro S.A. —Petrobras* United States District Court Southern District of Texas Houston Division, Civil Action No. 18-cv-2246; <https://globalarbitrationreview.com/article/1193157/petrobras-award-upheld-despite-bribery-claims> accessed on 29 December 2019

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

113 *Vantage Deepwater v. Petrobras America* (n 111) 13

114 *Ibid.* p. 16

115 *Ibid.* p. 50

116 *Ibid.* p. 50, award para 229

117 *Ibid.* p. 54, award para 252

118 *Ibid.* page 53, award para 247

119 *Ibid.* page 59 para 286

had failed to present 'sufficient' evidence to prove bribery and corruption in this case.[120] The tribunal ruled that it did not need to look into these assertions because 'such alleged breaches were waived or ratified by Petrobras entering into the Second Novation and Third Novation.'[121] This is because the tribunal agreed with the claimant's view and ruled that a contract procured by bribery called for a wider category of contracts. Such a category demands contracts to be voidable, not void.[122] The fact that Petrobras's decision to ratify the subsequent Novations means that 'the anti-waiver clauses can be waived by a party's silence and inaction over a lengthy period of time'.[123] The tribunal concluded that without sufficient evidence and the estoppel, Petrobras had failed to discharge its burden of proving its allegation of Vantage's commission of bribery and corruption.[124]

THE ILLEGALITY DEFECT IN CIVIL COURTS - LESSONS FROM *PATEL*

The tribunals in *Vantage v. Petrobras* and *BSG Resources Limited v. Guinea* cited the lack of resources available to investment tribunals to decide a criminal related matter, corruption, in arbitration. This argument was also supported by Reed et al.,[125] Scherer,[126] Cosar,[127] Haugeneder and Liebscher.[128] Partasides[129] spoke of the tribunal's 'relative factual freedom'[130] in determining the standard of certainty which only requires an adequate evidentiary rule.[131] Tribunals are not bound to adhere to strict judicial rules of evidence[132] in their decisions on the

[120] *Ibid.* page 60 para 292
[121] *Ibid.* page 60 para 358
[122] *Ibid.* page 73 para 372
[123] *Ibid.* page 73 para 374
[124] *Ibid.* page 42 para 173
[125] Reed, Paulsson and Blackaby (n 85) 142
[126] Scherer (n 86) 31
[127] Partasides (n 95) 60
[128] Haugeneder and Liebscher (n 22) 547
[129] Partasides (n 95) 60
[130] Haugeneder and Liebscher (n 22) 547
[131] Partasides (n 95) 60.
[132] Cosar, (n 87) 532

factual issues of alleged corruptive practice. This allows tribunals sufficient flexibility and a wide discretionary power to decide the matters of evidence.

The development related *Vantage v. Petrobras and BSG Resources Limited v. Guinea* seems to suggest that the call for a more precise evidence rule has yielded to the principle of finality of awards. Nevertheless, these cases have also demonstrated a real prospect of criminal investigation against the investors in their Home State; particularly with the extra-territorial effects of domestic anti-bribery legislation. Accordingly, as the same issue can be tackled by arbitration, civil or criminal proceedings, it is worth exploring 'effective civil remedies which are sufficient to address public policy concerns and the civil consequences of corruption' as raised by Haugeneder and Liebscher.[133]

Recognising arbitration as a civil dispute resolution mechanism, the standard of 'balance of probabilities' applied by the tribunals corresponds with the practice of the division of responsibility between criminal and civil courts and tribunals, rather than the lack of coercive powers and resources to carry out the investigation. Where the English law applies, the UK Supreme Court ruled that punishment for illegality is a matter for the criminal courts in *Patel v. Mirza.*[134] Lord Toulson articulated his ruling from the perspectives of avoidance of arbitrariness and policy of the statutes because arbitrary, unjust and disproportionate results can only be avoided where there is respect for the integrity of the justice system. The integrity of the justice system can only be achieved by the harmony of the law and its division of responsibility between criminal and civil courts and tribunals. He stated:

> Part of the harmony of the law is its division of responsibility between the criminal and civil courts and tribunals. Punishment for wrongdoing is the responsibility of the

