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Commentary

Coffins And Caimans: International Arbitral Tribunals Passing Judgment On National Court Proceedings

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I. Introduction

What does Mr. Jerry O'Keefe, of southern Mississippi, have in common with the Cofán Indians of eastern Ecuador? They both are, or were, at the center of cases that have become legendary among arbitration practitioners, with respect to the extent that international arbitral tribunals can or should sit in judgment upon the practices and procedures of courts of a State.

This is a sensitive area. At first sight, it may seem surprising, and presumptuous, that an arbitral tribunal, consisting generally of three lawyers who are not judges, should pass judgment upon the adequacy of the procedures of the courts of a State. What right, one may ask, does such a tribunal have to second-guess the courts of any State? The answer, surprisingly or not, is that there are indeed circumstances where arbitral tribunals may determine that court proceedings have fallen below minimum internationally acceptable standards, thus engaging the legal responsibility of the respective State.

II. Review Of Foreign Court Proceedings Generally

The law may authorize the courts of a country to review a foreign judgment or arbitral award in order to determine whether due process has been observed. For example, in accordance with the general criteria for enforcing a foreign judgment established in the U.S. by *Hilton v. Guyot*, 159 U.S. 113 (1895) and the Uniform Foreign Money-Judgments Recognition Act (as adopted by many States[1]), U.S. courts may refuse to enforce a judgment if the defendant was not properly served with notice of the proceedings, or if the judgment was obtained by fraud, or if "the judgment was rendered under a system which does not provide impartial tribunals or procedures compatible with the requirements of due process of law".[2] Similarly, under the 1958 Convention on the Recognition and Enforcement of Foreign Arbitral Awards ("the New York Convention"), enforcement of a foreign arbitral award may be refused by a court if, for example, "the party against whom the award is invoked was not given proper notice of the appointment of the arbitrator or of the arbitration proceedings or was otherwise unable to present his case" (Article V(1)(b) of the New York Convention).

But it is another matter for a court to go beyond these specifically delineated grounds for refusal of the enforcement of a foreign judgment or arbitral award, and to hold that the systemic defects of the courts of a foreign State are such as to render unacceptable a decision emanating from those courts. It is self-evident that such a power should be exercised rarely and with great caution.[3] Nations may differ greatly in their views as to what is or is not acceptable procedure, or how much delay is permissible. Care should be taken that more developed countries should not be perceived as overly critical of the procedures of countries with less available resources than they, including for the justice system.[4] And nations should also guard against excessive

smugness about their own judicial system, lest the tables be turned and they be found to have a beam in their judicial eye larger than the mote in the eye of supposedly less fortunate nations.[5]

Nevertheless, there are circumstances in which the courts have found it proper to determine that the judicial system of a foreign State is inadequate, whether because of systemic deficiencies, likely bias against a particular party, or for other reasons: see, for example, the *forum non conveniens* case of *Canadian Overseas Ores Ltd. v. Compania de Acero del Pacifico S.A.*, 528 F. Supp. 1337, 1342 (S.D.N.Y. 1982), finding that "serious questions" had been raised "about the independence of the Chilean judiciary", and that "a significant doubt remains whether [the defendant] could be assured of a fair trial in the Chilean courts".

III. Review By International Arbitral Tribunals Of Court Proceedings

In what context is it possible for an arbitral tribunal to consider the adequacy or inadequacy of court proceedings? In the investment arbitration context, it may arise as follows: among the protections typically afforded to investors under a Bilateral Investment Treaty ("BIT") made between two contracting states, are protection against expropriation, the obligation to provide full protection and security to the investment, and the duty to accord "fair and equitable treatment" to the investment.[6] Where the deficiencies of a court system or court procedures are alleged to constitute a violation of a BIT, it is frequently on the ground that the respective state's conduct thereby fell short of one or other of these standards.[7] There is no question but that the federal or state courts of a state are organs that can implicate the responsibility of that state.[8] While sometimes the deficiencies of a court system are alleged to amount to expropriation, or failure to provide full protection and security, more often they are alleged to fall under the "denial of justice" sub-category of breach of the "fair and equitable treatment" standard.[9]

