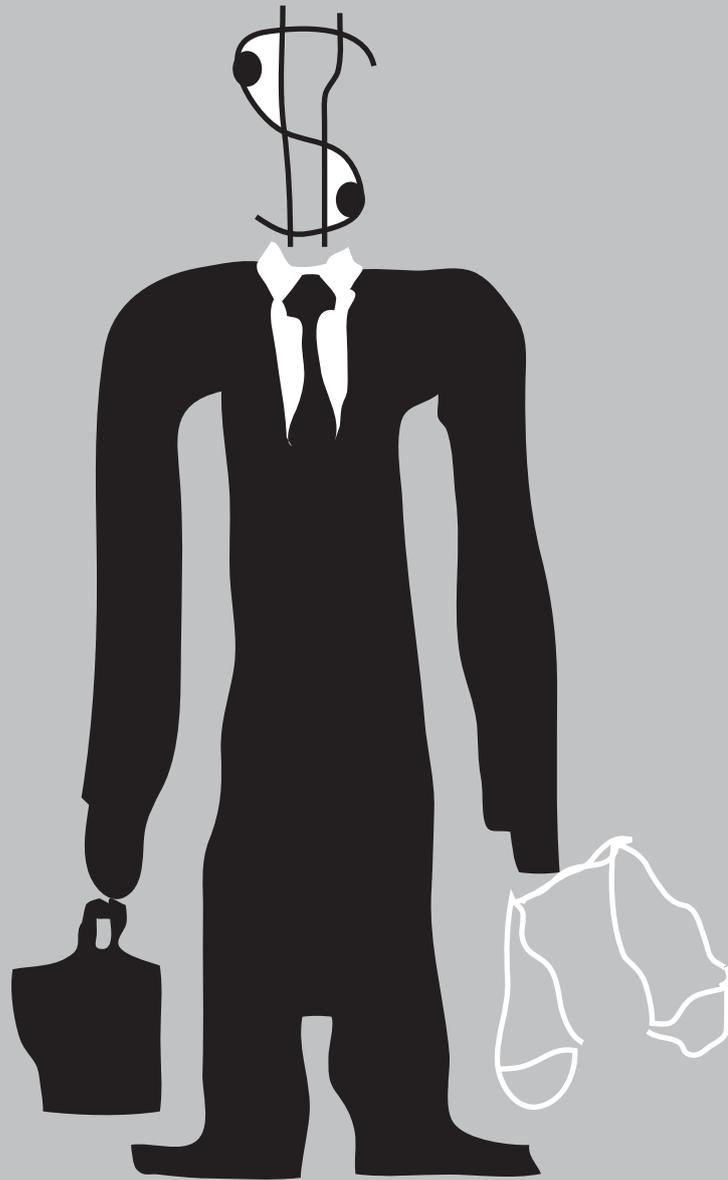


# LEGALISED PROFITEERING?



**How corporate lawyers  
are fuelling an investment  
arbitration boom**

## INTRODUCTION

On 10 March 2011, the world's attention was firmly focused on events in the north African nation of Libya. A popular uprising against Gaddafi a month before had turned into a full-scale civil war. The concern voiced by rebels and politicians throughout the UN was of a possible imminent massacre. On the very same day, a prominent international law firm, Freshfields Bruckhaus Deringer, also had its eye on Libya but seemed to have something very different on its mind than human casualties.