[133] Haugeneder and Liebscher, (n 22) 547. They also raised the possibility of violation of due process if the alleged corruptive practice was laid down to rest on the basis of diplomatic reasons.
[134] *Patel v Mirza* (n 14)

> criminal courts and, in some instances, statutory regulators. It should also be noted that under the Proceeds of Crime Act 2002 the state has wide powers to confiscate proceeds of crime, whether on a conviction or without a conviction. Punishment is not generally the function of the civil courts, which are concerned with determining private rights and obligations. The broad principle is not in doubt that the public interest requires that the civil courts should not undermine the effectiveness of the criminal law; but nor should they impose what would amount in substance to an additional penalty disproportionate to the nature and seriousness of any wrongdoing. … The illegality did not affect the main performance of the contract. Denial of the claim would have given the defendant a very substantial unjust reward. Respect for the integrity of the justice system is not enhanced if it appears to produce results which are arbitrary, unjust or disproportionate.[135]

Agreeing with Gloster LJ,[136] Lord Toulson also spoke of the importance of the policy behind the statutes:

> The essential rationale of the illegality doctrine is that it would be contrary to the public interest to enforce a claim if to do so would be harmful to the integrity of the legal system (or, possibly, certain aspects of public morality, the boundaries of which have never been made entirely clear and which do not arise for consideration in this case). In assessing whether the public interest would be harmed in that way, it is necessary a) to consider the underlying purpose of the prohibition which has been transgressed and whether that purpose will be enhanced by denial of the claim, b) to consider any other relevant public policy on which the denial of the claim may have an impact and c) to consider whether denial of the claim would be a proportionate response to the illegality, bearing in mind that punishment is a matter for the criminal courts. Within that framework, various factors may be relevant, but it would be a mistake to suggest that the court is free to decide a case in an undisciplined way. The public interest is best served by a principled and transparent assessment of the considerations identified, rather by than the application of a formal approach capable of producing results which may appear arbitrary, unjust or disproportionate.[137]

Not only did Lady Hale, Lord Kerr, Lord Wilson and Lord Hodge agree with Lord Toulson's view: it also corresponds with the majority of the results of the Law Commission's consultation on illegal transactions. According to the report, the majority of the consultees agree that criminal sanction is a matter for the criminal courts or regulators and the sanctions 'should not be invoked in determining parties' civil disputes.'[138] The Law Commission pointed out:

> Whether or not punishment can be a legitimate policy underpinning the illegality defence provoked some disagreement amongst the respondents to our two CPs. The large majority thought that punishment was the preserve of the criminal law, and should not be invoked by the civil courts. Certainly it is clear that if punishment were to be regarded as a true rationale, then the rules would need to be carefully applied in order

[135] *Ibid.* [108]
[136] [2014] EWCA Civ 1047 [42]
[137] *Patel v Mirza* (n 14) [120]
[138] *Ibid.* para. 22; The English Law Commission Consultation Paper (No. 189) on the Legality Defence: A Consultative Report (LCCP 189) 2009

> to ensure that any penal effect they produce is proportionate to the unlawful behaviour involved.[139] …
> While we agree with the majority that punishment should not be regarded as an aim underlying the illegality doctrine, the claimant might well regard the successful application of the defence as having exactly this effect.[140]

Following a series of cases[141] which rejected the applications to seek an extension of the 28-day period[142] to challenge the award, the division between proceedings is highlighted in *State A v Party B.*[143] In this case, Sir Michael Burton QC followed the "Colman Guidelines"[144] provided in *Kalmneft*[145] and re-emphased the importance of the finality of award[146] and the different philosophies between arbitration and civil proceedings. He stressed: 'In determining the relative weight that should be attached to discretionary criteria, the starting point must be to take into account the fact that the 1996 Act is founded on a philosophy which differs in important respects from that of the CPR.'[147]

