

# TheArbiter

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## Spotlight on Poland

by Adam Zwierzyński

### Poland Today — Facts and Figures

Foreign investors are increasingly casting a keen eye over Poland.

This article looks at Poland today, and explores the Polish legal framework for dispute resolution and arbitration.

Many will recall the iconic images of the revolutions of 1989, when Poland shook off the shackles of Communism. The victory of the *Solidarność* party in Parliamentary elections 21 years ago heralded the fall of Communism in Eastern Europe, and paved the way for a remarkable, indeed monumental, transformation of Poland. The advent of modern democracy left behind state-owned property and a centrally planned economy in favour of a free market economy. Poland's next milestones were accession to NATO in 1999, and to the European Union in 2004.

Today, in terms of GDP per capita (at PPP, or 'purchasing power parity')<sup>1</sup>, Poland ranks as the 6th largest economy in the European Union and the 20th globally. It is the only European country to have avoided recession during the recent financial crisis.<sup>2</sup>

In a 2008 report, Ernst & Young concluded that Poland was the most attractive destination for new foreign investment in Europe.<sup>3</sup> The country definitely deserves attention as a venue for potential investments. Poland represents a relatively large market of 38 million consumers, located in the heart of continental Europe. It is part of the trans-European road network and offers access to 250 million

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<sup>1</sup> [http://en.wikipedia.org/wiki/List\\_of\\_countries\\_by\\_GDP\\_\(PPP\)](http://en.wikipedia.org/wiki/List_of_countries_by_GDP_(PPP)).

<sup>2</sup> [http://www.bloomberg.com/apps/news?pid=newsarchive&sid=apz\\_BEuHrNpl](http://www.bloomberg.com/apps/news?pid=newsarchive&sid=apz_BEuHrNpl)

<sup>3</sup> <http://www.haga.polemb.net/index.php?document=139>

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consumers within a 1,000 kilometers radius. Poles are, in my view rightly, described as hard working and diligent — as the Organisation for Economic Co-operation and Development noted in a 2004 publication.

Poland's post-Communist legacy is that it still has an underdeveloped road, rail and infrastructure network. However, this is changing rapidly thanks to the influx of capital from EU Structural Funds. Huge highway and express roads construction projects are underway countrywide. More than 700 km are currently under construction. Main rail tracks are being modernized. Warsaw in particular is seeing a number of infrastructure projects. Most notably, a second line for the city's underground system is currently under construction, with the cost of the project exceeding £1 billion. Work obviously flows from this: for example, Chadbourne & Parke's Warsaw office recently acted in a successful Court case for the winning bidder in the tendering process.

The construction sector, as well as the Polish economy as a whole, also benefits from Poland co-hosting the 2012 European Football Championships. Six new stadia are presently being built, as well as many additional construction and development projects in the hotel, gastronomy and recreation industries.

In addition to infrastructure works, manufacturing of electronic consumer products is a strong sector in Poland. Since 2008 Poland has been the largest producer of home appliances in Europe.<sup>4</sup> Major manufacturers, including BSH Bosch and Siemens Hausgeraete GmbH, Indesit Company, Whirlpool, LG and Electrolux, have a base in Poland. There are also many domestic companies. In 2010, 77% of all LCD flat screens manufactured in European Union came from Poland.<sup>5</sup>

The government's plans to adopt the Euro (currently envisaged for around 2015) helps Poland in its bid to increase its reputation as a great place for business and new foreign investment.

### The Legal Framework — Arbitration and Dispute Resolution

Of course, foreign investors will be interested in the legal framework. Polish law is favourable to foreign entrepreneurs. The government offers investors various forms of state aid, such as: corporation tax at a flat level of 19%, investment incentives in 14 'Special Economic Zones' (among others: income tax exemption, real estate tax exemption, competitive land prices), several industrial and technology parks, and possible benefits from the EU's Structural Funds.

Disputes are a fact of life in business. Investors considering Poland may therefore be interested to learn about the Polish legal framework for resolving commercial disputes through

<sup>4</sup> <http://www.paiz.gov.pl/sektory/agd>.

<sup>5</sup> <http://www.paiz.gov.pl/sektory/elektroniczny>.

arbitration. This remains a popular form of alternative dispute resolution.

Some key features of the Polish arbitration framework include two main permanent Courts of Arbitration. We will explore below the rules regarding enforcement of arbitration awards in Poland, and will review the most recent initiative of the Polish arbitration society, the Code of Good Practices for Arbitration.

Poland is a civil law jurisdiction. Consequently, the rules governing arbitration have been codified as a separate part of the Polish Code of Civil Procedure ("CCP").<sup>6</sup> The current version of the CCP's arbitration rules were brought into force in 2005. At the time, it was decided that arbitration should be universally, and comprehensively, regulated in the CCP. Until then, the provisions relating to arbitration had been scattered across different areas of the CCP, and were not as developed and detailed as they are now.

The approach that Polish law has taken to the regulation and supervision of arbitration for the last five years follows the UNCITRAL Model Law on International Commercial Arbitration of 1985 (the "Model Law"). The CCP seeks to promote arbitration as a dispute resolution method in the widest sense<sup>7</sup>, and provides for a significant amount of party autonomy.

One notable feature of the 2005 arbitration provisions was the abolition of the old Article 1105 § 2 of the CCP. This was an anachronistic provision that prevented parties domiciled in Poland from agreeing to arbitrate purely domestic disputes, with no international element, in front of any foreign arbitration tribunal not seated in Poland. This restriction now no longer applies in commercial transactions.

