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Charles N. Brower

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President, Afnierican Society of International Law; Partner, White & Case, Washington, D.C. This is a revised version of an Edward Ball Chair Distinguished Lecture presented by the author at the Florida State University College of Law in March 24,1997.

Address

ARBITRATING AGAINST FOREIGN GOVERNMENTS

CHARLES N. BROWER*

I would begin this afternoon by remarking that my presence among you results from the efforts of two persons, memories of whom hopefully are as lively in your consciousness as they are deserving of my personal gratitude. The first is the estimable gentleman who made this lecture and the related chair possible. The second is the incomparable personality and scholar who held that chair until his untimely death last year.

I was never privileged to know Ed Ball myself, but the terms he prescribed for the chair bearing his illustrious name testify uncontradictably to a vision and an understanding of what is needed in the world that are impressive.

Professor Richard B. Lillich was a very good friend over a long period of years, during which we collaborated joyfully, and I dare say effectively, in the constant struggle to achieve the greatest possible application of the rule of law throughout the world. It was he who invited me here. It is my great fondness for him and my deep respect for his memory that have secured my performance this afternoon of the obligation undertaken at his behest.

This great university truly has been blessed by the attentions of these two giants in their respective fields. I am honored to be among you this afternoon and will do my humble best to fulfill their expectations.

I am given to understand that I was invited here particularly due to my status as a member of the international judiciary in order to acquaint you in some way with that special perspective. It is with pleasure that I shall endeavor to do so. I take as my subject "Special Aspects of International Arbitration Involving Sovereigns."

To be absolutely precise, I will be discussing international arbitration as the mandatory and binding default method for resolving legal differences between a state on the one side and a private business entity on the other side, agreed in advance of their dispute.

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Much of what I will have to say is valid also, however, with respect to arbitrations conducted pursuant to arrangements made by the parties after the eruption of the dispute that divides them.

I will first outline for you what it is, in fact, that the parties have agreed when they decide to engage in such arbitration. I will then detail the phenomena that I regard as necessarily resulting from such agreement. Finally, I will discuss the rather interesting consequences that ensue.

What have a state and a business entity which is a national of another state, in fact, undertaken when they agreed to international arbitration of their dispute? Clearly, they have agreed there must be in place a mechanism for resolving their dispute which the parties are under a legal compulsion to employ and which is one that will produce a resolution legally binding on them.

Second, they have agreed that this mandatory means of binding dispute resolution should not be the national court system of either party to the dispute and that, likewise, it should not be the national court system of any third country.

Third, the disputing state and its foreign national adversary have mutually concluded that what we know as international arbitration provides the acceptable, fair, and neutral alternative to national court systems.

Fourth, it is more than likely that the parties also will have selected a set of arbitration rules that affords each of them a role in the selection of the tribunal that is to apply the law to the facts of their dispute and issue a binding award. They will have done so because involvement of the parties in the process of selecting the tribunal is thought to increase the parties' confidence in the fairness of the actual proceedings and thus of the ultimate result.

Fifth, it is very possible that the parties, in addition to having opted for international arbitration, will have selected as the substantive governing law a jurisprudential corpus other than the national law of any country or have prescribed as governing law a combination of some national body of law and another body of law to supplement or modify it. Some examples are as follows:

- Article 42(1) of the Convention on the Settlement of Investment Disputes between States and Nationals of Other States, which provides that in the absence of any other agreement on the matter, "the Tribunal shall apply the law of the Contracting State party to the dispute (including its rules on the conflict of

laws) and such rules of international law as may be applicable";[1]

- the 1955 Libyan Petroleum Law (the law applicable to oil concession agreements in that country, some of which are still in effect) providing that the applicable law is the law of Libya and "such rules and principles of international law as may be relevant but only to the extent that such rules and principles are not inconsistent with and do not conflict with the laws of Libya";[2]

