Kluwer Arbitration Blog

LIDW 2022: States as First-Class Citizens?

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As part of the 2022 London International Disputes Week, 3 Verulam Buildings, Clifford Chance, Kroll, Mayer Brown, QMUL, Three Crowns and White & Case organized a conference on "States as first-class citizens? Special treatment for states in international disputes". This post covers both panels of the program.

Panel One: Procedural and Substantive Peculiarities of Arbitration Proceedings with a State Party

The stellar panel was composed of Loukas Mistelis (QMUL, Clyde&Co), Leilah Bruton (Three Crowns), Jessica Gladstone (Clifford Chance), Rachael O'Grady (Mayer Brown), and Vikki Wall (Kroll).

The panel discussed the procedural and substantive peculiarities of arbitration proceedings with a State party. They considered both investor-State and commercial arbitrations.

Loukas Mistelis opened the discussion with a historical observation. While the 1980s and 1990s saw the rise of non-state actors on the global scene, in the last two decades, States are reassessing and recalibrating their sovereign roles in international economic and investment law. Despite the focus on sovereignty, States themselves have become more complex, expanding their range of activities, including emerging roles in commercial transactions and participating in sovereign wealth funds with admirable investment portfolios. Prof Mistelis observed that States stand generally at the receiving end of investment arbitration, however, in commercial matters they may (and increasingly do) appear as the claimant. Does being a State party to an arbitration proceeding change the procedural dynamics? Does being a State Party to an arbitration proceeding change the behaviour of the tribunal? In other words, are States dealt with as first-class citizens in international arbitration?

To Jessica Gladstone (Clifford Chance), several phenomena come into play when a State is a party to an arbitration:

1. Even the decision to pursue or defend a claim has its own complexities. Considerations may include "opening the floodgates", maintaining the confidentiality of elements under dispute, and perhaps preferring the political cover of a judicial order over a political decision when it comes to

explaining an outcome to a domestic audience.
2. Diplomatic considerations may also drive a State's decision on how to deal with a dispute. Sometimes, a formal dispute process may be preferred to separate out and insulate the wider diplomatic relationship from the dispute.
3. The State may also need to manage particular public relationship implications with both a domestic and international audience.

In terms of evidence, States often present tribunals with the challenge of dealing with refusal to disclose government documentation that is classified as secret. In such cases, tribunals must be persuaded of the genuine purpose behind an application to redact or withhold a document. The IBA Rules on the Taking of Evidence in International Arbitration support this with a specific provision enabling the exclusion of evidence where there are grounds of special political or institutional sensitivity that the Tribunal has determined to be *compelling* (Art 9.2(f)). Ultimately, the arbitral tribunal must be sensitive to the challenges posed by evidentiary issues in cases involving states, and determine the relevance, materiality and the appropriate weight to be accorded to the evidence in all the circumstances.

Procedural issues may also arise. In general, States may take longer to organize themselves internally, consulting with a wide range of stakeholders from across the government before putting forward their legal or factual case. Similarly, jurisdictional objections arise more frequently in arbitrations with a State party, as the consent to arbitrate of a sovereign is often very specifically drawn. Finally, Jessica Gladstone argued that the potential concurrence of domestic and international proceedings has to be taken into account when arbitrating with a State party. In environmental cases, for instance, domestic proceedings may be preceding or parallel to an investor-state dispute. Questions may arise as to the relevance of and interaction between the parallel proceedings.

Reacting to the comment on public relations, Prof Mistelis recalled that the mere existence of disputes may affect the credit rating of the State. He further asked the panel whether it was true that representing a State these days had better-winning chances.

According to Leilah Bruton, tribunals ensure a fair level-playing field, and State representation benefits from advantages in the procedural phase. The most important privilege is *timing*. Tribunals are usually sympathetic to the State's specific circumstances. States may appoint or instruct specialist counsel very late, sometimes when the proceedings have already begun. This may lead to a disruption of the procedural timetable. Issues of instructions may arise too. When a State is a party, an instructing body is constituted within the government to instruct the outside counsel. That body may have a number of stakeholders, from the ministry of justice, ministry of energy, of international affairs, up to the agency that has substantive links with the dispute at stake. This may create extra layers of time in consulting and seeking instructions. The State's potential inconsistency is another issue The State may change its legal strategy throughout an arbitral proceeding, depending on a counsel adjustment, a policy shift or government change. Finally, State files can be kept by different state authorities. However, in Ms. Bruton's experience, tribunals are accommodating and fair.

