

# Kluwer Arbitration Blog

## For Whom The Bell Tolls: Is The Red-Flags Standard's Application Enough To Prove Corruption In International Arbitration?

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The *Rutas de Lima v. Metropolitan Municipality of Lima* case shows how arbitral tribunals deal with corruption allegations in disputes related to government contracts. The tribunal, chaired by current ICC International Court of Arbitration President, Alexis Mourre, issued its [Award](#) this May, which came to light when the Metropolitan Municipality of Lima (the "Municipality") [requested](#) and [sustained](#) an annulment application before the US District Court for the District of Columbia this August.

The dispute revolves around a commercial case where the claimant requested compensation for uncollected tolls under a toll concession agreement, which provided for compensation mechanisms that the respondent allegedly failed to apply. The Municipality argued that the concession agreement was null and void due to the presence of corruption, among other grounds. Ultimately the Tribunal held that there were *insufficient* red flags *directly* related to the concession agreement and rejected the corruption allegations. This award demonstrates that the presence of red flags is not enough to prove corruption. The proponent must prove a causal link between those flags and the event under analysis.

### Navigating through the case

The concession agreement resulted from an [unsolicited proposal](#) submitted on April 16, 2010 by the Lineas Viales de Lima Consortium for the "[Vias Nuevas de Lima](#)" Project, which contemplated the design, construction, operation, and maintenance of certain highways in Lima, Peru (the "Project"). On September 18, 2012, the Project was awarded to the Consortium. On January 9, 2013, the Municipality and Rutas de Lima S.A.C. ("RdL") (a company incorporated by the members of the Consortium) concluded a Concession Agreement (the "[Concession Agreement](#)") under which the Municipality was obliged to grant possession to RdL of the land in the area, the toll booths, and the right of way under concession.

The parties agreed that within 30 days of completion of the required works, the Municipality had to install a new toll in the Chillón district (the "Chillón Toll"). Clause 10.4 of the Concession Agreement provides that if RdL was prevented from collecting tolls due to social unrest, the

Municipality must compensate RdL for uncollected tolls.

In June 2016, after certain interferences with RdL's possession, the parties signed an agreement to implement the Chillón Toll by December 2016 (the "June 2016 Agreement"). On December 29, 2016, the Municipality implemented the Chillón Toll and RdL began collecting the toll. However, toll collection was suspended almost immediately due to unrest that led the Municipality to remove the toll permanently.

During 2017, the Municipality and RdL unsuccessfully sought alternatives to restore the economic equilibrium of the Project. RdL notified the Municipality of its intention to trigger the compensation mechanism under Clause 10.4 of the Concession Agreement and eventually submitted the controversy to arbitration claiming damages due to the interference with its right to collect the Chillón Toll. Among other things, the Municipality argued that the Concession Agreement and the June 2016 Agreement were null and void.

### **Corruption allegations and the standard of proof**

The Municipality submitted that RdL received the Project and the Concession Agreement through corrupt means and obtained illegal benefits during performance of the Concession Agreement. The Municipality did not, however, request the Tribunal to declare the nullity of the Concession Agreement based on these allegations.

The first issue the Tribunal analyzed was whether it had the duty and power to decide on the legality of the Concession Agreement and related documents based on corruption allegations, even when this had not been requested by either party. Based on Mr. Lagergren's famous award on the [ICC Case No. 1110](#) (which stated that "a case such as this, involving such gross violations of good morals and international public policy, can have no countenance in ... any arbitral tribunal"), the Tribunal argued that under both Peruvian legislation and international public policy, it has the duty to make an assessment of the incidences of corruption that could affect the object of the arbitration and decide on the civil consequences of these incidences with respect to the validity of the Concession Agreement.

The Tribunal undertook this not as a criminal judge, but rather as the 'judge of the contract.' Therefore, the declaration of nullity required not only sufficient indications of corruption, but also a showing of a corrupt conduct related to the contract. It was not enough that one of the parties made illegal payments to public officials. The Tribunal must find a causal link between these payments and the contract.

Further, the tribunal decided that in accordance with the current trend in international arbitration it was bound to apply a preponderance of evidence standard. Based on the alleged circumstances and existing indications of corruption, the Tribunal had to decide whether it was more likely than not that the Concession Agreement and/or the June 2016 agreement were obtained through corrupt means.

While not described in the Award, for the sake of this post it is important to briefly delve on how the standard of proof applicable to corruption allegations in commercial and in investment arbitration has evolved over time. In *EDF v. Romania*, the tribunal considered that there was a "general consensus among international tribunals and commentators regarding the need for a high

standard of proof of corruption,” requiring “clear and convincing” evidence. The same reasoning is found in *Belokon v. Kyrgyz Republic*, where the tribunal required “concrete and decisive evidence.”