- *lex mercatoria,* a concept reflected, *inter alia,* in Article 13(5) of the Rules of Conciliation and Arbitration of the International Chamber of Commerce, providing that "[i]n all cases the arbitrator shall take account of the provisions of the contract and the relevant trade usages";[3]

- the UNIDROIT Principles of International Commercial Contracts, a compendium of principles promulgated in 1994 by the International Institute for the Unification of Private Law and now sometimes adopted by name as the governing law in contracts;[4]

- the Declaration Concerning the Settlement of Claims between Iran and the United States establishing the Iran-United States Claims Tribunal and providing that the "Tribunal shall decide all cases on the basis of respect for law, applying such choice of law rules and principles of commercial and international law as the Tribunal determines to be applicable, taking into account relevant usages of the trade, contract provisions and changed circumstances."[5]

Thus it is clear that an important aspect of international arbitration on which the parties often endeavor to agree is that the substantive law governing resolution of their dispute should be a body of principles that might be deemed by a national court system to be too imprecise to be capable of application. In doing so, the parties

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1. Convention on the Settlement of Investment Disputes Between States and Nationals of Other States, Mar. 18. 1965, 17 U.S.T. 1270, 575 U.N.T.S. 159 [hereinafter ICSID Convention].

2. Petroleum Law of 1955 cl. 28(7), *as amended by* Royal Decree of July 1961 (Libya), *quoted in* Robert B. von Mehren & P. Nicholas Kourides, *International Arbitrations Between States and Foreign Private Parties: The Libyan Nationalization Cases,* 75 AM. J. INT'L L. 476, 482 n.22 (1981).

3. INTERNATIONAL CHAMBER OF COMMERCE NEW RULES OF CONCILIATION AND ARBITRATION art. 13(5) (1988), *reprinted in* 28 I.L.M. 231, 240.

4. INTERNATIONAL INSTITUTE FOR THE UNIFICATION OF PRIVATE LAW (UNIDROIT) PRINCIPLES OF INTERNATIONAL COMMERCIAL CONTRACTS (1994).

5. *See* Declaration of the Government of the Democratic and Popular Republic of Algeria Concerning the Settlement of Claims by the Government of the United States of America and the Government of the Islamic Republic of Iran (Claims Settlement Declaration) art. V, *reprinted in* 1 Iran-U.S. Cl. Trib. Rep. 9, 11 (1981).

clearly hope to afford the tribunal that is to decide their dispute a certain enhanced freedom to achieve a just result while, nonetheless, applying law. It is, if you will, another dimension of the "neutrality" that is essential to their ability to agree.

These, then, are the outlines of what an arbitrating state and the foreign commercial party with which it is contending actually will have agreed upon when they decide to resort to international arbitration. Let us now look at the phenomena that result when a dispute actually arises between the parties.

In the usual case, a tribunal will be formed of three members, most likely of three different nationalities. Although it could include co-nationals of the parties, it is noteworthy that co-nationals often are excluded from consideration. The tribunal may even include one member who is qualified in the governing national law that has been chosen (if, and to the extent, one has been chosen). The circumstance in which this situation arises almost inevitably is one in which the law of the host state has been selected as the governing law and the host state appoints as arbitrator a national of that state (or a national of a closely related state) who is qualified in the law of the state. I personally have had this experience in cases against Algeria, Iran, and Libya.[6]

A tribunal of three arbitrators of different nationalities necessarily will represent diverse legal systems and traditions. Such tribunals, therefore, often combine lawyers of common law background with those from civil law countries. In some cases, Islamic law or even the traditional or customary law of less developed societies will be combined with Western or European traditions more familiar to this audience.

Where a sovereign defendant is involved in an arbitration, political considerations alone may lead it to question, after the fact, whether or not it indeed did surrender its sovereign immunity by submitting to arbitration and, thus, search for a basis on which to attack the jurisdiction of the tribunal. In more than a few cases, sovereign states have chosen to make their jurisdictional point very boldly by refusing to participate at all in the proceedings or, which is worse, by determinedly disrupting the proceedings. The most conventional means of doing this is for the sovereign party to fail to appoint an arbitrator and to refuse to appear in the proceedings.