In a briefing published that day, they decided to advise multinational corporations on how to defend their threatened profits in Libya in the midst of a humanitarian crisis. Notably the briefing suggested corporations could use Bilateral Investment Treaties (BITs) to sue the Libyan state, claiming that investors could claim financial compensation for Libya's failure to comply with "promises to investors regarding physical security and safety of installations, personnel etc."<sup>1</sup>

Freshfields – whose equity partners earned £1.308 million pounds profit in 2010/11 at a time of global recession – was not the only international law firm looking to defend its clients in the midst of a civil war. Two months later in May 2011 at the height of NATO bombing, the international law firm King and Spalding advised multinationals that they could still sue Libya using BIT rules by arguing that Gaddafi had created an "untenable, unstable and unpredictable investment environment." The law firm even suggested that it would be possible to make claims against a possible post-Gaddafi government based on the principle of 'continuity of states' although it admitted that arbitrators "might be reluctant to impose substantial damages against Libya at a time when it is recovering from a major political, social, and economic crisis."<sup>2</sup>

The Libya case is just one case that stands out in a highly lucrative arbitration business where 390 cases have been filed by legal firms on behalf of multinational companies against governments. The payouts made by governments in terms of compensation have reached tens of billions of dollars, with legal fees worth tens of millions of dollars.

They suggest a new breed of international 'ambulance chasers' has emerged on the global stage. 'Ambulance chasers' was the term given in the late 19<sup>th</sup> Century to lawyers that sought to profit from someone's injury or accident. Today, they are international law firms making money from fuelling international investment disputes – with devastating social, environmental and budgetary impacts for sovereign states and ordinary people. To maximise their profits, law firms have promoted investment arbitration in universities, developed funding mechanisms to make it easier to finance cases, and have lobbied politicians to prevent changes to the investment regime. By doing so they have maintained and supported an international legal framework that is structurally biased in favour of corporations and prejudicial against sovereign states and ordinary people.

International investment arbitration lawyers have largely escaped public attention as their cases are largely unknown and the vested interests behind and social costs of their actions are largely hidden from view. So, it is time to shine a spotlight on the serious ethical concerns related to the role of law firms in the international investment regime.

## INVESTMENT TREATY BOOM CREATES BIG BUSINESS FOR LAWYERS

### How international arbitration tribunals work

International investment treaties grant foreign investors, who believe their investments have been damaged, the right to directly sue states at international tribunals. The majority turn to the World Bank hosted International Center for Settlement of Investment Disputes (ICSID); 25% take place under the United Nations Commission on International Trade Law (UNCITRAL) rules, with a few cases taken to the Paris-based International Chamber of Commerce (ICC) and the Stockholm Chamber of Commerce (SCC).

The arbitration process starts when a foreign investor files a claim with one of the arbitration facilities. They are usually assisted by arbitration lawyers/counselors who advise them through the process. With their help, both parties participate in the selection of the arbitration tribunal, with each party selecting one arbitrator and jointly appointing a third to serve as chairman. From there, the exact order of the process will depend on the relevant arbitration rules and the parties' preferences.<sup>3</sup> The tribunal ultimately determines if an award is justified. Most of the tribunals are held in secret unless agreed otherwise by both parties. Opportunities to challenge tribunal awards are very limited.<sup>4</sup>

The 1990s witnessed a dramatic growth in Bilateral Investment Treaties. Over 3000 BITs have now been signed almost exclusively between developed and developing countries. Nearly all of the investment agreements allow foreign investors to recourse to international legal tribunals, such as the World-Bank based International Center for Settlement of Investment Disputes (ICSID), even if they haven't used local legal mechanisms. Multinational investors can claim compensation for actions by host governments that have threatened their investments, either directly through expropriations for example, or indirectly through changes to regulation. 'Investment' is understood in such broad terms, that investors can even claim not just for money invested, but for future anticipated profits as well.

The result has been a boom in international investment arbitrations. According to UNCTAD<sup>5</sup>, the number of international arbitration cases has grown from five in 1995 to a total of 390 cases by 2010. The rapid growth has meant big business for legal firms, where investment arbitration has become one of the fastest-developing areas of international law, combining elements of private dispute settlement, treaty law and public policy<sup>6</sup>. Four firms in particular have emerged as the 'Big Four' of the international investment scene: Freshfields Bruckhaus Deringer, White & Case, King & Spalding, and Shearman & Sterling.