Thus, it is undoubtedly possible for deficiencies in a court system or proceedings to engage the international responsibility of a state for the purposes of a BIT. A case frequently cited for the purpose of defining what amounts to a "denial of justice" in a judicial context, is *Mondev International Ltd. v. USA*, ICSID Case No. ARB(AF)/99/2 (2002). The arbitral tribunal opined that conduct that occasions "shock or surprise" leading to "justified concerns as to the judicial propriety of the outcome" with regard to generally accepted standards of administration of justice would amount to a "denial of justice" for this purpose: see para. 127 of the Award. In this case, it was held that the United States did not breach its "fair and equitable treatment" obligation by, among other matters, according sovereign immunity to a State authority of the Commonwealth of Massachusetts.[10]

More dramatic is the case of *The Loewen Group, Inc. and Raymond Loewen v. USA*, ICSID Case No. ARB (AF) /98/3, 42 ILM 811 (2003). This case was brought by a Canadian funeral services provider against the United States, arising out of alleged judicial and procedural misconduct in connection with a trial in the State of Mississippi. The trial arose out of commercial arrangements, relating to funeral services, between Mr. Jerry O'Keefe and his family interests, and the claimants in the investment arbitration proceedings ("Loewen"). This resulted in a verdict against Loewen for $500 million for compensatory and punitive damages, and damages for emotional distress. This was apparently, at the time, the largest jury award ever in the State of Mississippi. At the trial, the plaintiffs' counsel was permitted to make repeated inflammatory remarks about Loewen's foreign nationality, and about race and class-based distinctions between the plaintiffs and Loewen. Loewen was then required, as a condition of appealing the verdict, to post a bond for 125% of the amount of the same. Rather than do so, Loewen settled with O'Keefe for $175 million.

The arbitral tribunal in the *Loewen* case did not mince its words with respect to the unfairness of these proceedings. They constituted "a miscarriage of justice amounting to a manifest injustice as that expression is understood in international law".[11] Further,

"By any standard of measurement, the trial involving O'Keefe and Loewen was a disgrace. By any standard of review, the tactics of O'Keefe's lawyers. . . . were impermissible. By any standard of evaluation, the trial judge failed to afford Loewen the process that was due".[12]

As a result,

> "the whole trial and its resultant verdict were clearly improper and discreditable and cannot

> be squared with minimum standards of international law and fair and equitable treatment".[13]

However, in order to determine whether the proceedings as a whole violated the "fair and equitable treatment" standard of NAFTA Article 1105, the tribunal went on to consider the post-trial remedies available to Loewen. It held that Loewen had failed to pursue all the remedies available to it, including recourse to the U.S. Supreme Court, and therefore there was no violation of customary international law and no violation of NAFTA. It also held that, because Loewen had assigned its claims to a Canadian corporation owned and controlled by a United States corporation, the tribunal lacked jurisdiction under NAFTA.

It may well be considered that the appellate recourses open to Loewen in the circumstances were illusory and that the tribunal was pusillanimous in failing to find a violation of the "fair and equitable" treatment standard of NAFTA Article 1105.[14] Nonetheless, this case provides a dramatic illustration of circumstances in which it is indeed appropriate for an international arbitral tribunal to find that the conduct of national courts falls below an acceptable standard.

The case of *Chevron Corporation and Texaco Corporation v. Ecuador*, in its different manifestations, has become "iconic".[15] The saga has taken in place in the U.S., Ecuadorean, and other national courts, and before at least two international arbitral tribunals. It arises out of the operations of Texaco Petroleum in eastern Ecuador between 1964 and 1992.[16] Allegedly, in the course of these operations, Texaco improperly dumped toxic by-products of the drilling process into two local rivers, and constructed a pipeline that leaked large quantities of petroleum into the environment, thereby severely damaging the health of local residents, including members of the Cofán Indian tribe. Litigation ensued between those allegedly affected and Texaco, in the U.S. and Ecuadorean courts, resulting, in February 2011, in a judgment in the Ecuadorean courts for a sum in excess of $18 billion, against Texaco and Chevron Corporation (with which Texaco had by then merged). It will be appreciated that this summary does no justice whatsoever (no pun intended) to the protracted and tortured nature of the litigation, which has included legal counterattacks by Chevron and Texaco against the plaintiffs' attorneys and experts, and enforcement proceedings in Canada, Brazil and Argentina.[17]