[139] The English Law Commission Consultation Paper (No. 189) on the Legality Defence LCCP 189, para. 2.28
[140] The English Law Commission Consultation Paper No. 189) on the Legality Defence LCCP 189, para 2.29
[141] *PAO Tatneft v Ukraine* [2018] EWHC 1797 (Comm) (Appeal against setting aside of award is currently outstanding.); [2019] 6 WLUK 226 (An extension of time to file acknowledgement of service pending Ukraine's appeal to the Supreme Court was rejected.), *Nestor Maritime v Sea Anchor Shipping, [2012] 2 Lloyd's Rep 144* (as per Eder J), *L Brown & Sons Limited v Crosby Homes (North West) Limited [2008] BLR 366* (as per Akenhead J); *Terna Bahrain Holding Co WLL v Al ShamsiAl Shamsi v Terna Bahrain Holding Co WLL* [2012] EWHC 3283 (Comm) (as per Popplewell J), *L Brown & Sons Ltd v Crosby Homes (North West) Ltd* [2008] EWHC 817 (TCC), *Chantiers de L'Atlantique SA v Gaztransport & Technigaz SAS* [2011] EWHC 3383 (Comm), *S v A [2016] 1 Lloyd's Rep 604, Squibb Group Limited v Pole 2 Pole Scaffolding Limited [2017] EWHC 2394, Telecom of Kosovo JSC v Dardafon.Net LLC [2017] EWHC 1326 (Comm), Daewoo Shipbuilding Ltd v Songa Offshore Equinox Ltd [2018] 1 Lloyd's 443, Broda Agro Trade Ltd v Alfred C Toepfer GmbH [2010] 1 Lloyd's 533*
[142] s70(3), of English Arbitration Act 1996. It reads: 'Any application or appeal must be brought within 28 days of the date of the award or, if there has been any arbitral process of appeal or review, of the date when the applicant or appellant was notified of the result of that process.' s 80(5) provides: 'Where any provision of this Part requires an application or appeal to be made to the court within a specified time, the rules of court relating to the reckoning of periods, the extending or abridging of periods, and the consequences of not taking a step within the period prescribed by the rules, apply in relation to that requirement.'
[143] *State A v. Party B, Party C* [2019] EWHC 799 (Comm)
[144] *Ibid.* [30]
[145] *Aoot Kalmneft v Glencore International AG* [2002] 1 All ER 76
[146] *State A v. Party B, Party C* (n 143) [30]
[147] *Kalmneft* [50] and *State A v. Party B, Party C* (n 143)) [30]

On the enforcement of the *Tatneft* award, [148] the English Commercial Court similarly dismissed the application for an extension in *PAO Tatneft v Ukraine.*[149] Subsequently, the same court was asked to rule on a challenge pursuant to s. 67 of Arbitration Act on the grounds that the tribunal lacked substantive jurisdiction over the claims in *Korea v Dyyani*. [150] In Mr Justice Butcher's decision confirming the Dyyanis' status as investors who conducted investment within the scope of the Korean-Iran BIT, [151] he repeatedly stressed the level of care the English courts should have towards arbitration when deal with the same issue related to the alleged breach of Dyyanis' exclusive right to participate in the process leading to acquisition.[152] He stated: 'given that the arbitral tribunal has considered the same issues, the Court will examine the award with care and interest. If and to the extent that the reasoning is persuasive, then there is no reason why the Court should not be persuaded by it.'[153]

CAN THE 'RANGE OF FACTORS APPROACH' IN *PATEL* ASSIST THE DEBATES OVER THE DEFINITION OF THE LEGALITY REQUIREMENT IN FOREIGN INVESTMENT LAW?

The debate over whether the illegality defence is viewed as a jurisdictional impediment can extend from serious corruption claims to illegality rooted in bureaucratic errors. The legality requirement was discussed in *Fraport*[154] where the illegality was claimed to take place during