### What Can Be Arbitrated?

Save where there is a specific provision of law<sup>8</sup> to the contrary, under Polish law the parties may submit a wide range of disputes to arbitration. In general, the test for arbitrability is whether the dispute could be settled before a state Court. In other words, is the dispute about rights or obligations that could be freely disposed of by one or the other party? The Polish Supreme Court confirmed in May 2010 that this test applies to both monetary and non-monetary claims (see Decision of 21 May 2010, // CSK 670/09).

<sup>6</sup> Articles 1154-1217 of CCP, further divided into sub sections - General provisions (Title 1 – Art. 1154-1160), Arbitration clause (Title 2 – Art. 1161- 1168), Arbitration Tribunal's composition (Title 3 – Art. 1169-1182), Jurisdiction of the Arbitration Tribunal (Title 4 – Art. 1180-1182), Arbitration proceedings (Title 5 – Art. 1183-1193), Arbitration award and completion of the proceedings (Title 6 – Art. 1194-1204), Challenging the award (Title 7 – Art. 1205-1211) and Recognition and enforcement of the award or settlement concluded in arbitration (Title 8 – Art. 1212-1217).

<sup>7</sup> See the grounds for the bill on amendment of the Code of civil procedure in the part regarding arbitration of 2005.

<sup>8</sup> All references to the "law" or "provisions of law" refer exclusively to statutory provisions contained in Parliamentary Acts.

When it comes to commercial, contractual disputes, however, arbitrability is generally as wide as one would expect. It extends to claims for breach of contract, tort claims, fraud claims, claims relating to the existence or validity of a contract or any other claims that are related to the contract. To illustrate this, the Supreme Court has said the following about an arbitration clause that was narrowly worded (5 February 2009, I CSK 311/08):

*“... submitting disputes that arise out of a contractual relationship to arbitration means that the arbitration tribunal is competent to hear any and all claims for performance of the contract, claims resulting from non-performance or improper performance of the contract, claims for restitution in the event of nullity or rescission of the contract, as well as claims based on tort, when they arise from an instance of non-performance or improper performance of a contract...”*

Finally, it should be noted that under Polish bankruptcy law, any arbitration agreement becomes automatically void if the relevant company becomes bankrupt. No new arbitration proceedings can be commenced against a bankrupt company, and existing arbitrations will be deemed discontinued (see Articles 142 and 147 of the Bankruptcy and Restructuring Law).

## The Arbitration Agreement

In line with internationally accepted principles, submitting any dispute to arbitration requires the agreement of the parties. The agreement should indicate the subject matter of the dispute, or the legal relationship from which the dispute has arisen or can arise.<sup>9</sup>

An arbitration agreement should be concluded in ‘writing’. That requirement is also met if the agreement is found in letters exchanged between the parties, or in declarations made by them. Provisions of any arbitration agreement that violate the principle of equality of the parties, in particular by authorising one party only to bring its statement of claim either to an arbitral tribunal or to a court, are ineffective.

Where a party submits a case to the Polish Courts that relates to a dispute which falls within the scope of an arbitration agreement, the Courts are required to decline jurisdiction provided that the objecting party has pleaded the arbitration agreement before making any submissions as to the merits of the case.

## Setting Aside and Enforcement of Arbitral Awards

A party who has obtained a favourable arbitral award will want to be assured that the award can be enforced. Polish law provides that assurance, in line with international norms.

<sup>9</sup> A literal translation of the term used in Polish would be closer to (but not identical with) the term “submission to arbitration” as used in the UNCITRAL Model Law.

Any arbitral award rendered in Poland may only be set aside in Court proceedings brought specifically for that purpose, and where any of the specific grounds listed in the CCP apply. In summary, these grounds include an absence, or invalidity, of the arbitration agreement, or where a party was deprived of the opportunity to defend its rights.

It is also possible to challenge or resist enforcement of an award because it contradicts the legal order of Poland — essentially the same as the ‘public policy’ exception found in the New York Convention. The Polish Courts have stated on a number of occasions that judicial review of arbitral awards should be limited, and that awards should only be set aside if there have been clear violations of basic values of ‘the legal, political or economic order’ or of fundamental principles. That said, there remains some uncertainty as to precisely how the public policy exception might be applied in a given case.

Looking at enforcement in a little more detail, the changes to the CCP introduced a much simplified procedure for enforcement of arbitral awards and settlements, both domestic and international. Poland is a party to the New York Convention of 1958<sup>10</sup>, and the provisions of the CCP largely follow, and supplement, the Convention rules. Both arbitral awards, and amicable settlements made before the arbitral tribunal, are as effective as a judgment of the national Courts, once they have been recognised or declared as enforceable by the Polish Courts.<sup>11</sup>

A party applying to the Polish Courts for a declaration of enforceability or recognition should submit to the Court:<sup>12</sup>

- (a) the original, or a copy certified by the arbitral tribunal, of the award or an officially certified copy of the settlement made before the arbitral tribunal;
- (b) the original or an officially certified copy of the arbitration agreement;
- (c) if an arbitral award or a settlement made before the arbitral tribunal are not in the Polish language, a certified translation into the Polish language.

The Court will then decide the question of enforceability during a closed session (for domestic instruments) or at a public hearing (for foreign instruments). The parties may, generally, appeal the ruling.

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<sup>10</sup> Convention on the Recognition and Enforcement of Foreign Arbitral Awards adopted in New York on 10 June 1958, Poland’s accession on 3 October 1961.