Bouncing off these potential disruptions, Prof Mistelis asked whether the panellist perceives a level of asymmetry in the arbitral decisions. Whether the equality of arms is maintained or whether they see an asymmetry of weapons. More generally, with the growing attention to the right to regulate, public interest challenges, such as climate change or the redrafting of new-generation BITs, is there

a disadvantage in representing a non-state party?

To Ms. Bruton, access to evidence can create an inequality of arms. In particular, documents linked with the exercise of the State's police powers are difficult to produce. From her experience, tribunals take initiatives to ensure that fairness is ensured. For instance, they may appoint a third-party reviewer to maintain a level playing field. In her view, tribunals are not unfair on the substance; they may be understanding of delays and timing issues that create a slight imbalance. To Rachael O'Grady (Mayer Brown), tribunals generally ensure a standard playing field level. In this sense, she noted that the new ICSID rules allow greater equality of arms, too.

The panel then turned to experts' appointments. In her capacity as expert in arbitral proceedings, Vikki Wall describes an asymmetry of information when appointed as accountant for the state party. In particular, access to financial information may be limited or inexistent. Often, her first contact with the State is through a specifically appointed counsel. She pointed out that the quantum of damages was a very important issue for claimants, but often left to the last day of a hearing, when asked whether tribunals pay enough attention to expert witnesses on accounting. She also noted that one way of assisting tribunals with engaging with expert evidence is for arbitral tribunals to appoint experts themselves, although seen only 11 times in 130 recent BIT cases where damages were awarded. Further, Prof Mistelis and Ms Wall remarked that a lack of diversity currently existed in the appointment of expert witnesses, but hoped to see improvement.

Another issue addressed was the conflict of state representation when two competing governments claim legitimacy or control over a specific territory – such as in Venezuela or Yemen.

In Ms Bruton's view, an issue of standing might arise when competing political factions claim to represent the same State. In general, arbitral tribunals have treated this as a procedural issue – they usually maintain the status quo and place the burden of proof on the authority seeking to change the party to the proceeding. For instance, in the case of Yemen, two competing governments coexist. One is internationally recognised; the other is not. One minister of legal affairs intervened in an UNCITRAL case to claim that it had authority, and the tribunal stayed the proceedings. Usually, tribunals afford greater weight to the territorial control in relation to the claim rather than the international recognition of the party to the proceedings. In any event, this raises significant issues that have yet fully known implications.

Last, Rachael O'Grady (Mayer Brown) looked at how in investment disputes, have procedural shields and a sword with counterclaims.

Counterclaims can be defined as positive claims by the State seeking relief from the foreign investor. Counterclaims seem counterintuitive in investment arbitrations since bilateral investment agreements (BITs) are meant to primarily protect investors from State's measures. Nevertheless, counterclaims are possible under article 46 of the ICSID Convention, which states the following:

> "Except as the parties otherwise agree, the Tribunal shall, if requested by a party, determine any incidental or additional claims or counterclaims arising directly out of the subject-matter of the dispute provided that they are within the scope of the consent of the parties and are otherwise within the jurisdiction of the Centre."

Rachael O'Grady elaborated on the three conditions set out by the article:

1. Both parties must have agreed to allow counterclaims. This is considered an issue of consent. Despite Reisman's opinion, arbitral tribunals generally have determined the consent by an agreement outside the ICSID convention. Tribunals infer consent from the treaty language underlying the dispute at hand. In particular, they may look for the fact that the treaty covers "all disputes concerning an investment".
2. The counterclaim must "arise out of the subject of the dispute". In other words, the counterclaim must arise out of the main claim. In Saluka v Czech Republic, the tribunal agreed that a counterclaim could be heard but decided that it was not connected sufficiently to the subject of the dispute.
3. The counterclaim must be within the "within the jurisdiction of the Centre", meaning it must fall within article 25 of the ICSID convention. In practice, the State and eventually the tribunal must establish a positive obligation on the investor, not the State. In Urbaser v Argentina, the tribunal found that the BIT was broad enough to allow counterclaims. However, it could not pinpoint an international law obligation on the part of the investor. While there is not a general rule that international law obligations only apply to States, in this case, the tribunal could not find an applicable law to the investor's conduct.

Counterclaims raise interesting questions. What kind of positive obligation may come to be placed on investors? Will the new wave of investment treaties refer to positive international obligations on the investor? Will these obligations be substantial enough to find liability? Other questions of procedural economy and equality of arms may arise in case of parallel proceedings in domestic courts too. Finally, could counterclaims eventually defeat the original purpose of BITs?