Of more relevance to this article, the events described have spawned two investment treaty arbitrations, both under the UNCITRAL Rules, pursuant to the U.S. – Ecuador BIT. The first one, *Chevron Corporation and Texaco Petroleum Co. v. Ecuador*, PCA Case No. 34877 (www.italaw.com/cases/251) related to investment agreements between an affiliate of Texaco, and the Ecuadorean Government, with respect to petroleum exploration and production, out of which activities the environmental claims described above arose. Claims were filed in the Ecuadorean courts for the recovery of in excess of $500 million under those agreements. The delays in the proceedings, and the nature of the decisions by the Ecuadorean courts, were such as to induce the filing of the investment treaty claim, for denial of justice and violation of Ecuador's treaty obligations. The tribunal held that the delay in the proceedings, of in excess of thirteen years, was such as to violate a specific provision in the BIT, requiring Ecuador to provide "effective means of asserting claims and enforcing rights" with respect to the investment.[18] The tribunal noted that delay of itself might not constitute a violation of Ecuador's treaty obligations; it was necessary for the delay to be unjustified, and it so found. The tribunal awarded the claimants approximately $96 million in damages, including interest, and after deduction of tax.[19]

The other investment arbitration proceeding arising out of the *Chevron* chain of events is *Chevron Corporation and Texaco Petroleum Corporation v. Republic of Ecuador*, PCA Case No. 2009-23 (www.italaw.com/cases/257). This case directly impugns the Ecuadorean proceedings which culminated in the February 2011 judgment of the Ecuadorean courts against the claimants in the arbitration. It alleges that the Ecuadorean Government improperly interfered with the proceedings in total disregard of Ecuadorean law, international standards of fairness, and basic due process, thereby violating Ecuador's obligations under the BIT. It will be seen from a review of the U.S. cases, particularly Judge Kaplan's decision in *Chevron Corporation v. Donziger*, 768 F. Supp. 2d 581 (S.D.N.Y. 2011),[20] that the U.S. courts appear to take a favorable view of the claimants' allegations. While the arbitral tribunal in this case has not yet issued an award on the merits, it has issued an Interim Order (later converted to an Interim Award) directing Ecuador to take all measures at its disposal to suspend or cause to be suspended the enforcement or recognition of any judgment against the

claimants in the Ecuadorean proceedings,[21] and has subsequently decreed that Ecuador is in violation of its orders to this effect.[22]

These cases demonstrate that, in proper circumstances, an international arbitration tribunal may indeed find that the procedures or decisions of national courts may be such as to violate the international obligations of the relevant State, resulting in an award of damages against it, and even what amounts to an injunction requiring it to ensure that it act in accordance with those obligations. However, the circumstances must generally be such as to "shock or surprise", in the words of the *Mondev* tribunal. It is enough to read the description of the proceedings in the *Loewen* award, or Judge Kaplan's description of the Ecuadorean proceedings in the decision referred to in the preceding paragraph, in order to perceive the type of behavior that may trigger a State's international responsibility.

IV. Review By International Tribunals Of Court Proceedings Concerning Arbitration Awards

It is apparent, therefore, that, in a proper case, an international arbitration tribunal may find that national court procedures or proceedings may be such as to violate the international obligations of the respective State. What about decisions or actions of national courts with respect to arbitration proceedings or arbitral awards?