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6. In such cases, it is imperative that the claimant engage an expert in the law of that country, so that the arbitrator appointed by the claimant and the president or chairman of the tribunal will have some objective basis upon which to differ with the arbitrator appointed by the host state as to what in fact the governing law provides, should they be so inclined.

However, neither one of these steps will bring the process to a halt. All modern sets of arbitration rules provide for the appointment of missing arbitrators by an "appointing authority," normally a designated institution but sometimes even a particular individual. Modern sets of arbitral rules also fully empower a tribunal to proceed to a conclusion and render an award even in the total absence of any participation by the defendant.

The more sophisticated operators among recalcitrant state defendants in international arbitral proceedings will find more subtle means of abusing the process. They might, for example, appoint as arbitrator someone who is not truly independent and impartial as required by all modern sets of arbitral rules. It may be difficult for the claimant to satisfy the appointing authority, which must pass on the issue, that the appointee is so clearly disqualified that he should be denied office or removed from it. Also, a claimant sometimes will prefer to leave such an arbitrator in place, calculating that retention of the dubious appointee will be to the net advantage of the claimant in that the appointee's apparent bias will preclude him from being at all persuasive with the other members of the tribunal. In extreme cases, however, a clearly unsuitable arbitrator designated by a state may aggressively manipulate the proceedings by absenting himself at critical points on some pretext or other, only to reappear and insist on restarting proceedings. I already have alluded to the possibility that he may misinterpret the law to his colleagues if the applicable law is that of his state.

In extreme cases—and I have known such cases in my function as a Judge of the Iran-United States Claims Tribunal—such antics on the part of a state-appointed arbitrator may be combined with carefully timed nonappearances and subsequent problematic reappearances of the state defendant itself. All of these difficulties can be overcome but necessarily only at a cost. However, they may not be overcome if the tribunal president or chairman is not both knowledgeable and determined.

I wish to be careful not to overstate the frequency of occurrence of the kind of events I have been describing. Such tactics are far from unknown, however, and they simply represent the most extreme manifestations of what is likely to be present in some degree in an international arbitration in which a government or important state entity is the defendant. These tactics, of course, are less likely to be encountered in a case of a simple sale of ordinary goods to a state-owned trading enterprise than in a case involving the premature termination of a concession granting rights for the exploitation of the principal natural resource of the host country.

Having first set the stage and then provided both play and players, let me now acquaint you with how the drama may unfold. The points I will now cover are ones about which nonstate parties, i.e., foreign investors, frequently complain but which, I submit, always must be viewed in light of the alternative to international arbitration. Put another way, when viewing each of the anomalies with which I will now acquaint you, and after exclaiming the inevitable "But how can this be?!," you should ask yourself, "Is this not still better than being subjected to domestic judicial proceedings in the courts of the host country?" It is fundamental to know, and to understand, that awards issued in international arbitrations which I am discussing are widely subject to compulsory enforcement by national courts under various conventions,[7] although execution on such awards normally is subject to national rules regarding sovereign immunity.[8]

First of all, at the procedural level, the clash of common law and civil law traditions will produce curious hybrid arrangements regarding the taking of evidence. For example, the civil law tradition tends to disqualify from testifying any person having an interest or involvement in the dispute. Thus, in common law countries officers, directors, employees, and agents of corporate parties testify under oath, subject to rigorous cross-examination for bias; however, in civil law jurisdictions, they may not be permitted to testify at all because of presumed bias. This is what I, only partially tongue-in-cheek, refer to as the principle of disqualifying from testifying anyone who might actually know something about the subject matter of the dispute. At the Iran-United States Claims Tribunal, this cultural conflict was adjusted by allowing officers, directors, employees, and agents of corporate parties to appear at hearings on the merits and make statements (not under oath and not subject to any other "solemn declaration") as "party representatives" rather than as "witnesses," the latter status being reserved to presumptively disinterested persons. I leave it to your imagination to determine what in fact makes the difference.