Throughout the years, these criteria evolved to reflect the complexity of proving corruption. In *Oostergetel v. Slovak Republic*, the tribunal acknowledged that “*for obvious reasons, it is generally difficult to bring positive proof of corruption. Yet, corruption can also be proven by circumstantial evidence.*” This argument was then taken by the *Metal-Tech v. Uzbekistan* tribunal (discussed in [here](#)) noting “that corruption ... can be shown through circumstantial evidence.”

Further, the *Churchill v. Indonesia* tribunal decided to apply a “standard of balance of probabilities or *intime conviction*,” taking into account that more persuasive evidence is required for implausible facts and weighing the available evidence as part of relevant circumstances. The *Libananco v. Turkey* tribunal expressed that “[allegations of fraud] may simply require more persuasive evidence, in the case of a fact that is inherently improbable, in order for the [T]ribunal to be satisfied that the burden of proof has been discharged.”

As has been stated, circumstantial evidence is nothing other than a list of red flags that provides the tribunal with “a valuable tool to analyze whether or not the direct evidence available was sufficient to establish a reasonable inference that the elements of an act of corruption were more likely than not present.”

### **Ruling and Importance of the Award**

In the case under analysis, the Tribunal used the red flags method to reach a decision based on the preponderance of evidence, stating that the flexibility allowed by this standard does not entail a failure to require sufficient evidence of particular incidences of corruption to reasonably establish that corrupt payments were made and their connection to the Concession Agreement or the June 2016 agreement.

The Tribunal began its analysis stating that considering the ongoing international investigations, the fact that companies investigated for corruption were members of the Consortium and that they continue to have interest in the Project is evidence of the possibility of corruption in the Project. However, the Tribunal did not conclude that the sole presence of such companies in a contract necessarily entails corruption. The mere presence of general red flags should not make a tribunal lean towards finding corruption. If a specific party is known for being more tolerant to corruption, it should be considered a general red flag. Nevertheless, in order to tip the scale towards the existence of corruption in a particular case, red flags must be found with regards to a specific fact under the contract, and the tribunal should give each red flag a proportional weight, depending on the inference it provides.

The Tribunal concluded that no allegation or evidence proved that the investment in this case was obtained through corrupt means, considering that the Consortium was the only bidder, RdL submitted 5 versions of the proposal reflecting comments made by the Municipality before it was approved, and the execution of the Concession Agreement is the natural result of the declaration of public interest with respect to the proposal and its subsequent award. Applying the same standards, the Tribunal concluded that the allegations of corruption made by the Municipality with respect to political contributions made to mayor Susana Villaran’s campaign against her removal were not a

red flag, given that the campaign began two months after the Project was awarded. While the Contract was awarded in September 2012, the events that gave rise to Villaran's removal request only began in November 2012. In that context, the Tribunal found no reasons for RdL to need to pay bribes in November 2012 for a contract that it had already obtained in September that year.

The Tribunal also analyzed general corruption allegations made by the Municipality, including with respect to statements made by the Ad Hoc Prosecutor, which the Tribunal found not to provide material information allowing it to presume that corruption existed before and during the Concession Agreement, especially given the Tribunal's lack of access to complete records of the criminal investigations surrounding the case. In sum, the Tribunal was not provided with sufficient evidence to identify red flags directly related to the Project.

Finally, the Tribunal considered that even though there were certain elements that could allow a suspicion of corruption with respect to the Concession Agreement, the fact that the Municipality did not request a declaration of nullity of said agreement reflected the absence of sufficient evidence of the allegations made.

In a nutshell, to the authors' opinion, the importance of this Award is twofold. First, it confirms the trend that since corruption is hard to prove, a preponderance of evidence standard based on red flags should apply. Second, apparent red flags are not enough. The party submitting the presence of red flags has the duty to also show a causal link between such flags and the event under analysis, otherwise those flags will just fly away with the wind.

### **Set aside request before the DC Courts**

Based on the above, the Tribunal went to the merits of the case and awarded approximately US\$ 68 million to RdL. Consequently, the Municipality requested the Courts of the District of Columbia to set aside the award based on the Tribunal's alleged incorrect application of Peruvian law and allegedly new evidence of corruption.

A recent [IBA Report on annulment of arbitral awards](#) indicates that annulment decisions for procedural reasons heard by national courts of jurisdictions that attract the majority of international arbitration proceedings are not common. US courts are no exception. Let's stay tuned for the outcome of the Municipality's application.

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