Panel Two: Whether States have Preferential Treatment before the English Courts in Arbitration-related Cases

The second brilliant panel was composed of David Goldberg – Moderator, White & Case), Mark Wassouf (3 Verulam Buildings), Zahra Al-Rikabi (Brick Court Chambers), and Cameron Miles (3 Verulam Buildings). This panel revolved around the question of whether States have preferential treatment before the English courts in arbitration-related cases. The panel took opposing views in answering this question, thereby creating an engaging discussion.

Mark Wassouf argued that States do not receive any special treatment before English courts and, in consequence, they do not have a privileged standing. In fact, it was said that States are generally treated as regular commercial parties.

Under English law, the only statutory advantage that States have is the State Immunity Act. Although it gives States immunity from the court's adjudicative and enforcement jurisdiction, commercial judges in England try to avoid granting the State special treatment in arbitration-related applications. Admittedly, this trend can be seen in the General Dynamics v Libya saga, in which the Court of Appeal found a way around the statutory requirement set forth in Section 12 of the State Immunity Act. However, this judgment was later overturned by the Supreme Court.

Another example of this stance is the case Micula v Romania. Here, the Supreme Court decided whether enforcement proceedings against Romania could continue, even if such enforcement implied that the State would breach its international obligations under EU law. The Supreme Court analysed the issue without paying deference to any of Romania's international obligations. In

short, it was treated like any other commercial party would have been treated. The panellist concluded that counsels representing States before English courts are better off grounding their "arguments in ordinary commercial and legal logic".

Conversely, Zahra Al-Rikabi considered that States do have, as a matter of fact, some advantages under the State Immunity Act. For instance, unlike commercial parties, States are not precluded from raising objections to the arbitral tribunal's jurisdiction that were not disputed before. As the court in PAO Tatneft v Ukraine held, there is no foreclosure of the type of arguments that the State may raise as to the applicability of the State Immunity Act, regardless of what might have occurred before the arbitral tribunal.

In general, the panellist discussed that there are several obstacles when claimants face proceedings involving a State. Parties need to tackle this issue both from the adjudicative and enforcement immunity perspective. In particular, claimants must be able to address the court's jurisdiction and prove why the State cannot benefit from the immunity as established in the State Immunity Act.

Finally, Cameron Miles offered a more pragmatical approach to the treatment of States in English courts. It was discussed that the State Immunity Act is not only driven by customary international law. In fact, considerations of comity are always relevant. Section 15 of the act supports such an argument. For that reason, where the case deals with issues of State immunity, depending on the judge and its background, some outcomes might be preferred over others.

Touching upon the previously mentioned General Dynamics v Libya cases, the panellist suggested that the decisions adopted by the Court of Appeal and the Supreme Court can be explained by taking into account the judges' backgrounds. Interestingly, it was argued that the Court of Appeal's judgement gave more weight to the commercial arguments of the case because the panel was composed of two judges that had been members of the Commercial Court and the Chancery Division, respectively. On the other hand, the Supreme Court's decision to overturn the appeal was taken by a majority composed of former academics, one of them specialising in public international law. Arguably, they were more inclined to give the State special treatment. The panellist concluded that both rulings could be justifiable. The differences between them can be better described as conflicting approaches to the same issue.

The key takeaway of the session is that English courts take State immunity seriously but maintain a fair level-playing field between the parties. Even though the State Immunity Act does raise additional hurdles for claimants, counsel acting for States should not only rely upon State immunity arguments.

Conclusion

The first panel showed the many procedural and substantive intricacies that arise when a State is party to an arbitral proceeding – whether commercial or Investor-State. Three main topics are of importance and may raise concerns of fairness: the privileges over the production of (expert) evidence, the issue of standing before arbitral tribunals and the increase of counterclaims. Bearing in mind that a State must manage public and diplomatic relationships when taking part in arbitration, the panel opined that arbitral tribunals have and should continue to offer a balanced level-playing field to all parties.

The second panel demonstrated that cases involving States before domestic courts can be tricky. States enjoy a differential treatment before courts that is established in law. States' sovereignty and immunity is to be taken seriously as it poses specific challenges to the jurisdiction and access to evidence. However, to the panel, immunities and privileges must be assessed cautiously, and should be grounded in well-reasoned commercial and legal logic to win over the opinion of domestic courts.

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