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7. *See* Convention on the Recognition and Enforcement of Foreign Arbitral Awards, June 10, 1958, art. III, 21 U.S.T. 2517, 2519, 330 U.N.T.S. 38, 40 ("Each Contracting State shall recognize arbitral awards as binding and enforce them in accordance with the rules of procedure of the territory where the award is relied upon . . . .") [hereinafter New York Convention]; ICSID Convention, *supra* note 1, art. 54(1), 17 U.S.T. at 1291, 575 U.N.T.S. at 194 ("Each Contracting State shall recognize an award pursuant to this Convention as binding and enforce the pecuniary obligations imposed by that award within its territories as if it were a final judgment of a court in that State.").

8. *See* New York Convention, *supra* note 7, art. III, 21 U.S.T. at 2519, 330 U.N.T.S. at 40; ICSID Convention, *supra* note 1, art. 54(3), 17 U.S.T. at 1292, 575 U.N.T.S. at 194.

I should add here that regardless of the procedures, the difference in cultural attitudes towards the concept of "the truth," which is all-important in Western judicial proceedings, has raised in my mind fundamental doubts about witness testimony in particular proceedings. I have had the highly unpleasant experience of having to completely withdraw an Asian witness, some hours after I had put him on the stand to testify on behalf of a client in an arbitration in which I was acting as counsel. Because he was testifying in complete contradiction to what he had told me previously over a period of many months, by my lights, he was lying. I eventually came to understand that despite his Western experience—he was a graduate of an Ivy League university particularly prominent in his chosen field—his conduct was in accordance with the dominant personal imperative in his society, namely harmony with one's surroundings, truth being further down the scale of social values. I think I never did satisfy myself entirely as to whether he had told me "the true story" in the months before the hearing or, in fact, was telling it at the hearing on the merits.

In another case, a university-educated Muslim who was a top executive of the company I was representing, one of the most important in its field in his country, quite matter-of-factly explained to me that there was a significant difference between what he would be able to say in an arbitration hearing on the merits if he were required to swear an oath on the Holy Koran and what he would be free to say were that prelude omitted.

Admittedly, these two examples are particularly graphic and compelling. They are reflective, however, of the broader reality that international arbitration, a concept that is predominantly Western in form, cannot always proceed just as we suppose it should.

Another surprise is posed on occasion in international arbitration by the actual interpretation of the applicable law. Where a somewhat flexible or even amorphous body of legal principles is agreed to constitute the governing law, the parties necessarily have contemplated the possibility that interpretations of that law may be made that might appear to some to be "unusual." In addition, the differing legal and cultural backgrounds of the respective arbitrators may lead them to take entirely disparate views of the legal consequences of a set of undisputed facts. Then, too, interpretation of the applicable law may be complicated by a sharp clash of expert testimony or by a state-appointed arbitrator who is qualified in the applicable law and is biased.

Another consequence frequently encountered is that the arbitral proceedings will be quite formal and interspersed with a variety of

procedural complications, even including unjustified challenges to the independence or impartiality of particular arbitrators, which challenges must be considered and decided by the appointing authority.

Turning to the decisional process itself, you will find the tribunal doing a number of things which may be very frustrating to the claimant but in the end are designed by the tribunal to insure that the award it ultimately renders is, in fact, accepted as legitimate by the parties and can be enforced by any relevant national court. Thus you will see, for example, a "bending over backwards" by the tribunal as it deems necessary in order not only to accord due process to the state party but also to be seen undeniably to accord such due process. In this sense, in accordance with the Orwellian precept, states are "more equal" than other parties. Therefore, if the state defendant does not appear, is poorly represented, or even is not represented by counsel at all, the members of the tribunal will tend to act as if they were the lawyers for that state party in order to be sure that the claimant's case is fully tested.