Average hourly rates at such law firms range from \$500 to \$1000 an hour<sup>7</sup>. Given that international arbitrations are likely to be handled by a team of lawyers and the arbitration process frequently takes two or more years to complete, the legal bill for countries, particularly those in the South, that are defending cases can be staggering – and the consequent profits for legal firms highly significant.<sup>8</sup> The average cost for hiring a three judge panel of arbitrators runs at US\$ 400,000 dollars or more – an arbitrator earns US\$3,000 dollars a day.<sup>9</sup> In a recent award made to Chevron, Ecuador's costs for legal representation and assistance came to US\$ 18 million dollars.<sup>10</sup> In all cases, lawyers whichever side they take and whatever the result of the case stand to make significant income and profits.

## INCENTIVES TO INCREASE LITIGATIONS AGAINST COUNTRIES

The conversion of international investment arbitration into a lucrative business has provided a great incentive for lawyers to look to maximise business. Keeping corporate clients constantly informed about the possibilities for litigation no matter the context (as we could see with the case in Libya) is just the bread and butter of an international investment arbitration lawyer. But there are many other ways arbitration lawyers can drum up business.

First like the infamous 'ambulance chasers', many lawyers are motivated to seek as many ways as possible to increase the number of investor-to-state disputes. In some cases, lawyers have taken advantage of the fact that multinational corporations pretend to multiple domiciles to even sue the same country under multiple BITS.<sup>11</sup> In one case American businessman Ronald Lauder brought a claim against the Czech Republic under the US-Czech Republic BIT via the UNCITRAL venue.<sup>12</sup> But as he had structured his investment in TV Nova (a broadcasting firm), through a Dutch investment vehicle, he made a similar claim against the Czech Republic under the Netherlands-Czech Republic BIT via the ICSID venue. The Czech Republic was ordered via ICSID to pay US dollar 270 million plus substantial interest while the other case was dismissed.<sup>13</sup> The lawyers meanwhile made US\$ 10 million money for both cases.

### Law firms handling the most arbitrations in 2009-10<sup>14</sup>

| Rank | Law firm                             | Total arbitrations in 2009 and 2010* | Total firm revenue and profits per equity partner (PPEP) in 2010 |
|------|--------------------------------------|--------------------------------------|--|
| 1    | Freshfields Bruckhaus Deringer       | 39                                   | \$1.84 billion (\$2.11 million)                                  |
| 2    | White & Case                         | 27                                   | \$1.28 billion (\$1.56 million)                                  |
| 3    | King & Spalding                      | 26                                   | \$718.2 million (\$1.73 million)                                 |
| 4    | Shearman & Sterling                  | 19                                   | \$737 million (\$1.56 million)                                   |
| 5    | Curtis, Mallet-Prevost, Colt & Mosle | 17                                   | \$140 million  |
| 6    | Latham & Watkins                     | 14                                   | \$1.82 billion (\$1.90 million)                                  |
| 7    | Cleary Gottlieb Steen & Hamilton     | 13                                   | \$1.05 billion   |
| 8    | Hogan Lovells                        | 13                                   | \$1.66 billion (\$1.14 million)                                  |
| 9    | Clifford Chance                      | 11                                   | 1.219 billion pounds (933,000 pounds)                            |
| 10   | Debevoise & Plimpton                 | 10                                   | \$657 million  |

\* Total arbitrations based on investment treaties and contract cases.

*“Bringing a billion-dollar claim is no longer enough to stand out in a survey of international arbitration. Nor is it enough to win a measly \$100 million. Attention, arbitration lawyers: What it takes to distinguish yourself these days is a \$350 million award, minimum. Submissions are due January 2013.”*

American Lawyer Magazine<sup>15</sup>

Second, law firms or individual lawyers can profit even when they settle before a final trial, which happens with many disputes. “It is reliable ...to conclude that lawyers may take investment treaty cases on a contingency fee basis, and that in doing so the proportion of an award that goes to the lawyers may be quite high (i.e. 30-50% or even higher in rare cases),” one expert who wants to be unnamed writes<sup>16</sup>. A settlement award would pay out the contingency fee to the lawyers without having to undertake arbitration, which may be attractive in certain difficult or weak cases. Even where contingency fees are not paid, lawyers can still bill for the work they have done and profit considerably.