<sup>11</sup> 1212 CCP.

<sup>12</sup> 1213 CCP.

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Recognition, or a declaration of enforceability of an award or a settlement *must* be refused if either of the following grounds apply:<sup>13</sup>

- (a) the dispute was not capable of being referred to arbitration as a matter of law;
- (b) the award or settlement would contravene principles of the Polish public order — the ‘public policy exception’.

The Court is obliged to investigate whether any of these grounds are made out *ex officio*, even if the parties do not raise these issues.

When it comes to foreign awards or settlements, there are a limited number of additional grounds the parties can raise before the Court when resisting enforcement or recognition:<sup>14</sup>

- (a) There was no arbitration agreement, or the arbitration agreement is invalid or ineffective under the law applicable;
- (b) The relevant party was not informed of the appointment of arbitrator, of the arbitral proceedings, or was otherwise unable to argue its case before the tribunal;
- (c) In making the award, the tribunal exceeded its jurisdiction and dealt with matters which were not contemplated to be referred to arbitration. However, if it is possible to separate the part of the award that did not exceed the tribunal’s jurisdiction, then that part will be enforceable.
- (d) The composition of the arbitral tribunal, or the conduct of the proceedings, were contrary to the agreement of the parties, or (failing any such agreement), were in contravention of the law of the place where the arbitration proceedings took place.
- (e) The arbitral award has not yet become binding upon the parties, has been set aside or declared unenforceable by the competent court (of the state where the arbitration proceedings took place).

The foregoing circumstances are only taken into account upon the party’s initiative and evidence produced thereby.

### Permanent Courts of Arbitration

In addition to an arbitration-friendly legal framework, Poland also offers arbitral institutions — or ‘permanent courts of

arbitration’ — to oversee arbitral proceedings. There are, in fact, over 40 permanent courts or institutions in Poland: in this article, we describe two of the main ones, SAKIG and Lewiatan.

#### SAKIG

The Court of Arbitration (‘SA’) at the Polish Chamber of Commerce in Warsaw (‘KIG’) (hence the Polish abbreviation ‘SAKIG’) is the largest and the best-known institution of its type in Poland. SAKIG has a long history. It has operated since January 1, 1950, as an independent entity charged with the amicable settlement of commercial disputes. Every year it deals with 400-500 cases, and its caseload is the largest for this part of Europe. In its 60 year history, SAKIG has seen the conclusion of around 10,000 disputes.

SAKIG deals with both national and international disputes, and provides both arbitration and mediation services. Nearly 20% of the cases heard before SAKIG have an international element. The Court of Arbitration handles proceedings on the basis of the well-known UNCITRAL Rules of Arbitration, and has close relationships with many other arbitral institutions the world over — for example, within the framework of the International Federation of Commercial Arbitration Institutions and the ICC’s European Arbitration Group. The average value of a case before the SAKIG Court is presently close to €500,000.

#### Lewiatan Court of Arbitration

The most recent alternative to SAKIG is the Court of Arbitration established by the Polish Confederation of Private Employers, ‘Lewiatan’. The Lewiatan Court was created in Warsaw in 2005. It was formed to be a modern alternative institution to SAKIG. Two of the strong features of the Lewiatan Court are flexible procedural rules and a focus on creating a body of arbitral jurisprudence to give insight into the workings of tribunals appointed before the Lewiatan Court. To assist with the latter, Lewiatan publishes a free electronic arbitration review, with publications by eminent arbitration authors. The fees of the Lewiatan Court are also generally lower than those of SAKIG (both are calculated by reference to the value of the dispute).

In May 2010, the Lewiatan Court adopted a fast track procedure for smaller cases (around £10,000) as part of its rules, something that is unique in the Polish arbitration community. The distinctive features of the fast-track procedure are adjudication by a single arbitrator, electronic service, a one-day hearing and the aim to complete the proceedings in 8 weeks. This procedure is envisaged as a dispute resolution tool for small entrepreneurs.<sup>15</sup>

<sup>13</sup> 1214 CCP.

<sup>14</sup> 1215 CCP.

<sup>15</sup> Fast - track, czyli arbitraz przyspieszony po polsku - dr Andrzej W. Wisniewski, e-Przegląd Arbitrazowy nr 2/2010.

## Code of Good Practice of Permanent Arbitration Courts

One of the most recent initiatives in Polish arbitration came from the Polish Arbitration Association ('PAA')<sup>16</sup>, which after a long debate, in May 2010 adopted a draft "Code of good practice of permanent arbitration courts." The Code was produced to improve the organisation and operation in practice of Poland's permanent courts of arbitration. It does not contain any specific procedural rules for the conduct of arbitration proceedings, but instead sets out guidelines for arbitration courts, as regards their statutes and rules.<sup>17</sup>

One central recommendation of the Code is that any arbitration court, a judicial body, should be impartial and fully independent from any other institution with which it might have been associated, or which might have established the relevant arbitration court. Such independence should extend to the court's own statutes and rules, and the appointment of the members of any panel.<sup>18</sup>

The Code seeks to make arbitration proceedings more transparent<sup>19</sup>, and to that end recommends that hearings should be recorded, and that arbitral awards should be publicised (on an anonymous basis, with the names of the parties redacted). The belief is that publishing awards should contribute to ensuring that they are of high quality, and may serve to publicise arbitration among businessmen and also increase awareness of the relevant institutions. The President of the PAA panel which drafted the Code, Prof. Tomasz Siemiatkowski<sup>20</sup>, has commented that the "aura of secrecy which hitherto surrounded [arbitration] cannot be properly justified".