Similarly, the nonstate party, even where the state is decently represented, is likely to feel that it is being held to a higher standard of proof than the state defendant. It has been my observation over a number of years that the nonstate investor is held to a high standard in direct proportion to its presumed sophistication and the presumed competence of its counsel. That is to say that since much is expected of top-class Western counsel in general, more will be expected of such counsel in international arbitrations with foreign states than will be expected from others as to which a less a exalted standard of performance is presumed.

In addition, to the extent a state party may give evidence of reluctance to participate in the proceedings, the tribunal is likely to extend itself to the end that the state is persuaded to remain fully active in the proceedings and thereby give them maximum legitimacy. For these reasons, a tribunal may grant objectively unwarranted extensions of time or permit the filing of additional memorials, even following the expiration of a "firm" deadline.

Similarly, at the Iran-United States Claims Tribunal, for example, the tribunal majority notoriously took several actions clearly designed to mollify an irate Iran. For five years following the establishment of the tribunal, it did not apply the expropriation provisions of the bilateral Treaty of Amity, Economic Relations and

Consular Rights[9] concluded between the United States and Iran in the time of the Shah because Iran strongly took the position that the treaty was no longer in force. The tribunal found instead that principles of customary international law had the same effect as the treaty and then relied on that customary law instead. Only after the lapse of five years and, I suspect, taking some soundings among the Iranian judges, did the tribunal venture finally invoke the Treaty of Amity. All of this took place notwithstanding the fact that the International Court of Justice in 1980 had expressly found the Treaty of Amity to have been in force at the time of the hostage crisis.[10] It is an interesting footnote to history that Iran itself subsequently relied on the same Treaty of Amity as the jurisdictional basis for proceedings that it commenced and that are now in progress at the International Court of Justice, in which Iran has sought damages from the United States for the destruction of two oil platforms offshore of Iran in the 1980s.[11]

The tribunal also avoided for many years holding hearings on its "dual national cases," cases in which former Iranians who had become United States citizens but still were regarded by Iran as nationals of that country brought claims against Iran. The tribunal did so due to the intense political furor on the Iranian side over the notion that Iran could be sued internationally by persons it regarded as its own nationals.

For the same reasons, the tribunal, through various juridical devices, has consistently avoided any finding that Iran has acted "unlawfully." For more than fifteen years, it has assiduously avoided finding that Iran violated the Articles of the International Monetary Fund, that any one of its various expropriations of American property was "unlawful" (although the tribunal has required that all such expropriations be compensated) or that any of the hundreds of American citizens who claimed they were "wrongfully expelled" from Iran were in fact subjects of a wrongful act.

Finally, when an award is issued against a sovereign state which has been and remains recalcitrant, one can expect such a state to utilize every means available to attack the award. However, this is no more than can happen in any domestic judicial proceeding although, like anything else, it can be carried pretty far. Perhaps the

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9. Treaty of Amity, Economic Relations and Consular Rights, Aug. 15, 1955, U.S.-Iran, 8 U.S.T. 899, 284 U.N.T.S. 93.

10. *See* United States Diplomatic and Consular Staff in Tehran (U.S. v. Iran), 1980 I.C.J. 3 (May 24).

11. *See* Oil Platforms (Iran v. U.S.), 1994 I.C.J. 3 (Jan. 19).

most memorable case in this regard involved a scheme to develop a tourist complex around the base of the Egyptian pyramids at Giza.

When political opposition to the project arose, the contract concluded by the investor was terminated. The foreign investor commenced arbitral proceedings under the auspices of the International Chamber of Commerce against the Egyptian government and the Egyptian state authority with which the investor principally had dealt. Eventually, a distinguished panel of arbitrators issued a monetary award against the Egyptian government but excused the Egyptian state authority on the ground of *force majeure*.[12]

The Egyptian government successfully achieved annulment of the award by the highest courts of France, where the arbitration had been held, on the ground that the government of Egypt was not, in fact, a party to the contract containing the arbitration clause on which the arbitration was based and that the arbitral tribunal, therefore, had exceeded its jurisdiction.[13] Thereafter, the investor concluded that a certain provision of the Egyptian foreign investment legislation constituted consent by the Egyptian government to arbitration of investment disputes at the World Bank's International Centre for Settlement of Investment Disputes ("ICSID") and commenced a second proceeding there. After another furious jurisdictional battle, the investor prevailed and eventually received a substantial monetary award.[14] After Egypt had commenced annulment proceedings, a settlement was finally achieved.

