On 2 August 2006, an ICSID tribunal dismissed for lack of jurisdiction all claims brought against the Republic of El Salvador by the Spanish company Inceysa Vallisoletana S.L. ("Inceysa"), in a ruling believed to be the first ever to rest on interpretation of "accordance with law" clauses found in many bilateral investment treaties. The award may stand as a stark warning to the unscrupulous who would prey on small countries and bolster the reputation of ICSID as a forum for even-handed resolution of investment disputes.

Inceysa initiated ICSID arbitration against El Salvador in July 2003, alleging numerous violations of the 1995 investment treaty between Spain and El Salvador (the "Treaty"), as well as breach of contract and violation of El Salvador's 1999 Investment Law. The case arose from a decision by El Salvador's Ministry for the Environment and Natural Resources (known as "MARN") not to proceed with a concession contract it had signed with Inceysa in November 2000 following a public bidding process, that would have allowed Inceysa to serve for ten years as one of two authorized providers of vehicle inspection services in El Salvador.

Inceysa alleged that MARN's decision not to proceed with the concession, and its commencement of proceedings in the Salvadoran courts to terminate the concession contract, violated several provisions of the Treaty, including provisions providing for "fair and equitable treatment" and "protection" and prohibiting expropriation absent prompt, adequate and effective compensation. Inceysa claimed damages exceeding $120 million for alleged violations of these Treaty provisions, and for the alleged related violation of the national investment law and breach of contract.

In September 2004, following constitution of a tribunal consisting of Rodrigo Oreamuno Blanco (as President), Burton Landy and Claus von Wobeser, El Salvador objected to ICSID jurisdiction over the dispute. The centerpiece of El Salvador's objections was that Inceysa had obtained the concession contract through massive fraud in the public bidding process, and that accordingly the investment had not been established "in accordance with law," as it argued that the Treaty required. Specifically, El Salvador offered to demonstrate as a matter of fact that Inceysa had grossly misrepresented both its financial condition and its relevant experience in its bid submission, had submitted fraudulent and forged supporting documentation, and had disguised its close link to a second Spanish company participating in the same bidding process (ICASUR S.A.), to circumvent clear rules that prevented related companies from bidding independently. El Salvador argued that this fraud deprived Inceysa of the right to invoke the protections of the Treaty, because its threshold consent to ICSID jurisdiction had been preconditioned on investments being made "in accordance with law," a clause that appeared three times in the Treaty (although not its introductory definition of "investment").

El Salvador argued that Inceysa's fraud also prevented it from pursuing ICSID arbitration under the national investment law, which was similarly intended to protect only investments made in compliance with Salvadoran legislation. Finally, El Salvador argued that the ICSID tribunal had no jurisdiction over claims framed solely as breach of contract, because the forum selection clause of the contract provided for such disputes to be submitted exclusively to local arbitration in El Salvador.
Together with its objections to jurisdiction, El Salvador filed a request for provisional measures in the form of security for costs, citing Inceysa's tenuous financial condition as apparent from public records in Spain, as well as its history of falsifying financial documents and of making financial transfers to ICASUR S.A. and other companies that ostensibly were arms-length, but in fact were controlled by a common principal. The ICSID Tribunal declined to rule on the provisional measures request in advance of the hearing on jurisdiction.

The jurisdictional hearing was held in Washington, D.C. from 2-5 May 2005. The Tribunal heard testimony and cross-examination of fact and expert witnesses for both sides.

On 2 August 2006, the Tribunal issued its Final Award, upholding El Salvador's objections to jurisdiction. The Tribunal accepted that El Salvador's consent to ICSID jurisdiction embodied in the Treaty did not extend to investments that were made fraudulently, and therefore not in accordance with law. The Tribunal relied both on the express language of the Treaty and on references in the travaux preparatoires to investments complying with local law as a precondition to benefiting from Treaty protection. Although prior ICSID decisions (Tokios Tokeles v. Ukraine and Salini Construttori S.p.A. v. Kingdom of Morocco) had briefly addressed the function of "accordance with law" clauses in investment treaties, the decision in this case is believed to be the first to apply such clauses for purposes of jurisdictional analysis and decision.

On the facts, The Tribunal found that Inceysa's bid in the tender process had presented false information about its financial condition, about the experience and capability of its administrator, and about the identity and experience of a supposed "strategic partner" that was supporting its bid. Inceysa also misled Salvadoran officials about its relationship with ICASUR, the other Spanish company participating in the tender process. The Tribunal found in light of these facts that Inceysa's investment in El Salvador, which gave rise to the dispute presented to ICSID, was made in violation of law and of the principle of good faith on which it found El Salvador's consent to jurisdiction to have been conditioned. The Tribunal noted that any contrary finding would run counter to the general principle that parties should not benefit from their own wrongdoing, which it believed inherent in notions of international public order. The Tribunal reached the same conclusion with regard to El Salvador's national investment law, namely that its protections did not extend to investments made in violation of Salvadoran law. Finally, the Tribunal found that it had no jurisdiction to hear Inceysa's breach of contract claims, rejecting Inceysa's argument that the contract's referral of such matters to "arbitration in accordance with Salvadoran legislation" constituted indirect consent to ICSID jurisdiction over pure contract claims, by virtue of the Treaty and other Salvadoran legislation referring generally to international arbitration.

The Tribunal ordered Inceysa to bear the full costs of the proceeding, including 100% of the Tribunal's fees and expenses and the administrative expenses of the Tribunal.

An Arnold & Porter LLP team of Whitney Debevoise, Jean Kalicki and David Orta represented El Salvador. Inceysa was represented by Alfonso López-Ibor of Ventura Garcés & López-Ibor of Madrid.