The Code also calls for clarity when it comes to the costs of the arbitration<sup>21</sup>, proposing that the system for calculating costs should always be objective and independent of the outcome of the case. In a perhaps more challenging recommendation, the Code recommends that arbitral institutions or courts should be not-for-profit organisations, so that the fees levied

<sup>16</sup> The Polish Arbitration Association was established in 1990. A member of the Association can be any individual interested in arbitration and alternative dispute resolution. The main purposes of the Association are: to promote the development of alternative dispute resolution and particularly, arbitration in the resolution of disputes arising between economic organizations both in Poland and in international relations, conducting research on and popularization of Polish and foreign laws on arbitration, maintaining contacts with scientific centers, permanent arbitration courts and other institutions interested in the development of arbitration organization of lectures, conferences and congresses devoted to arbitration. [http://www.pssp.org.pl/a\\_index.htm](http://www.pssp.org.pl/a_index.htm)

<sup>17</sup> Code Article 2.

<sup>18</sup> Code Article 3.

<sup>19</sup> Code Article 4.

<sup>20</sup> in: *Commercial arbitration to be more transparent*, Marek Domagalski, Rzeczpospolita, 23rd April 2010.

<sup>21</sup> Code Article 5.

should only cover the remuneration of the arbitrators and the actual costs of the institutions.

"We do not hide that motives for commencement of the works on the Code are the experiences of the critical voices against arbitration" explained Mr. Sylwester Pieckowski, President of the PAA and a partner in Chadbourne & Parke's Warsaw office.<sup>22</sup> The impact of the Code remains to be seen. It is currently being studied by the major permanent courts of arbitration. ©

## Recent Decisions of the Constitutional Court of Ecuador Regarding Arbitration

by Luis Enrique Graham and Salvador Fonseca



### Arbitration According to the New Constitution

The 2008 Ecuadorian Constitution introduced significant changes to its arbitration regime. The new Constitution introduced two articles concerning arbitration.

Article 190 reads:

*Article 190 — Arbitration, mediation and other alternative methods for dispute resolution are recognized. These proceedings shall be applied in accordance with the law on matters where, by reason of their nature, it is possible to compromise.*

*Arbitration at law shall apply on public contracting upon a prior favorable opinion from the Attorney General of the State pursuant to conditions set forth in the law.*



This gives constitutional status to arbitration, recognising it as a legitimate means for dispute resolution. Article 422, however, introduces uncertainty:

*Article 422 — It shall not be possible to enter into international treaties or instruments in which the Ecuadorean State waives sovereign jurisdiction to international arbitration venues in contractual or* / continued page 6

<sup>22</sup> in: *Commercial arbitration to be more transparent*, Marek Domagalski, Rzeczpospolita, 23rd April 2010.

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*commercial disputes between the State and private individuals or corporations.*

*Excepted from the foregoing are international treaties and instruments providing for dispute resolution between States and citizens of Latin America by regional arbitral venues or by jurisdictional organizations designated by the signatory countries. Judges from the states that as such or as nationals of those states are parties to the dispute cannot participate.*

*In the case of disputes relating to the foreign debt, the Ecuadorean State shall promote arbitral solutions in terms of the origin of the debt, subject to principles of transparency, equity and international justice.*

Article 422 prevents Ecuador entering any treaty that provides for international arbitration to settle *commercial* disputes between the Ecuadorian government and private entities.

### Recent Decisions of the Constitutional Court

This year, Ecuador sought rulings from its Constitutional Court on the constitutional validity of more than 12 bilateral investment treaties (BITs) which Ecuador had entered between 1990 to 2000 (including one with China and one with the United Kingdom).

All provided for arbitration between foreign investors and Ecuador. The intention is to obtain a judicial decision stating that BITs violate Article 422 of the new Constitution, as a preliminary step to the denunciation of said treaties. The decisions issued so far by the Constitutional Court have declared those BITs unconstitutional.

These decisions are concerned only with BITs, but the reasoning in those decisions is not clear enough to dissipate the concern that commercial arbitration involving public entities in Ecuador is outlawed by the new Constitution, particularly in light of the court's expansive statements regarding sovereignty being incompatible with arbitration.

### Secondary Legislation Regarding Arbitration of Commercial Disputes Involving Ecuador as a Party

On October 14, 2010, as a response to critics and to ease the growing concern, the Legislative Assembly issued the "Public Planning and Finance Code"<sup>1</sup>, which contains the following provision:

*...[W]ith the prior authorization of the General Attorney it is permitted to accept other jurisdiction and laws for the solution of divergences or controversies connected with contracts, agreements or legal instruments executed by the*

*State and the entities or organs of the public sector with foreign governments, public or private entities.*

Some critics have expressed skepticism regarding the effectiveness and constitutional validity of this provision in the light of the prohibition contained in the article 422 of the Constitution.

### Additional Recent Events and Final Comment

Despite the Constitutional Court declaring the BIT with China unconstitutional, the Ministry of Finance of Ecuador recently entered a major contract to sell 36,000 barrels of oil a day to the Chinese government for the next four years, and this included an LCIA arbitration clause. Furthermore, Ecuador's Finance Minister recently declared that, in his opinion, "[LCIA resolutions] are very flexible and neutral"<sup>2</sup>.