[148] *OAO Tatneft v. Ukraine*, PCA Case No. 2008-8, Award on the Merit <https://www.italaw.com/cases/4736> accessed on 29 December 2019. In this case, the tribunal confirmed the breach of the FET standard due to the illegality on amended capital contributions and invalidation in investment.
[149] *PAO Tatneft v Ukraine* (n 141) where Ukraine sought an extension of time to submit its grounds of challenge under the Arbitration Act 1996 until 14 days after the Supreme Court's determination on the issue of state immunity.
[150] *Korea v Dyyani [*2019] EWHC 3580 (Comm)
[151] *Ibid.* [37, 42, 46,47, 48]
[152] *Ibid.* [51]
[153] *Ibid.* [26]
[154] *Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines* (n 18) para. 399

the procurement and subsequent negotiations of the concession agreement. This was against the Philippines Anti-Dummy Law. In this case, the Philippine Constitution and the BOT Law required that the project proponent of a public utility project involving foreign investment must be a Filipino or a corporation registered with the SEC, and be up to at least 60% owned by Filipinos and at most 40% owned by foreign investors. This requirement was also stressed in Article 2 of the Protocol of Agreement to the BIT.[155]

The operation of the investment was allegedly in breach of the Anti-Dummy Law[156] which imposed nationality restrictions on the employment of foreign nationals and members of the Executives and management. The tribunal placed emphasis on legality by referring to 'investment …. accepted in accordance with the respective laws and regulations of either Contracting State' required by Article 1(1) of the BIT between Germany and the Philippines.[157] The tribunal's analysis of the language of both Articles 1 and 2 of the BIT stressed that the compliance with the law of the host state at the 'initiation of the investment' provided a ground for the tribunal's jurisdiction[158] because 'allegations by the host state of violations of its law in the course of the investment, as a justification for state action with respect to the investment, might be a defence to claimed *substantive* violations of the BIT, but could not deprive a tribunal acting under the authority of the BIT of its jurisdiction.'[159]

[155] *Ibid*. para 336
[156] *Ibid.* para 309
[157] *Ibid*. para. 300, 399
[158] *Ibid.* para 345
[159] *Ibid*. para 345

If one takes Lord Toulson's point on the division of proceedings on board, a civil action that raises the defence of illegality may not prevent a claimant from making a claim or seeking a legal remedy simply because he placed his reliance on his own illegality to establish the claim. For instance, the agreement 'failed to materialise or, if it did exist, has failed to sustain itself.'[160] Moving from the '*reliance test*' articulated in *Tinsley v Milligan*,[161] Lord Toulson also pointed out that consideration should be placed on the underlying purpose of the prohibition, public policy and proportionality in terms of denial of the claim based on illegality; in particular, when courts are asked to decide whether allowing such a claim would breach the public interest and damage the integrity of the legal system.[162]

If the policy based 'range of factors approach' emphasised in Gloster LJ and Lord Toulson's decisions is taken up by the tribunals, tribunals would no longer need to struggle to place minor breaches on the scale of illegality. Tribunals would only need to decide whether the policy demanding nationality restriction on the employment of foreign nationals and members of the Executives and management as imposed by the Anti-Dummy Law[163] in *Fraport*[164] is breached, whether allowing recovery for something which was illegal would produce inconsistency and disharmony in the law, and whether the breach would cause damage to the integrity of the legal system. Similarly, the focus on an illegality defence can be placed on serious breaches, such as corruption on the far end of the spectrum. If this approach is adopted then one would not see less significant administrative omissions, such as obtaining required permits for the investment

160 Peter Birks, *An Introduction to the Law of Restitution* (Clarendon Press 1989) 223
161 [1994] 1 AC 340
162 paras, 101 and 120.
163 *Ibid.* para 309
164 *Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines* (n 18) para. 399

discussed in *Mamidoil v Albania*[165] being used as a jurisdictional impediment or as a serious breach of the investment policy undermining the legal system; not to mention the minor errors or 'a failure to observe the bureaucratic or administrative formalities of the domestic law'[166] discussed in *Tokios Tokelės v. Ukraine*[167] and *Desert Line v. Yemen*.[168]

In the absence of clear language in the treaty prescribing legality in the BITs, the tribunal used 'general recognised rules and principles of international law' to be added to its interpretation of the illegality defence. The efforts to remove minor breaches from the illegality defence would allow the tribunal to look for the real intention of the Contracting Parties from the *travaux préparatoires* and the actions taken by both States at the negotiation stage as the *Inceysa* tribunal did.[169] Consequently, tribunal capacity can be extended to those illegal matters viewed as a breach of international public policy, the good faith principle, unjustified enrichment, and profiting from illegal actions as tribunals are mandated to use 'general recognised rules and principles of international law' to add to their interpretation of the illegality defence.