And what happens if a multinational company decides it doesn't have the upfront capital to start an investor-to-state dispute? Fortunately enterprising investment lawyers have come up with a solution. The latest development in the investment arbitration world is the arrival of a phalanx of funds that finance international arbitration by paying the legal fees and initial costs to pursue a claim in return for getting a share of the amount that is awarded. Several firms have entered this market, including Juridica, AllianzProfessFinanz, IM Litigation Funding, and Burford Capital. Other firms, such as the London-based Global Arbitration & Litigation Services Ltd., are specialised in seeking third party funding for international arbitration. The firm is currently encouraging its clients to register “claims arising out of the current Libyan conflict” with values of between US\$1 and 100 million.<sup>17</sup>

It is perhaps no surprise that these financing funds have strong links with the corporate law firms they serve. Selvyn Seidel, Managing Director of Burford Capital, was previously a senior partner at Latham & Watkins, the number six law firm in the global investment arbitration business. In an interview for Global Arbitration Review he boasted of the strong links he had with arbitration lawyers, institutes and law firms. “These sources have been a big help to us and we hope to make our contribution to them through helping international arbitration,” he says.<sup>18</sup>

## EXPENSIVE CONSEQUENCES FOR STATES

The consequences of the rapid expansion of investment arbitration may be attractive for law firms, but it has cost

many states dearly as the legal fees together with the original claims for damages have involved a major diversion of resources that governments could use for social and environmental investment. The *American Lawyer* magazine reported in 2011 on 113 cases that involved costs of at least a 100 million dollars – a significant amount of money for any state budget – 65 based on contracts and 48 based at least in part on investment treaties or legislation.<sup>19</sup>

Argentina, which according to *American Lawyer* “remains the favorite target”<sup>20</sup> of foreign investors, has been sued, in total 51 times, mostly due to economic reform programs that were implemented after the 2001 financial and economic crisis. Awards against Argentina have already reached a total of US\$912 million dollars, equivalent to the annual average salary of 75,000 public hospital doctors. The pending demands in ICSID against Argentina are estimated at US \$20 billion dollars, almost 6 times Argentina's current public budget for health (US\$ 3.4 billion dollars) or almost 3 times Argentina's current public budget for education (US\$ 7.4 billion dollars).<sup>21</sup>

## INTERNATIONAL LAW IN PUBLIC OR CORPORATE INTEREST?

The international investment regime at its heart has a profound injustice as it allows multinational companies to sue governments, but governments are unable to use the same international legal mechanisms to sue companies. International arbitration lawyers – which profit so well from the arbitration process – mirror in many aspects the corporate-biased nature of the investment regime. Not only are most based at companies where the main clientèle are corporations; in a system where only corporations can sue – most are active mainly advising companies on how to sue governments. Most of the top ranked arbitration law firms act as counsels for the investor's side. Only a few have specialized in defending governments.<sup>22</sup>

Arbitrators are not exempt from this potential institutional bias as they are chosen on a case-by-case basis, mainly from the same firms that provide counsels.