It will be necessary to observe future developments closely in order to better understand the effects of the Constitutional Court decisions on Ecuador's arbitration regime, particularly regarding the validity of arbitration clauses in commercial contracts to which Ecuadorian public entities are parties. ©

## JURISDICTIONAL HURDLES IN INVESTMENT TREATY ARBITRATIONS

# 'Catching the Quango' — State Responsibility for Actions of Public Bodies

by Melanie Willems



### Introduction

Over the past twenty years, foreign investors who have suffered losses as a result of the actions of the host state where their investments were made have increasingly resorted to investment treaty arbitrations to seek to recover their losses. Such proceedings are brought under a network of bilateral investment treaties ('BITs') that spans the globe.

Through BITs, both state parties to the relevant treaty frequently agree to the submission of disputes between one state party and investors domiciled in the other to arbitration before

<sup>1</sup> Código de Planificación y Finanzas Públicas.

<sup>2</sup> See [www.elnuevoempresario.com/noticias\\_25956\\_patricio-rivera-aclara-que-ecuador-no-pagara-con-petroleo-prestamo-con-china.php](http://www.elnuevoempresario.com/noticias_25956_patricio-rivera-aclara-que-ecuador-no-pagara-con-petroleo-prestamo-con-china.php) and [www.eluniverso.com/2010/09/04/1/1356/prestamo-chino-hara-garantia-petrolera.html](http://www.eluniverso.com/2010/09/04/1/1356/prestamo-chino-hara-garantia-petrolera.html).

an international arbitral tribunal. The tribunal will apply principles of international law to determine whether the host state has acted in breach of its obligations to protect the investment: key principles include fair and equitable treatment of investors; non-discrimination as between foreign investors and domestic businesses (or those from a ‘most favoured nation’); and a prohibition on expropriation, or nationalisation, of assets without payment by the state of effective compensation.

The International Centre for the Settlement of Investment Disputes (‘ICSID’) established under the Washington Convention 1965, oversees investment treaty arbitrations. ICSID provides a procedural framework and arbitration rules, and also offers a panel of qualified arbitrators from which appointments can be made. Arbitral tribunals appointed under BITs wield considerable power. Though they are private individuals, they can (and routinely do) order sovereign states who have breached their international law obligations to pay hundreds of millions in damages to claimants. In practice, many ICSID awards are honoured by respondent states.

### ‘State Responsibility’ — The ICSID Convention

Having overcome the jurisdictional hurdles as regards the identity of the claimant and the nature of the investment, the respondent must (perhaps stating the obvious) be the correct state entity: that means a state which is a party to the relevant BIT. The BIT must also have been ratified, and it must be in force (there are some that have been signed but were never brought into force).

To illustrate a rather straightforward scenario, assume a state passes a law or enacts a presidential decree that, with immediate effect, the investor’s business and assets in the jurisdiction are nationalised without any compensation being paid to the investor. Here, it is easy to see that the state will have acted in its own right, through its legislature or the executive arm of the government. It must be responsible for these actions. But where the investor deals with an agency or body that exercises some public functions, but is not a government department or ministry, one enters a legal grey area where it is not always clear cut if the state itself will be responsible.

As noted, many BITs provide in their dispute resolution provisions that an investor may refer a claim to arbitration under the ICSID Convention. The ICSID Convention deals with jurisdiction in Article 25. That provision confirms that it is not only states that may be a party to such arbitrations, but also their ‘subdivisions and agencies’ (a term that is not further defined):

#### ‘ARTICLE 25

*(1) The jurisdiction of the Centre shall extend to any legal dispute arising directly out of an investment, between a Contracting State (or any constituent subdivision or agency of a Contracting State designated to the Centre by that State) and a national of another Contracting State, which*

*the parties to the dispute consent in writing to submit to the Centre. When the parties have given their consent, no party may withdraw its consent unilaterally.”*

As is apparent from Article 25(1), where the proposed respondent is a ‘subdivision or agency of a state’, it must have been so designated (by notification to ICSID) by the state in question. This important proviso is expressly noted in Article 25(3), which explains that:

*“(3) Consent by a constituent subdivision or agency of a Contracting State shall require the approval of that State unless that State notifies the Centre that no such approval is required.”*

The requirement for consent by the state cannot be overridden by any contractual agreement by a ‘subdivision or agency’. This important limitation was illustrated in the recent *Hamester v Ghana* award. Hamester was a German company engaged in the international cocoa trade and the processing of cocoa products. Its predecessors had entered a joint venture agreement with the Ghana Cocoa Board. The Board had been established pursuant to a local law (the Ghana Cocoa Board Law), which assigned to the Board a number of functions and activities such as promoting the Ghanaian cocoa industry — the relationship between these parties is discussed in more detail below. For present purposes, the joint venture agreement included the following ICSID arbitration provision:

*“Where any disputes arise between the parties hereto which cannot be amicably settled, then the dispute shall be referred to the International Centre for the Settlement of Investment Disputes.”*

Despite the fact that the Board had voluntarily accepted that ICSID should have jurisdiction, Ghana had never given its consent that the Board was a subdivision or agency as required under Article 25 of the ICSID Convention. A dispute arose, and the claimants in *Hamester* filed a request for arbitration with ICSID on the basis that the Board satisfied Article 25. This request was rejected by the ICSID Secretariat in the absence of the required consent by Ghana.