In several other notorious cases, all at the ICSID, disputing parties completed one arbitration, went through an annulment proceeding, lived through a second arbitration and, finally, another annulment proceeding before either settlement was reached or the matter was otherwise concluded.[15]

After reciting these cases, I again wish to be cautious. These are the most notorious and extreme cases which certainly do not

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12. *See* Case YD/AS 3493/1983 (Southern Pac. Properties (Middle E.), Ltd. v. Egypt) (ICC Ct. Arb. Mar. 11, 1983), *reprinted in* 22 I.L.M. 752.

13. *See* Judgment of July 12, 1984 (Egypt v. Southern Pac. Properties (Middle E.), Ltd.), Cour d'appel de Paris, 1re Ch. suppl., 1986 REVUE DE L'ARBITRAGE [REV. ARB.] 75, *translated in* 23 I.L.M. 1049, *aff'd*, Judgment of Jan. 6, 1987, Cass. civ. 1re, 1987 REV. ARB. 469, *translated in* 26 I.L.M. 1004.

14. *See* Southern Pac. Properties (Middle E.), Ltd. v. Egypt, ARB/84/3, ICSID Doc. 16/Rev.4 (July 31, 1995).

15. *See, e.g.*, Amco Asia Corp. v. Indonesia, ARB/81/1, ICSID Doc. 16/Rev. 4 (July 31, 1995) (involving dispute between an American investor and government of Indonesia over control of a hotel in Jakarta, Indonesia); Klöckner Industrie-Anlagen GmbH v. Cameroon, ARB/81/2, ICSID Doc. 16/Rev.4 (July 31, 1995) (involving dispute between a German investor and government of Cameroon over a joint venture agreement for construction and operation of a fertilizer factory in Cameroon).

represent the mean. They give an indication, however, of what can occur and of the heights to which political concerns may drive a sovereign defendant (as these concerns, indeed, may drive particular litigants in any system).

In now concluding my discourse on this subject, I return to the point I made just before citing this litany of potential travails and tribulations. Let me now put it differently: If international arbitration with sovereigns is a substitute for litigation in national courts that provides effective relief, is it not reasonable that certain attributes of national judicial proceedings be present, such as formality and detail of procedure and the availability at least of limited possibilities for review of resulting awards? Stated more broadly, having in mind the goal of an effectively enforceable award against a foreign sovereign, which then also is paid, are not the less edifying aspects of international arbitration with such sovereigns in the end acceptable?

Let me approach this still differently. I firmly believe that, by and large, the results of international arbitrations are as just as those achieved in our preferred Western national court systems. If that is the case—and I firmly believe that it is the case—should we not accept the otherwise objectionable anomalies of international arbitration as being worth the resultant continued willingness of sovereigns to submit to binding arbitration producing effectively enforceable awards? Clearly, I believe, the answer is yes.

Let me finish on a personal note. In the process, as I see it, of participating in an effective international arbitral system of justice, I have had the privilege to experience not only severe intellectual and political challenges but also great joy and satisfaction. Perhaps it is the politics that make it especially interesting. I have witnessed everything from a premeditated and very nasty physical assault on a septuagenarian Swedish colleague at the Iran-United States Claims Tribunal by two of our much younger and very fervent revolutionary Iranian colleagues, to the Prime Minister of an important Middle Eastern country putting the finishing touches on the happy settlement of a festering investment dispute. I hope that this afternoon you not only have learned something about particular aspects of international arbitration with sovereigns but also have been caught up for a moment in the excitement of the process.