The application of the policy consideration could also tackle the challenge presented by the debates over whether the legality requirements should be dealt with by a tribunal as a jurisdictional or merit issue in international investment arbitration. The challenge is a particularly acute one if the illegality claimed by the host state overlaps with the breach of substantive protections argued by the investors. Paulsson highlighted that the use of

[165] *Mamidoil Jetoil Greek Petroleum Products Societe S.A. v. Republic of* Albania, ICSID Case No. ARB/11/24 < https://www.italaw.com/cases/3003> accessed on 29 December 2019
[166] *Tokios Tokelés v. Ukraine* (n 15) para 297
[167] *Ibid.*
[168] *Desert Line Projects LLC v. The Republic of Yemen*, ICSID Case No. ARB/05/17. Award, para 104 < https://www.italaw.com/sites/default/files/case-documents/ita0248_0.pdf> accessed on 29 December 2019
[169] *Inceysa Vallisoletana* (n 31) paras 192-196

admissibility as a ground for the legality requirement may run the risk of 'an unjustified extension of the scope for challenging awards' on the basis of jurisdiction.[170] The combination of the range of factors approach and the threshold of 'scale of illegality' should be able to address this issue jointly. That is, an obvious fault raised as an illegality defence which undermines the policy behind prohibition can be seen as a jurisdictional issue[171] whereas a minor breach, such as administrative omissions,[172] a failure to observe the bureaucratic formalities of the domestic law,[173] or a delay to the issuance of certificate[174] would not be viewed as an effective illegality defence excluding the investors' access to the substantive provisions and protections. Such an interpretation does not conflict with the tribunals' current decisions on the illegality defence where minor defects proceed into the merit stage.

Equally, this approach could be applied to the host state's acceptance of the tribunal's jurisdiction when, in that State's own appreciation, the illegality of the investment was susceptible of being cured, as that State's legislation offers,[175] corresponding with *Vantage v. Petrobras*.[176] This approach would also support the tribunal's use of good faith in its interpretation of the legality requirement by examining the parties' performance prior to the illegality taking place, such as mutual assumption[177] in *Malicorp*.[178] Both policy consideration and the application of good faith could see the tribunal examine the issue at the second stage,

170 Jan Paulsson, 'Jurisdiction and Admissibility' in G. Aksen et al. eds, *Global Reflections on International Law, Commerce and Dispute Resolution – Liber Amicorum in Honour of Robert Briner* (ICC Publishing 2005) 601
171 *Phoenix Action, Ltd. v. Czech Republic*, ICSID Case No. ARB/06/5, (Award, 15 Apr. 2009), para 104, < https://www.italaw.com/cases/850> accessed on 29 December 2019
172 *Mamidoil* Jetoil *Greek Petroleum Products Societe S.A. v. Republic of* Albania (n 165) para 208, 239
173 *Tokios Tokelés v. Ukraine* (n 15) para 297
174 *Desert Line Projects* (n 168) para 117
175 *Ibid.* paras 117, 492
176 *Vantage Deepwater Company v. Petrobras America, Inc*. (n 111)
177 *Franck Charles Arif v. Republic of Moldova,* ICSID Case No. ARB/11/23, Award (8 Apr. 2013) para 376 where article 1(1) of the France-Moldova BIT expressed provided 'in accordance with the legislation …, on the territory or maritime area of which the investment is made'.
178 *Malicorp Ltd. v. Egypt*, ICSID Case No. ARB/08/18, (Award 7 Feb. 2011) para 118, < https://www.italaw.com/cases/660> accessed on 29 May 2019

'from the standpoint of the merits, in relation to the validity of the investment.'[179] This would not conflict with the tribunal's decision based on the consideration of the principle of autonomy of the arbitration agreement, varied grounds of invalidity of an investment and the factual analysis of the case,[180] and would moreover indeed support it: '[i]n order for an ICSID arbitral tribunal to be able to render an award against a State for breach of obligations concerning the protection of an investment, such investment must be valid. That is why the issue of the possible application of the principle of good faith is then considered as part of the issues on the merits.'[181]