This requirement for notification or designation has been criticised. An investor might genuinely believe that he or she had secured a contractual undertaking that an investment treaty would apply, given by an ‘official’ body connected to the relevant state or government, while in truth the state remains free not to designate the relevant body under the ICSID Convention. By way of analogy with the English law of agency, for the purpose of conferring jurisdiction under the ICSID Convention itself a state would not be bound by the apparent authority of the relevant public body, whereas a principal under English law could be bound if they allowed someone to hold themselves out as being duly authorised to bind the principal.

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## State Responsibility

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That is not, however, the end of the matter. Public international law recognises that in certain circumstances, states can nevertheless be responsible for the actions of connected entities. A tribunal reviewing jurisdiction in any ICSID or BIT claim will therefore be able to find that, irrespective of the lack of consent given by a state under Article 25 of the ICSID Convention, nonetheless the state is responsible for the acts of the relevant public body.

### State Responsibility — Public International Law

ICSID tribunals, including the arbitrators in the *Hamester* decision, apply the public international law principles of ‘attribution’, or ‘state responsibility’, in order to determine whether a state must stand behind any ministry, organisation or body. By virtue of entering the BIT, the state has consented not only to the jurisdiction of ICSID (assuming the BIT contains a relevant article to that effect), but it has also accepted that the rules of public international law will apply in any claim brought by an investor under the BIT in question. Those rules include the principles of state responsibility that are reviewed below.

Public international law is often unwritten and determined by the custom or actions of states. However, in this particular area it is considered to have been codified through a Resolution of the United Nations General Assembly. The International Law Commission’s Articles on State Responsibility (the ‘Articles’) were adopted by the General Assembly in December 2001, through Resolution 56/83. As the tribunal in *Hamester* noted, this was a “codification of customary international law” (see paragraph 171). The Articles may very well be applied by future BIT tribunals when a question of state responsibility or attribution falls to be decided.

The key provisions are found in Articles 4, 5 and 8, which set out three distinct bases on which conduct can be attributed to a state under international law:

- Where the actor is an ‘organ’ of the state.
- Where the actor is ‘a person or entity exercising elements of governmental authority’.
- Where the conduct in question is directed or controlled by the state.

#### *Organs of the state*

A state is responsible for the consequences of any act of one of its ‘organs’, provided of course that such an act is in contravention of international law and the BIT. The Articles state:

##### **“ARTICLE 4**

##### **Conduct of organs of a State**

1. *The conduct of any State organ shall be considered an act of that State under international law, whether the*

*organ exercises legislative, executive, judicial or any other functions, whatever position it holds in the organization of the State, and whatever its character as an organ of the central government or of a territorial unit of the State.*

2. *An organ includes any person or entity which has that status in accordance with the internal law of the State.”*

The International Court of Justice has defined ‘organs of the state’ as follows (see *Bosnia and Herzegovina v Serbia and Montenegro, Genocide Case*, Judgment of 26 February 2007, para. 384):

*“... persons or entities whose conduct is necessarily attributable to [the state], because they are in fact the instruments of its actions.”*

State ‘organs’ would include the legislature, the executive (government ministries or departments), the judiciary, military and police forces, security services, state officials (holders of public office) in general. A state is also responsible for the acts of provinces, or the constituent territories of a federation or dependent territories, and any of their organs. Under international law, a state cannot plead its own constitution or municipal laws — insofar as they purport to show that a municipality or province are separate from the state — by way of defence and so as to avoid responsibility (see *Brownlie, Principles of International Law, 7th Edition*, page 451 and the authorities cited there).

As Article 4.2 makes clear, what is a state organ is a question to be decided by applying the internal laws of the state, such as its constitution and other relevant acts of the legislature. The ICSID tribunal in the *Hamester* case explained that (paragraph 182):

*“An organ is part of the structure of the State itself, whether its central organisation (i.e. its legislative, executive or judicial structures), or decentralised organisation (e.g. territorial entities such as federated States; provinces; municipalities; etc.). In the present case, it is clear that the Tribunal has jurisdiction over the acts of the Ministers and over the acts of the police, which are part of the executive power of the Ghanaian State.”*

It does not matter that the ‘organ’ of the state acts in the commercial sphere and is carrying out a business function (sometimes called *acta iure gestionis*) rather than being engaged in acts of a governmental nature (*acta iure imperii*). Responsibility for **all** acts will be imputed to the state.

Similarly, where the acts of the organ in question are *ultra vires* and go beyond the scope of their authority, the state could still be responsible. This appears, for instance, from the *Youmans* decision (an arbitration award made by the U.S. / Mexico Claims Commission, November 1926): Mexican sol-

diers had been ordered to protect American nationals who were under siege by rioters, but instead joined in their killing. Although the acts did not follow a state decision or instruction, Mexico was nonetheless ordered to pay reparations to the U.S. In another decision, the Caire award (1929), the Claims Commission explained further that in order to justify “*objective responsibility*” on the part of the state for *ultra vires* acts, the officials or organs “*should have acted, at least apparently, as authorized officials or organs, or that, in acting, they should have used powers or measures appropriate to their official character...*”. Arguably, the decision in the *Youmans* case went quite far in light of this statement of principle.