It is indeed possible for a State's international obligations to be breached where national courts act inappropriately with respect to an arbitral award or arbitral proceedings. In *Saipem SpA v. People's Republic of Bangladesh*, ICSID Case No. ARB/05/7 (2007) (Decision on Jurisdiction), the question arose as to whether the subject-matter of the dispute concerned an "investment" so as to afford jurisdiction to the investment tribunal under Article 25(1) of the ICSID Convention.[23] The case involved a gas pipeline contract. A dispute arose thereunder, which was referred to arbitration, resulting in an ICC award in Saipem's favor. The Bangladesh courts refused to acknowledge the ICC award. The ICSID tribunal held that the dispute and the award arose directly from the investment, and therefore the award was considered part of the investment.[24] The tribunal therefore had jurisdiction. While this decision is on jurisdiction only, and does not determine whether the decision of the Bangladesh courts amounted to a breach of the respective BIT, it at least opens the door to the possibility of such a decision.

In *ATA Construction, Industrial and Trading Company v. Hashemite Kingdom of Jordan*, ICSID Case No. ARB/08/2 (2010), the annulment of an arbitration award and the extinguishment of the respective arbitration agreement were held to constitute a violation of Jordan's obligations under the applicable BIT. The arbitral tribunal held that, under the BIT, the right to arbitration could constitute an "investment", and that the extinguishment of the right to arbitration deprived the claimant of an asset, in violation of the BIT's investment protections.[25]

GEA Group AG v. Ukraine, ICSID Case No. ARB/08/16 (2011) represents a step back from these earlier cases. This case involved, among other matters, the inability of the investor to enforce an ICC award in the Ukraine. The arbitral tribunal held, disagreeing with the tribunal in *Saipem*, that the ICC award in question did not constitute an "investment".[26] It further held that the actions of the Ukraine courts did not amount to expropriation or denial of justice, and that the mere decision of the courts not to enforce the award did not amount to a breach of the respective BIT. For that to occur, there would have to exist an element of discrimination or other egregious conduct.[27]

White Industries Australia Ltd. v. India (UNCITRAL arbitration award, November 30, 2011; see www.italaw.com/cases/1169) involved an ICC award which remained unenforced by the Indian courts after some eight years.[28]of efforts to do so by the claimant. The tribunal held that the ICC award did constitute part of the claimant's rights under the investment, amounting to a "crystallization" of its rights under the investment contract, or as "continuing" those rights.[29] In this, the tribunal disagreed with the *GEA Group* tribunal. The tribunal went on to hold that there was no breach of the "fair and equitable" standard and no denial of justice. However, it found that the court delays in question did constitute a breach of a provision of the BIT in question requiring the host state to provide foreign investors with "effective means" of enforcing their rights.[30]

It will be seen that an important threshold decision, where court proceedings involving an arbitration award are alleged to constitute a breach of a BIT, is whether the arbitration award itself, together with the underlying contract and/or dispute, constitute an "investment" so as to enable the arbitral tribunal to exercise jurisdiction.[31]

It appears to be settled that legal proceedings in the host country, related to an investment, may themselves constitute an "investment" for the purposes of a BIT, since they are deemed to be a continuation of the investment.[32] The trend, based on the cases referred to above, appears to be in favor of treating an arbitration award consequent upon the investment in the same manner.

V. Conclusions And Final Considerations

It is therefore indeed the case that international arbitral tribunals, constituted in accordance with a BIT, may pass judgment upon the legal system or proceedings of a State and find it or them so lacking as to constitute a breach of the State's international obligations, even to the extent of being liable for damages. For example, in the *Chevron Corporation and Texaco Petroleum Co. v. Ecuador* (PCA Case No. 34877), and *White Industries Australia Ltd. v. India* cases, substantial damages were awarded against Ecuador and India, respectively. However, it is clear that such decisions are not reached lightly. If courts are on their guard against overreaching in criticizing the judicial system of a foreign State, this is, or should be, even more the case for arbitral tribunals, which typically consist, not of judges, but of distinguished lawyers.[33]

In the investment arbitration context, even though members of the tribunals are frequently nationals of less developed countries, especial care must be taken that tribunals are not perceived as overly critical of the practices of such countries, not only in the judicial sphere, but also in the regulatory and other spheres.[34] This is not just a question of justice being seen to be done; it is also a matter of fairness, and an expression of the basic principle, going back at least as far as the *Oscar Chinn* case of 1934,[35] that the foreign investor takes the commercial or other conditions in the host State as he finds them. This extends to the judicial system: see the *White Industries* Award, para. 10.3.15.[36] Indeed, the *White Industries* tribunal, at para. 10.4.18 of its Award, appears to accept in principle the following argument by the Indian Government:

