II ICC Arbitration Day
VI Congress of the Brasilian Arbitration Comittee
Salvador - Bahia – 30/10/2006

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HOW TO AVOID THE "NATIONALIZATION" OF INTERNATIONAL CONTRACTS?

Contractual relations of international extent, in which one of the parties is a sovereign state and the other a private corporation from another country, are becoming increasingly frequent each day. These commercial relationships are a result of the globalization, the increase of international competition, the economic growth of less developed countries, the galloping process of technological innovation and of the reorganization of the traditional model of the State's role in the economics.

These are probably the reasons why these contractual relations are taking place in an environment that is submitted to two opposite movements. On the one hand, States, particularly the less developed ones, want to draw foreign productive investment. This attitude results from a number of reasons, such as the lack of "know-how" in major productive sectors, the shortcoming of internal resources for investment, the budget constraints which do not allow for the State to allocate needed resources for capital intensive projects, the will for diversification of dependencies, the wish to increase the competition, the intention of provoking the internalisation of technologies.

Naturally, the Governments are, therefore, willing to take initiatives that induce the investors to invest in their countries and reduce the fear of these to shift to an environment they don't know, being subject to unknown cultural structures, to exotic legal and regulatory standards and to human and social groups with whom they have few or no connection at all.

But, on the other hand, these States often look upon foreign investment with distrust and hostility. This attitude is also a result from several factors. Among them, we can mention the following facts: the younger States, or the less developed ones, quite often have unsolved problems of national unity; they are particularly zealous of their national sovereignty; they are subjected to internal economic and social

forces that look upon foreigners, sometimes, with negativity and concern; they believe (with or without enough reason) that the existing terms of trade and transfer prices drain excessive and unfair resources to the outside. And, above all, as the History of Mankind proves, the foreigners ("hostes" in Latin, expression that is in the etymological origin of expressions such as "hostil" (Portuguese) and "hostile" (English), as a synonym for enemy…) are excellent scapegoats for governmental policies' failures.

The combined action of these two contradictory movements provokes dynamics that affect foreign investment and the stability of international contracts, with generally very dangerous consequences for all parties involved.

Times of real search for foreign investment, with the important required incentives, are followed by periods of hostility and opposition towards the same kind of investment. Therefore, no foreign investor can act without keeping in mind this oscillation that, in a higher or lower scale, affects all countries, even some of the more developed World, at least in the relatively most benign way of protection and preference for national companies.

Taking all this into consideration in this text I will try to answer the following question: How can potential foreign investors reduce the risk of damage if and when political authorities change their attitude and take decisions that affect them in an illegal and/or unjustified way? And, how can they protect themselves if and when this occurs?

The first precaution should be analysing the international law of the Country in which they plan to invest. Among the signs to scrutinize are: (i) Is the State a party in international, multilateral or bilateral treaties? (ii) Will the concrete investment be protected by any of these treaties? (iii) Was the Convention of New York about the recognition of arbitral awards ratified? And without relevant reservations? (iv); Is there any track record of illegal actions, or actions causing damages which were not compensated, against foreign investors?

Afterwards, the country's legal relevant regime (referred by Anglo-Saxon authors as "municipal law") should be cautiously analysed, searching for answers to questions such as these: (i) Does a national law allowing international arbitrations exist? Does this law accept that the arbitration should take place abroad? Is the law also friendly with other relevant aspects (acceptance of foreign arbitrators, of the use of a non-national language, of the application of other national law for contracts, of the impossibility of an appeal to local courts against arbitration awards)? (iii) Do the rules that are being applied for State contracts allow the submission of disputes to an arbitral court or do they demand the subordination to national courts, namely administrative ones? (iv) Is it possible for an arbitral court to decide without appeal (except for setting aside the award on formal grounds) for local courts? (v) Is it possible (and in which conditions) to enforce arbitral decisions against the State? (vi) Is there a track record of the impossibility of enforcing arbitral or judicial decisions, in which relief has been granted against the State?