#### ***Persons or entities exercising governmental authority***

A state will also be responsible for the acts of persons or entities that exercise governmental authority, if such authority has been delegated to them. The Articles provide:

##### **“ARTICLE 5**

##### ***Conduct of persons or entities exercising elements of governmental authority***

*The conduct of a person or entity which is not an organ of the State, under article 4 but which is empowered by the law of that State to exercise elements of the governmental authority shall be considered an act of the State under international law, provided the person or entity is acting in that capacity in the particular instance...*”

Article 5 is concerned with legal entities that exist independently of the state, such as corporate bodies or even private individuals. The state will not, however, be responsible for **all** the acts of entities to which governmental power might have been delegated, under this rule. In the Commentaries to the Articles, Professor Crawford explains that entities that could be caught by Article 5:

*“(a) ... may include public corporations, semi-public entities, public agencies of various kinds and even, in special cases, private companies, **provided that** in each case the entity is empowered by the law of the State to exercise functions of a public character normally exercised by State organs, and the conduct of the entity relates to the exercise of the governmental authority concerned.”*

The Commentaries also set out some examples of entities that fall within Article 5:

- Private security firms contracted to act as prison guards, exercising powers of detention in relation to a judicially-imposed prison sentence.
- Airlines, state-owned or even private, to which a state has delegated powers of immigration or quarantine.
- Railway companies may have been given certain police powers.

Where these entities act otherwise than in the exercise of their governmental powers or public duties, state responsibility under the Articles will *not* be engaged. So if a state-owned airline breaches a contract of carriage or freight, that remains a matter to be resolved under the applicable law of the contract, but not public international law — and that would be so even if the airline in question is wholly owned by the state and enjoys a total monopoly (so that the counterparty would have had no choice but to deal with this particular entity for relevant services in the territory in question). Here, international law does draw a distinction between *acta iure gestionis* and *acta iure imperii*.

That distinction is also reflected in English law. In *C. Czarnikow Ltd v Centrala Handlu Zagranicznego* [1978] QB 176, the Court of Appeal found that the Polish state trading agency ‘Rolimpex’ was not to be equated with the Polish government or state. The Polish state had authorised Rolimpex to export sugar, since in line with the expected demand for the centrally-planned Polish economy for particular years there would be a surplus. Czarnikow contracted to buy the sugar but Rolimpex failed to deliver. Under the arbitration rules (of the Refined Sugar Association) that were incorporated into contract, Rolimpex would not be liable if performance of its obligations became impossible due to *force majeure*, which included government intervention. Rolimpex failed to perform its contractual obligations, and sought to rely on the acts of the Polish state.

Lord Denning rejected the argument that Rolimpex was, for all intents and purposes, the Polish state in another guise, even though in a centrally-controlled economy, Rolimpex had little or no independence when it came to making commercial decisions. He said:

*“I do not think that Rolimpex can be considered to be a department of the Government of Poland... Rolimpex is a State trading agency.”*

#### ***Conduct directed or controlled by the state***

State responsibility can also arise where the conduct in question is directed or controlled by the state. This is dealt with in Article 8:

##### **“ARTICLE 8**

##### ***Conduct directed or controlled by a State***

*The conduct of a person or group of persons shall be considered an act of a State under international law if the person or group of persons is in fact acting on the instructions of, or under the direction or control of, that State in carrying out the conduct.”*

International law applies a high threshold here, in the form of the ‘effective control’ test (see *Nicaragua v United States*, ‘*Contra Case*’, Merits, Judgment of June 27, 1986, ICJ Reports 1984).

*/ continued page 10*

## State Responsibility

*continued from page 9*

Clear evidence of actual control or direct influence by public officials would be needed to discharge the evidential burden.

### Illustrations — ICSID Awards in Hamester and Jan De Nul

How these principles are applied by international arbitral tribunals is illustrated by the decisions in *Hamester* and in *Jan De Nul*, an award published in November 2008 (*Jan de Nul NV Dredging International NV v Arab Republic of Egypt*, ICSID Case No ARB/04/13). In both cases, the tribunals found that the state was not responsible for the actions of bodies which, at first glance, might appear to be closely connected to the state.

In *Hamester*, the claimant sought to hold Ghana responsible for certain actions of the Cocoa Board. In its submissions to the tribunal, the claimant sought to convince the tribunal that the Cocoa Board was “a monopolistic statutory public body with administrative responsibility for controlling and regulating the cocoa industry in Ghana...” (paragraph 150). The gist of the submissions was that the Cocoa Board was an organ of the state, since it had been created by legislation. That legislation gave the competent minister the power to give directions to the management of the Cocoa Board. Article 32 of Law 1984 provided:

*“The Minister [responsible for Trade] may after consultation with the Board of Directors or the Management, give the Board in writing directions of a general character not being inconsistent with the provisions of this Law or with the contractual or other legal obligations of the Board relating to the exercise of the Board of its functions under this Law and the Board shall give effect to such directions.”*

The tribunal agreed with the respondent that the Cocoa Board was not an organ of the state. Under Ghanaian law (which the tribunal applied), the board was created as a separate legal entity and was to carry out its functions in a sound, commercial manner, generating a reasonable return on its capital.