This would also address Paulsson's concerns over opening the door on the grounds for challenge and would no longer view the minor breaches of 'in accordance with the law' prolonging the arbitration proceedings at the preliminary stage as jurisdictional impediments, particularly as the importance of the laws and regulations of the host state is stressed by various commentators. For instance, Francioni highlighted that the extensive penetration of foreign investment guarantees into the areas of national regulation reserved to domestic jurisdiction can only be counter-balanced or met if the investor pursues 'legitimate' public policy objectives.[182] Likewise Dolzer and Shreuer spoke about how foreign investment may reach far into the 'domain réservé' in domestic law against the concerns over the preservation of national sovereignty and the democratic legitimacy of the process of foreign investment.[183] Kriebaum argues for the gravity of violation of domestic regulations to be recognised, setting

[179] *Ibid.* para 117
[180] *Ibid.* para 119
[181] *Ibid.* para 117
[182] Francesco Francioni, 'Access to Justice, Denial of Justice, and International Investment Law' in Pierre-Marie Dupuy, Francesco Francioni and Ernst-Ullrich Petersmann (eds) *Human Rights in International Investment Law and Arbitration*, (OUP 2010) 63, 81
[183] Rudolf Dolzer & Christoph Schreuer, *Principles of International Investment Law* (OUP 2008) 84

a threshold for an infringement to be considered serious enough to invalidate the investment.[184]

Where the BITs fail to provide clarity, the vagueness of 'domain réservé' of the host state laws raised in arbitration proceedings would have to rely on the interpretations given by the tribunal to set the boundaries on the sources and definition of the legality requirement. For instance, the tribunals in the *Inceysa* and *Metal-Tech* cases highlighted the prerequisites of the 'state's consent to be subject to arbitration' and 'defined investment in compliance with local law' before the tribunal would exercise jurisdiction.[185] This corresponds with Cosar's view that the state's consent to arbitration included in the BITs is only conditional and depends on whether the investment disputes fall into the definition of legal investment.[186]

Nevertheless, one is witnessing the host states' increasing attempts to use minor technicalities as a litigation strategy to challenge the tribunal's jurisdiction with an intention to prolong the proceedings and exclude the investors' claims. While the tribunal's decision in the *Malicorp* arbitration was commented on as a 'judicial common sense to deal with issues of jurisdiction at the outset of investment arbitrations'[187] which reflects the practice of the acceptance of legality requirements as a jurisdictional impediment,[188] the policy based approach would allow the jurisdictional impediment caused by a serious breach to stand and impact on the investors carrying out actions against the policy on foreign investment. As the tribunal in *Achmea B.V.*

[184] Ursula Kriebaum, Investment Arbitration – Illegal Investments, (2010) Austrian Yearbook on International Arbitration, 307, 319

[185] *Metal-Tech Ltd. v. The Republic of Uzbekistan* (n 98) para. 373; <https://www.italaw.com/sites/default/files/case-documents/italaw3012.pdf>; *Inceysa Vallisoletana* (n31) para 238

[186] Cosar, (n 87) 540

[187] See the Respondent's submission in *Malicorp Ltd. v. Egypt*, para 98; The tribunals in *Mamidoil v Albania*, *Tokios Tokelės v. Ukraine*[187] and *Desert Line v. Yemen*[187] also confirmed their respective jurisdiction and proceeded to the merit stage of the dispute resolution.

[188] Cosar (n 87) 540

v Slovak Republic[189] correctly pointed out, a distinction between compliance with laws that limit the scope of permissible investments and compliance with each and every law of the host state must be made. It stated: 'it is in the view of the Tribunal entirely reasonable to interpret the terms of Article 1(a) without reading in a requirement that there must be no infraction of the host state's law in the course of the making of the investment, if the investment is to be within the scope of the Treaty protection.'[190] The question is whether such a distinction is necessary since the accepted view is that foreign investments are only protected by the international law or the general principles of law when they are made in accordance with the legislation of the host state.