Hereafter, it should be necessary to look specifically to the juridical environment: (i) Does a legal profession exist, which actually has the liberty and courage to defend the interests entrusted to them, even if against the State? (ii) Are judicial magistrates independent towards government and are they considered to be honest and not affected by corruption practices? (iii) Is it possible for foreign law firms

to act in this market? Are there any local qualified law firms with connexions to foreign firms? (iv) In general, does “rule of law” and “due process” exist in this Country?

It’s not always possible to have positive answers to all these questions and, in spite of that, the investment can make sense from a strategic and/or commercial point of view. But obviously there’s a limit from which the investment gets clearly riskier than acceptable.

The definition of this limit shall be made on a case by case approach, as it is impossible to find a sole and standard answer. But, in general, I think there are a number of strict conditions that should be always present. In my opinion, the more important consist in (i) the acceptance by the State of the arbitrability of conflicts related with contracts of investment in which he is a party, (ii) that these contracts will accept that the place of arbitration may be abroad and (iii) that the arbitration can be submitted to rules of a credible international institution, such as ICC or LCIA, and that the arbitral process can take place in its sphere of action.

These minimum essential conditions allow to reduce substantially the capacity of manipulation of the system by one of the parties in the contract, because, after all, this is the risk we are talking about.

With the submission to arbitration, problems caused by the hypothetical lack of preparation and specialization, partiality or lack of independence of national judges will be solved. The localization outside the national State allows for the protection of the arbitration process from procedural national rules that “pollute”, often too much, arbitral proceedings and also to withdraw the capacity to interfere in arbitrations, through the setting aside of arbitral decisions, by local courts. The arbitration’s integration in an international credible institution solves material problems such as the choice of the President of the Panel, the guarantee of quality and accuracy of proceedings, the independence and autonomy of the arbitral court itself.

Some other very important conditions, such as the existence of international treaties to protect the investment, don’t depend on the private and foreign party; or they can be outdone (the enforceability of the award – if not possible in the State’s jurisdiction - can be achieved abroad upon assets detained by the State, if it refuses to respect an arbitral award), but those considered as the essential ones – when they are missing – cause uncontrolled and unavoidable effects.

From the States’ point of view, these conditions should not be considered as excessive burdensome and/or as a sign of loss of sovereignty. We’re dealing with the State’s commercial and economic relationships and not with the known and classical functions of the State’s sovereignty. Experience shows that more developed countries can easily deal with positive answers to all the questions I have raised as tests of adequacy. And we cannot forget the enormous potential of advantages to less developed countries, of the possibility that the international community of business considers a specific Country as a good example of an “international investment friendly” entity. This is of the utmost importance especially as States are presently in competition with one another for the attraction of international investments.

On the contrary, the submission of conflicts in which the States are a party thereto, to respected institutional arbitrations entities, should be faced by these as a comparative advantage in relation to ad hoc arbitrations, even if located on their own national territory.

It is often the national States' tendency to choose ad hoc arbitrations when they cannot have the other party accepting to submit future litigations to their own local courts, as this later option is usually a "deal-breaker" in international contracts. An arbitral ad hoc court relies fully on the quality, accuracy, ethics and independence of the chosen arbitrators. An arbitral court formed in the sphere of a credible institution adds to all these important factors the credibility and independence of the institution itself, which must be a factor of additional attraction for the States.

To increase favourable political and sociologic conditions for this evolution, I think it would be a good idea if the institutions that dedicate themselves to international arbitration prepare a check-list of the conditions that make – from a dispute resolution point of view - each Country more or less favourable to international investment. This work should be published and regularly updated, becoming an international and independent "ranking" for countries, in the light of being more or less "friendly", from a legal system point of view, to investments.

I hope the issues raised in this communication are of help to this project.

The challenge is therefore made, especially for ICC.

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