*“A government friendly system would make it much less interesting for investors to bring claims. So, there is an inherent problem in that those who want to keep the system alive because they profit from it, tend to lean towards the investor”,*

Nathalie Bernasconi-Osterwalder, senior lawyer at the International Institute on Sustainable Development (IISD)<sup>23</sup>

This has encouraged a closed ‘old boys’ network, in which counsels and arbitrators are motivated to exchange favours. As elite Chilean arbitrator Francisco Orrego-Vicuña of the London-based 20 Essex Street put it when he explained his rise to the top of international arbitration: “I think I have just been fortunate in that friends have looked upon me kindly.”<sup>24</sup>

On several occasions, governments have even had to challenge the appointment of arbitrators from firms, which were involved in other dispute settlement cases against them. Some of the challenges led to resignations of arbitrators, but not all. In October 2009 Venezuela challenged the arbitrator Robert Von Mehren on the ground that he was a retired partner of, but maintained an office and secretariat services at, Debevoise & Plimpton, which was concurrently representing claimants in a similar case against Venezuela in the same year (Holcim versus Venezuela). But its appeal was rejected.<sup>25</sup>

A pro-corporate bias is made even more probable by the fact that investment counsels and arbitrators often serve (and are legally allowed to) on the board of directors of commercial entities with financial or other interests.

Canadian Yves Fortier, once named ‘world’s busiest arbitrator’ by a leading arbitration journal is just one such example: while senior partner for the Ogilvy Renault law firm, he was also director of mining giant Rio Tinto plc

and before that chairman of the Canadian mining company Alcan. The extractive industry is one of the most powerful claimants within the arbitration system<sup>26</sup>. Yet Fortier is known to have presided over five known arbitration cases where an extractive industry was claimant. Forbes estimated his total compensation for Rio Tinto in 2010 at US\$ 172,000 dollars.<sup>27</sup> Rio Tinto also showed its appreciation to the world of investment law and Fortier by funding the L. Yves Fortier Chair in International Arbitration and International Commercial Law at the McGill Faculty of law.

*“Prominent figures in the industry often sit as arbitrators while advising and representing claimants or respondents and while promoting arbitration clauses in investment contracts, treaties, or arbitration rules. This provides a basis for reasonable suspicion of bias in the investment treaty system”.*

Investment lawyer who did not want to be named.<sup>28</sup>

### Arbitrators with the busiest caseloads in 2009-10<sup>29</sup>

|    | Arbitrator                                      | Current position/ affiliation   | Total arbitrations in 2009 and 2010* |
|----|---|---|--------------------------------------|
| 1  | Charles Brower (male, US)                       | Self-employed member of 20 Essex Street chambers, London<br>Frequent lecturer and teacher including as Visiting Fellow at Cambridge University and Distinguished Visiting Professor at the University of Virginia School of Law | 25                                   |
| 2  | Gabrielle Kaufmann-Kohler (female, Switzerland) | Partner at Lévy Kaufmann-Kohler, Geneva<br>Also Professor for Private International Law at the Geneva University Law School and Director of the Master in International Dispute Settlement                                      | 18                                   |
| 3  | Brigitte Stern (female, France)                 | Emeritus Professor of International Law at the University of Paris I, Panthéon-Sorbonne   | 18                                   |
| 4  | Bernard Hanotiau (male, Belgium)                | Partner at Hanotiau & van den Berg, Brussels<br>Professor (Professeur extraordinaire) at the law school of the University of Louvain, Centre de Droit International   | 17                                   |
| 5  | Albert Jan van den Berg (male, The Netherlands) | Partner at Hanotiau & van den Berg, Brussels<br>Also Professor of Law at Erasmus University Rotterdam and Visiting Professor at the University of Miami School of Law   | 16                                   |
| 6  | William Park (male, US)                         | Professor of Law at Boston University   | 15                                   |
| 7  | Henri Alvarez (male, Canada)                    | Partner at Fasken Martinau, Vancouver<br>Also teaching international commercial arbitration and dispute resolution at the Faculty of Law at The University of British Columbia  | 14                                   |
| 8  | Karl-Heinz Bockstiegel (male, Germany)          | Sole Practitioner, Germany<br>Member of Law Faculty of University of Cologne as Professor Emeritus  | 13                                   |
| 9  | L. Yves Fortier (male, Canada)                  | Senior partner and Chairman Emeritus at Norton Rose OR, Montreal  | 10                                   |
| 10 | Marc Lalonde (male, Canada)                     | Sole Practitioner   | 10                                   |

\* Total arbitration based on investment treaties and contract cases.