> "India, as a developing country, with a population of over 1.2 billion people and an overstretched judiciary, must be held to different standards than, for example, Switzerland, the United States or Australia".[37]

Tribunals in future cases will be required, as they have in the past, to balance such considerations against the requirements that a court system and court proceedings comply with "minimum standards of international law and fair and equitable treatment".[38]

Endnotes

1. See, for example, New York Civil Practice Law and Rules, § 5304.

2. Uniform Foreign Money-Judgments Recognition Act, § 4(a)(1); and see *Hilton v. Guyot* at pp. 203, 205: recognition may be refused if the foreign country lacks a system of "impartial administration of justice"; see also *Bank Melli Iran v. Pahlavi*, 58 F. 3d 1406, 1410 (9th Cir.), *cert. den.* 516 U.S. 989 (1995).

3. See, for example, the tribunal in the *Mondev* case, cited hereafter, at para. 126: "it is not the function of NAFTA tribunals to act as courts of appeal". The same could be said of any investment arbitration tribunal.

4. Developing nations may legitimately consider that their limited resources are better spent on improving health care, education, housing, or prisons, rather than on a more expeditious or efficient court system. And, lest it be thought that excessive delay is exclusively the province of less developed nations, and that the legal systems of England and other developed countries are always "the envy of less happier lands" (Shakespeare, *Richard II*, Act II, Scene 1), be it recalled that the notorious Chancery case of *Jarndyce v. Jarndyce*, lasting decades, described in Dickens' *Bleak House* (1852), was intended to highlight the deficiencies in the judicial system of what was, at that time, the world's pre-eminent trading and military nation.

5. Matthew 7:3-5; and see the *Loewen* case, described hereafter.

6. See Bianchi, "A Look at Some Recurring Issues in Investment Arbitration", May/July 2012 Dispute Resolution Journal, at p. 68.

7. The claim may also be brought on the basis of "denial of justice" under international law (see endnote ix), or under a specific provision in the respective BIT, as in

the *Chevron and Texaco v. Ecuador* and *White Industries v. India* cases, cited below.

8. See *Arif v. Moldova*, ICSID Case No. ARB/11/23 (2013), para. 439: "the State has to be seen as a unity and the acts of any of its organs, including the judiciary, may violate international law".

9. McLachlan, Shore and Weiniger, "International Investment Arbitration" (Oxford Univ. Press 2008), paras. 7.80 – 7.98. Note also that there is substantial authority for the proposition that international law allows a free-standing claim for denial of justice, for failure to provide a system of justice which treats aliens fairly, honestly and impartially: *Arif v. Moldova, supra*, paras. 433-5, citing Paulsson, "Denial of Justice in International Law" (Cambridge Univ. Press 2005).

10. See also *Arif v. Moldova, supra*, para. 445: the State is in breach of its obligations "if and when the judiciary breached the standard by fundamentally unfair proceedings and outrageously wrong, final and binding proceedings".

11. Para. 54 of the Award.

12. Para. 119 of the Award.

13. Para. 137 of the Award.

14. Without prejudice to the validity of the tribunal's finding that it lacked jurisdiction.

15. Mistelis, "Award as an Investment: the Value of an Arbitral Award or the Cost of Non-Enforcement", 28 ICSID Review – Foreign Inv. L.J. 64, 85, fn. 114 (2013).

16. The author of this article has visited eastern Ecuador, including Lago Agrio (which figures significantly in the various *Chevron* proceedings), and can vouch for the presence there of caimans and other, larger, reptiles.