CONCLUSION

The policy based 'range of factors' approach and the divisions between civil and criminal proceedings articulated by the UK Supreme Court in *Patel v Mirza*[191] can lend a hand to the long-debated issues of a 'scale of legality' and the standard of burden of proof in foreign investment law. Taking the 'division between criminal and civil proceedings' into consideration, foreign investment tribunals are correct in their approach of applying a lesser standard of proof to determine the factual issue of illegality claims. However, the grounds should be rooted in the division of the civil and criminal proceedings, not the lack of coercive power and resources to carry out investigation of the illegality defence, as most literature and

[189] *Achmea B.V. v Slovak Republic*, UNCITRAL, PCA Case No. 2008-13 (formerly Eureko B.V. v. The Slovak Republic). The case concerned the interpretations of the Agreement on Encouragement and Reciprocal Protection of Investments between the Kingdom of the Netherlands and the Czech and Slovak Republic, which was signed on 29 April 1991 and entered into force on 1 October 1992, <https://www.italaw.com/sites/default/files/case-documents/italaw3206.pdf.> accessed on 29 December 2019

[190] *Ibid.* para 172

[191] *Patel v Mirza* (n 14)

practice have claimed. After all, international investment arbitration is a civil dispute resolution mechanism which is to provide an independent, flexible and efficient forum to resolve investment disputes, not setting out to perform criminal investigation. As a form of civil dispute resolution, investment tribunals are not mandated to assume the role of the criminal courts. The requirement of tribunals to examine the evidence in accordance with the standard of beyond reasonable doubt is indeed outwith their remit. Furthermore, *Patel's* range of factors approach does not conflict with most tribunals' decisions on minor breaches. It further supports the application of the 'scale of legality' where the serious corruption claims debar the investors from treaty protections. Without an intention to benefit unlawfully or breach the investment policy of the host state, much lesser bureaucratic, administrative or procedural omissions would allow the tribunals to assume jurisdiction, and resolve the disputes by adopting a new policy oriented approach to settle the debate over the appropriate standard of proof.

Demanding a higher degree of burden of proof to be performed by an investment tribunal which enjoys no coercive powers over witnesses is unreasonable in a civil action setting. Furthermore, a higher degree of burden of proof should be reserved for criminal courts. With the application of a lesser standard of burden of proof being invoked, one may argue that host states would have an easier task to prove serious illegal acts carried out by the investors whose intention is to breach the investment policy or damage the system. In turn, investors may be subject to criminal sanctions or civil remedies pursued by the Home State due to the extra-territorial effects of anti-bribery legislations. However, the division of proceedings must be maintained to ensure that the integrity of the systems is not damaged. One may view this as unfair to investors who are more likely to lose out on the treaty protections and the chance to receive compensation for the loss of investment caused by a host state's expropriations. However, taking Lord Toulson's 'range of factors' approach into consideration, a review of the policy

behind the use of arbitration and the engagement in foreign investment activities may go some way in addressing the concerns over unfairness.

The use of arbitration in foreign investment disputes is to ensure an unbiased dispute resolution system in place to provide the investors a fair chance to put their case forward to an efficient mechanism for an effective as well as a speedy resolution. The policy behind the use of arbitration should not be placing a jurisdictional impediment to every illegality defence raised by host states; in particular, those with minor breaches which are currently dealt with by the investment tribunals at the merit stage. Furthermore, in terms of policy for foreign investment activities, it is understandable that, through the international and national anti-corruption legal instruments, the investment policy behind them is to eliminate the serious scale of breach of legality with corruptive practices. Moreover, it would be beyond comprehension that foreign investment policy is to set up hurdles as jurisdictional impediments at the preliminary stage of investment arbitration proceedings and disallow illegality caused by minor bureaucratic or procedural breaches which do not contravene the relevant investment policy. With the anti-corruption pledge from the international community, the extra–territorial effects of potential criminal sanctions exercised by both host and home states can support the drive towards a clean foreign investment framework which is free from corruption, as foreign investment should be in the first place. This will be beneficial to investors, host states, home states and the international community supporting the economic, social and financial integrity of foreign investment.

Dr Hong-Lin Yu, Reader in Law, University of Stirling, UK