Fortier has recently announced that he plans to retire from his law firm at the end of 2011 saying "Being an international arbitrator as a member of a global legal practice can create inherent conflict risks."<sup>30</sup> He also resigned from the Board of Rio Tinto, but newspaper reports don't suggest that concern over conflict of interests was the main reason for his departure. Rather it seemed his resignation was forced by Rio Tinto to appease shareholders who wanted to punish Fortier and others on the Board for an unsuccessful \$US38 billion acquisition of Canadian aluminium group Alcan in 2007.<sup>31</sup>

In one known case an arbitrator was challenged for her corporate relations with a bank. In Vivendi versus Argentina, Argentina argued that the award should be annulled as one of the arbitrators, Gabrielle Kaufmann-Kohler, lacked independence and impartiality as she was also a member of the Corporate Responsibility Committee, of the Swiss bank UBS, which at the time was the single largest shareholder in claimant Vivendi. However while ICSID's adhoc committee was critical of Kaufmann-Kohler's judgment in failing to disclose her potential conflicts of interests, the committee members declined to annul the award. They argued that the Swiss arbitrator's independence was not actually impaired and that it would be unjust to deny the claimants the benefit of the award due to the arbitrator's failures, and the lengthy proceedings.<sup>32</sup>

## PROPPING UP AN UNJUST BUT LUCRATIVE SYSTEM

The investment regime has come under increasing challenge in recent years for its inconsistencies and injustices. Bolivia announced its withdrawal from ICSID in 2007 and Ecuador in 2009. Nicaragua and Venezuela have threatened to do the same. Some investment arbitration lawyers have also publicly voiced concerns, such as Philippe Sands of London-based Matrix chambers who questioned the 'propriety' of a system of 'revolving doors'.<sup>33</sup> Law professor Gus Van Harten has said investment treaty arbitration is inconsistent with the rule of law.<sup>34</sup> However their voices have been in the minority and completely overshadowed by the active lobbying by most corporate law firms to prop up an unjust but highly lucrative system.

*"Through academic teaching, conferences, research and publications, Levy Kaufmann-Kohler's lawyers are constantly at the forefront of the developments in international arbitration law."<sup>35</sup>*

Website of law firm Lévy Kaufmann-Kohler, Geneva

With the number of investor-to-state cases rising by at least 30-40% per year,<sup>36</sup> the last thing the majority of investment lawyers want is any radical reform, stricter definitions or safeguards in either the arbitration system or the text of the investment treaties themselves. However investment arbitration lawyers were faced with that possibility when the European Union in 2009 agreed in the Lisbon Treaty to shift the competency for investment agreements from member states to the European Union. In response investment lawyers came out in force to push the EU Commission and the European Parliament to maintain the status quo and argue against any change of existing 1,300 EU member states' BITs.

In emails Corporate European Observatory obtained after an access-to-information request to DG Trade the EU Commission and from interviews with via key members of the European Parliament, it was clear that law firms lobbied vigorously against future changes to EU investment policy. They did this by organising round-tables and conferences in Brussels, London and Frankfurt between key corporate foreign investors and Commission officials and through lobbying of key MEPs on the European Parliament Committee on International Trade (INTA).<sup>37</sup> In a close vote in the INTA on 13 April 2011, the lobbyists finally got their way. The Committee granted the Commission weaker powers of review over existing BITs by EU Member States and also limited the reasons for which the Commission can withdraw the authorisation of certain BITs.

## INTELLECTUAL SUPPORT

Political lobbying is backed up by considerable promotion of investor-state dispute settlement and investors rights by arbitration lawyers within the academic world. Those invested in the system financially are some of the prime defenders of it within the ideological and academic sphere.