17. The U.S. proceedings include *Aquinda v. Texaco Inc.*, 945 F. Supp. 625 (S.D.N.Y. 1996), *Jota v. Texaco Inc.*, 157 F. 3d 153 (2d Cir. 1998), *Aguinda v. Texaco Inc.*, 142 F. Supp. 2d 534 (S.D.N.Y. 2001), *Aguinda v. Texaco Inc.*, 303 F. 3d 470 (2d Cir. 2002), *Re Chevron Corporation*, 709 F. Supp. 2d 283, aff'd. *sub nom. Chevron Corporation v. Berlinger*, 629 F. 3d 297 (2d Cir. 2010), *Re Chevron Corporation*, 749 F. Supp. 2d 135 (S.D.N.Y. 2010), *Re Chevron Corporation*, 749 F. Supp. 2d 141 (S.D.N.Y. 2010), *Chevron Corporation v. Donziger*, 768 F. Supp. 2d 581 (S.D.N.Y. 2011), *Chevron Corporation v. Naranjo*, 667 F. 3d 232 (2d Cir. 2012), *Chevron Corporation v. Donziger*, 800 F. Supp. 2d 484 (S.D.N.Y. 2011), *Chevron Corporation v. Donziger*, 871 F. Supp. 2d 229 (S.D.N.Y. 2012), and *Republic of Ecuador v. Chevron Corporation and Texaco Petroleum Company*, 638 F. 3d 384 (2d Cir. 2011).

18. Paras. 250-270 of the Interim Award dated March 30, 2010.

19. Final Award dated August 31, 2011.

20. This decision was reversed on appeal, but on grounds that do not affect the substance of Judge Kaplan's determination with respect to the adequacy of the Ecuadorean proceedings and legal system.

21. Interim Order dated February 9, 2011.

22. Fourth Interim Award dated February 7, 2013.

23. Article 25(1) begins as follows: "The jurisdiction of the Centre shall extend to any legal dispute arising directly out of an investment. . .".

24. Para. 114 of the Award.

25. Paras. 125-126 of the Award.

26. Paras. 161-164 of the Award.

27. Paras. 236 and 312-319 of the Award.

28. At the time of the initiation of the UNCITRAL arbitration proceedings.

29. Paras. 7.6.1-7.6.10 of the Award.

30. Paras. 11.4.19–11.4.20 of the Award. A similar provision was found to have been violated in the *Chevron* Interim Award of March 30, 2010, mentioned in endnote 18 above.

31. See article by Mistelis cited in endnote 15 above.

32. See the *Mondev* case, cited herein, at para. 77; and see paras. 177-186 of the Interim Award on Jurisdiction dated December 1, 2008 in *Chevron Corporation and Texaco Petroleum Co. v. Ecuador*, PCA Case no. 34877.

33. It is true that international investment arbitration may be considered "intergovernmental" in nature, and its decisions and awards are typically made public, and therefore it may be viewed as a superior animal and closer in nature to court proceedings than regular commercial arbitration: *cf. National Broadcasting Co. v. Bear Stearns & Co.*, 165 F. 3d 184, 189-190 (2d Cir. 1999); but such tribunals generally are, and should be, aware that they may be viewed as consisting of "unknown" academics and lawyers that exercise "anonymous" or "secret" government, and whose decisions constitute the exercise of "sweeping powers" with "broad impact": see "Nafta's powerful little secret", New York Times, March 11, 2001, Section 3, page 1. This includes passing judgment on the judicial system or proceedings of a State.

34. In this context, an alleged perception that ICSID investment arbitral tribunals may be biased against developing countries has led three countries - Ecuador, Bolivia and Venezuela – to denounce the ICSID Convention.

35. See [1934] PCIJ Rep. Series A/B No. 63, para. 82 of the Award.

36. And see Potesta, "Legitimate Expectations in Investment Treaty Law: Understanding the Roots and the Limits of a Controversial Concept", 28 ICSID Review – Foreign Inv. L.J. 88, 118 (2013): "Tribunals have observed that the investor's legitimate expectations must relate to the specific characteristics of the investment environment in the host State. It would seem quite obvious that what an investor can legitimately expect. . . . cannot be the same in a highly developed country as it is in a developing or emerging economy".

37. Para. 5.2.18 of the Award.

38. *Loewen* Award, para. 137, already cited. ■

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