Nonetheless, the Cocoa Board did have public powers and might, in principle, be an entity that was exercising governmental authority within the meaning of Article 5. The claimant suggested that the Cocoa Board had relied on such powers in negotiations concerning the price at which *Hamester* could purchase certain cocoa products and as regards the terms of the JVA. After a careful review of the evidence, the tribunal concluded that the Government, although it followed the negotiations, had not used any kind of “*puissance publique*” / public power in disregard of the rights of the investor. The negotiations had been at arm’s length throughout. The Ghanaian government had not “*imposed*” a price on *Hamester* through *Cocoabod*. When it came to the proposed exit from

the JVA (which caused protracted and difficult discussions), the tribunal concluded that:

*“283. To the Tribunal, these letters are clearly part of a general corporate battle, between the shareholders of Wamco. On one side was the majority shareholder, Hamester, which expressed a desire to withdraw from the company and whose representative (the Managing Director of Wamco) had, at a certain point in time, physically abandoned his post, and had given orders to shut down Wamco. On the other side was the minority shareholder, Cocoabod, which was trying to keep the business going. Not one of these letters contains an act of *puissance publique* which could be attributed to the State.*

*All of these letters could have been written by a frustrated private minority shareholder who was compelled to run the company, faced with the withdrawal of the majority shareholder. Corporate life is replete with such examples of shareholder disputes.”*

So while the Cocoa Board did have some public powers, Ghana could not be held responsible for all of the actions of this body. The claimants did not have the evidence needed to establish attribution either under Article 5 or 8.

The same result, that the state was not responsible for the actions of an entity that at first glance appears to be ‘public’ in nature, was reached in the *Jan De Nul* arbitration. The issue in that case was whether the actions of the Suez Canal Authority (‘SCA’) could be attributed to Egypt under either Articles 4 (organ of the state), 5 (exercising governmental authority) or 8 (controlled by the state).

The tribunal concluded that the Suez Canal authority was not an organ of the state, applying a ‘structural test’. The authority had been created to take over a nationalised activity — management and operation of the Suez Canal, overseeing and administering shipping traffic and transit. Those activities were, the tribunal noted, public in nature. However, from a structural perspective the authority was not a part of the Egyptian state. The law establishing the authority required it to follow commercial methods of management and exploitation, and it was to do so without any steer or direction from the Egyptian state. The authority also had its own budget, consisting of purely private funds.

Nor was the SCA a public body exercising governmental functions within Article 5. Article 5 required the fulfilment of two conditions:

- the relevant entity must be empowered to exercise elements of governmental authority; and
- the act itself must be performed in the exercise of governmental authority.

As to the first, the SCA was empowered to exercise elements of governmental authority, including issuing decrees related to the navigation in the canal and imposing and collecting charges for the navigation and passing through the canal. However, the second condition was not fulfilled. Although the contract was awarded through a bidding process governed by the laws on public procurement, the acts relied on were commercial rather than governmental in nature.

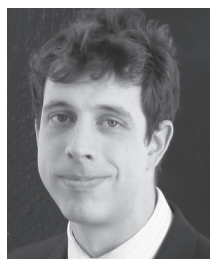
Nor was the SCA directed or controlled by the state within the meaning of Article 8. The test of “effective control” for these purposes was a very demanding one, requiring proof of both general control over the entity in question and specific control over the relevant act. The evidence failed to establish the requisite degree of control.

## Conclusion

The two ICSID awards discussed in this article show that under international law, state responsibility is not imposed lightly. It is not imposed simply because the body whose actions are under review has some public or ‘governmental’ powers. International law allows states to create separate legal entities with a commercial function, setting them up under the state’s own national law, and to offer these entities as contractual counterparties in dealings with investors. Provided that the actions complained of stay firmly within the commercial field, and the state did not ‘effectively control’ the actions, the investor may find that a BIT claim against the state is not possible. The identity of any contractual counterparty, and the appropriate dispute resolution provisions, should always be looked at closely at the time of entering into any agreement. ☺

## Update on *Oceanbulk*

By Robert Blackett



the Court of Appeal.<sup>2</sup>

In the last newsletter we discussed ‘without prejudice’ privilege, and the Court of Appeal’s majority decision in *Oceanbulk Shipping & Trading SA v TMT Asia Limited and others*.<sup>1</sup> On October 27, 2010 the Supreme Court handed down its judgment in an appeal against that decision, unanimously ruling to overturn

In a lecture earlier this year, Lord Phillips described with some enthusiasm some new practices which their Lordships had adopted since the change from Judicial Committee to Supreme Court:

*“All our proceedings are recorded by permanent cameras and it is open to the media to request any part of this record for broadcasting purposes.<sup>3</sup> When a judgment is delivered, a press release will be prepared for distribution explaining what has been decided. In addition, the judge delivering the judgment will prepare a short oral statement of its effect. Where the case is one of general public interest this is likely to be broadcast as part of the news, so that we have a valuable opportunity to give an accurate explanation of what the case has been about. You have, however, to condense the judgment into a statement about 30 seconds long. I have become quite good at this and am at risk of turning into a TV personality. Some have suggested that we should adopt a similar approach to the length of the judgments themselves.”*

This enthusiasm for clarity and concision is also apparent in the judgments themselves, and Lord Phillips’ one paragraph judgment in *Oceanbulk* is a good example:<sup>4</sup>

*“The principle to be derived from this appeal can be shortly stated. When construing a contract between two parties, evidence of facts within their common knowledge is admissible where those facts have a bearing on the meaning that should be given to the words of the contract. This is so even where the knowledge of those facts is conveyed by one party to the other in the course of negotiations that are conducted without prejudice. This principle applies both in the case of a contract that results from the without prejudice negotiations and in the case of any other subsequent contract concluded between the same parties.”*

All this makes the job of writing updates on Supreme Court decisions for The Arbitrator NewsWire a rather easy one! ☺

<sup>1</sup> [2010] EWCA Civ 79

<sup>2</sup> [2010] UKSC 44

<sup>3</sup> Fortunately for my productivity, none of these media companies has opted to provide live internet broadcasts of all this material for me to watch at my desk.

<sup>4</sup> Lord Phillips, paragraph 48.

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