A close look at the table on page 5 reveals that almost all the richest and most successful arbitrators are frequently teaching in public and private law schools. The explosion of international arbitration courses has given arbitrators and counsels plenty of scope to promote the investment arbitration system. Moreover the secrecy and lack of transparency of most arbitration cases enables them to defend their arguments and share information without the normal academic checks and balances to verify their claims.

Swiss law firm Lalive has even found that teaching can be a new way of acquiring potential clients. The law firm signed a contract with United Nations Institute for Training and Research (UNITAR) to conduct a new e-learning course titled 'Introduction to Investment Arbitration' which took place from March 14 to April 15, 2011.<sup>38</sup> Twenty-one lawyers, officials and professionals mostly from developing countries and transition economies attended the course, all potential future clients for LaLive.

## CONCLUSION:

The American Lawyer magazine boasted that arbitration was a 'secret world' made up of the "biggest cases you have never heard of".<sup>39</sup> That has certainly been the case as multinationals worldwide have taken full advantage of an unjust investment regime to sue sovereign governments for millions of dollars. The full costs have been felt in diversion of limited government budgets removed from social spending, and the undermining of governments' capacity to protect their citizens from corporate abuses. Lawyers throughout the process have been largely ignored or seen as neutral intermediaries.

The evidence however suggests that lawyers not only have a strong vested interest in the current international investment regime, but actually perpetuate and exacerbate its profound injustice. At great personal financial gain, arbitration lawyers have actively pursued cases, exploited loopholes and created an explosion in the number and costs of dispute settlement cases. They have also actively fought for maintaining the current system, against its critics, in academic circles and through direct political lobbying. The end result has been the maintenance of a regime that continuously favours investors over sovereign governments. As the international investment regime comes under public challenge, it is time for the international ambulance chasers of today to come clean on the way they have personally benefited and accept radical reform.

## ALTERNATIVES

Most of the problems presented in the study would be solved if dispute settlement would be restricted to state-state disputes instead of investor-state. For diplomatic and budgetary reasons, states would most likely not enter into numerous costly disputes, which only affect the interest of an individual company or even a sector. In order to not privilege foreign investors over domestic ones or citizens, states should review their investment treaties with a view to replace the current investor-state arbitration system for a state-to-state one (as proposed by several countries, including Australia).

But, while countries are still locked-in to an investor-state dispute system, the following changes are necessary to avoid investment lawyers and law firms exploiting the current investor-state dispute system:

*"I have never seen such an extreme and exclusive focus on corporate interests... nobody ever thought of protecting anything else but industry."*

Carl Schlyter, MEP, Rapporteur in European Parliament on the future of EU member states' BITs<sup>40</sup>

- The arbitration industry should play no role in solving investment disputes that affect questions of public law and policy because its significant financial interest in the field is incompatible with the principles of judicial independence and impartiality. States should review their investment treaties with a view to exit ICSID and other facilities for the commercial arbitration of investment disputes.
- Investment disputes should be solved by independent adjudicative bodies. This could be national courts or specifically created bodies with sitting 'judges' who enjoy objective guarantees of independence and impartiality, and are accountable to the general public and have legal expertise in the field of regulation/public law. A working group of the Latin American regional block UNASUR has proposed a Permanent Arbitration Tribunal to solve investment disputes, where the selected arbitrators would not be allowed to hold other positions.
- Considering the vested interest of law firms in the debate on reform of the international investment regime, politicians should be wary of their advice.
- A cap should be imposed on the costs of lawyers and arbitrators. Within UNASUR, countries have proposed a Centre for Legal Advice that could represent the interests of the states being sued and would follow the model of the Legal Centre for Dispute Settlement in the WTO, whose services are ten times cheaper than the costs of international law firms. Another proposed solution is the creation of an international standard that sets maximums on legal expenses.
- Lawyers with economic interests in arbitration should not be allowed to teach arbitration law.

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