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Paris Arbitration Week Recap: Affaires d'Etats: Practical Considerations When Defending States In International Arbitration

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In the last three decades, the advent of investment treaty arbitration and more recently third-party funding have led to an exponential rise in the number of international arbitrations pursued by private parties against sovereign States. Against this background, on March 28, 2022, as part of Paris Arbitration Week, Curtis, Mallet-Prevost, Colt & Mosle hosted the webinar "*Affaires d'Etats*: Practical Considerations When Defending States in International Arbitration." This session examined the practical challenges faced by States when defending themselves against these claims. The event featured Marie-Claire Argac, Jaroslav Kudrna, Claudia Salgado Levy and Jeremy Sharpe, and was moderated by Simon Batifort. This post encapsulates key takeaways from the webinar.

The Lack of Institutionalization of Investor-State Dispute Settlement (ISDS)

The speakers noted the differences between ISDS and other forms of dispute settlement involving States. Mr. Sharpe pointed out, for instance, that a first structural difference between ISDS and other forms of international dispute settlement lies in the absence of institutionalization. ISDS differs in this respect from the international trade regime institutionalized around the WTO. The WTO regime is comprised of treaties setting out obligations common to all member States, which facilitates the system's accessibility. At the domestic level, a bureaucratization is implemented through the establishment of offices and ambassadors. ISDS is different in that there is generally no single body of laws that apply to all States, and BITs may differ greatly from one another. There is also no overarching supervisory international institution managing disputes or delimiting State obligations. As a result, it falls upon each State to organize itself. However, in practice many States have focused on ISDS episodically, when faced with a claim, rather than through a systemized approach towards arbitration claims.

Dr. Salgado illustrated the impact of these features of ISDS by reference to the evolution since the early 2000s of Ecuador's legal mechanisms for responding to ISDS claims. Initially, although the Attorney General Office ("**AGO**") already existed, there was no specialized team in charge of handling international investment disputes. Ecuador's first arbitration cases illustrated the need for specialized counsel and experienced arbitrators. The AGO is now a 12-member division dedicated

to international affairs, which includes international commercial and investment arbitration. Ecuador combines retaining outside firms to handle arbitral proceedings, while ensuring that they collaborate with the local team for research on domestic law and liaison with public entities. Depending on the workload (currently 15 international commercial arbitrations and 7 investment arbitrations) the local team can play a more active role within the arbitrations.

Dr. Kudrna explained that the Czech Republic has adopted a hybrid model for its defense. A 10-member internal team is heavily involved in the cases and to the extent necessary is supplemented by outside firms that are chosen after taking into account the initial analysis of the case, the amounts claimed, the expected complexity and risks, and the quality of the opposing counsel. Boutique law firms tend to be favored for smaller cases. He went on to list some of the attributes that States value most in outside counsel, including: the experience of the lead counsel and excellent pleadings skills; organizational skills to avoid unnecessary hastiness or delays; an understanding of the State's needs, interests and inner workings; attention to the client-relationship, including having the lead counsel devote the necessary amount of time to the case; and effective cost management, for example to ensure that not too many resources are spent on secondary issues.

Mr. Sharpe spoke about the importance of formally designating a State agent, i.e., someone within the State bureaucracy who will take the lead on the State's defense and oversee inter-agency coordination, drawing lessons from the way agents operate in international litigation. Such agents would officially represent States before tribunals, thereby enhancing the reliability of the State by reflecting its consistent position on a given issue. They may also help to coordinate and manage litigations and liaise with outside counsel. Finally, agents can help States articulate their views, as Mr. Sharpe detailed in an article.

Access to Documents and Witnesses

Panelists also engaged with certain practical difficulties that may be faced by States defending ISDS claims. Dr. Kudrna mentioned some of the specific challenges that may be encountered during the document production phase such as the fact that many document requests are drafted in an overly broad manner. Furthermore, he noted that, given the lack of any statute of limitations in old BITs, some investment claims related to facts that occurred decades ago, when documents were not digitalized and have since been destroyed. Dr. Kudrna also referred to the misconception that the State entity in charge of the State's defense can access any documents produced by other state organs, such as those relating to criminal investigations. Ms. Argac also stressed how difficult it can be to gain access to all of the relevant information and individuals in some cases due to the fact that claims are often brought years after the fact, when the relevant individuals have left and documents may have been lost or destroyed.

Dr. Salgado underscored difficulties arising from the lack of inter-institutional coordination between public entities. In the case of Ecuador, she explained that the law now requires public entities to provide the AGO with relevant documents within a few days. Dr. Kudrna added that it can be more challenging to find witnesses who will testify on behalf of a State, as opposed to employees of the claimant, a difficulty that may be compounded if hearings become open to the public.

Procedural Challenges

The session also addressed several difficulties that might arise procedurally for States in ISDS, including challenges associated with frivolous claims and with information asymmetry and limited preparation time.

The proliferation of third-party funding has led to an increase in the number of frivolous claims, said Dr. Salgado. Some investors resort to arbitration as a means of pressure against States. Even if States ultimately prevail in such scenarios, it may represent a waste of costs and human resources.

Another significant challenge in the defense of States relates to the fact that claimants have months to prepare their case with outside counsel and come up with their optimal case strategy, while States rarely have this luxury. Ms. Argac noted that in investment arbitration in particular, States receive a request for arbitration with a basic description of the claims and little more to work off of and that they have to wait until the memorial on the merits to get a proper view of the claims. The limited information available to the States at such early stages may affect their ability to effectively present their case. In addition, many arbitration rules require that certain rights be exercised early on, such as the right to raise counterclaims for instance.

Ms. Argac emphasized the importance of retaining outside counsel sufficiently early in the case to advise on the composition of the tribunal, noting that arbitration rules generally provide for tight deadlines within which to constitute the tribunal and that there is a limited pool of arbitrators who are sufficiently sensitive to the interests of States. Another important aspect resides in the arbitrator's approach towards quantum and DCF, as this can have a devastating effect on potential damages. Dr. Salgado also referred to the fact that the significant amount of cases faced by Ecuador and the limited pool of arbitrators have led to situations where the same arbitrators who had already decided cases involving Ecuador were reappointed in other cases against the State, which could lead to them being influenced by their previous decisions. One solution proposed by Mr. Sharpe was to increase the pool of arbitrators sensitive to the interests of States by encouraging former State agents who were directly involved in the defense of States in international arbitration to act as arbitrator.

Recommendations for States

In closing, Ms. Argac offered recommendations to States seeking to improve their defense practice:

1. **select outside counsel as soon as possible** to be advised early on, especially regarding the constitution of the arbitral tribunal.
2. **think carefully about the selection of outside counsel**: prior experience in international arbitration, particularly representing States, is fundamental; parallel representation of investors with diametrically opposed positions on key recurring issues may raise difficulties.
3. **pay attention to the early stages of a case**: while it may be tempting to respond to all the accusations raised in a notice of dispute or a request for arbitration, it is often prudent for the respondent to limit itself to what is required by the applicable rules and stay concise.
4. **facilitate counsel's access to relevant documents and individuals**, for example through the designation of an agent to liaise with external counsel or assist with the search for potential

witnesses and document gathering.

A final recommendation was directed towards tribunals and arbitral institutions: the legitimate push towards expediency should not come to the detriment of States' rights to plead their case, locate and gather evidence or witnesses in these often complex, high-stakes disputes, and have sufficient time to liaise among the relevant agencies and obtain necessary approvals. Having a more realistic schedule from the start will ultimately ensure a smoother arbitration.

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