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Nationality of investors in ICSID arbitration

VALTS NERETS

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TABLE OF CONTENTS

Summary	4
Introduction	6
1 ICSID jurisdiction	9
1.1 Requirement of <i>ratione materiae</i> for jurisdiction	10
1.1.1 Legal nature of dispute	10
1.1.2 Definition of investment	12
1.2 Requirement of <i>ratione personae</i> for jurisdiction	15
1.2.1 Identifying the Contracting State party	16
2 Determining the investor's nationality	18
2.1 Nationality under international law	18
2.1.1 Nationality of individuals	20
2.1.2 Nationality of legal entities	20
2.2 Nationality requirements under the Convention	22
2.2.1 The individual as a national of 'another Contracting State'	23
2.2.2 The legal entity as a national of 'another Contracting State'	25
3 Nationality of a legal entity 'because of foreign control'	28
3.1 The concept of foreign control	29
3.1.1 Agreement on foreign control	31
3.1.2 Existence of foreign control	32
3.2 Indirect control v. indirect claim	39
3.2.1 Indirect claims in ICJ jurisprudence	40
3.2.2 Indirect claims in ICSID jurisprudence	43
Conclusion	52

SUMMARY

This paper analyzes the concept of nationality as a *ratione personae* requirement for jurisdiction of the International Centre for Settlement of Investment Disputes (ICSID, the Centre), which was created under the Convention on the Settlement of Investment Disputes between States and Nationals of Other States (the Convention) in 1965.

Under Article 25 of the Convention, the jurisdiction of the Centre extends to any legal dispute arising directly out of an investment between a Contracting State and a national of another Contracting State. Nationality is the most important jurisdictional requirement of the Convention, since nationals of host States and non-contracting States are explicitly precluded from bringing claims before the Centre.

Additionally, the Convention does not define nationality, so that a broad discretion is given to the parties to define this term. Of all requirements for jurisdiction, application and determination of nationality for the purposes of the Convention have caused the most difficulty for tribunals. Since only a minor part of foreign investment occurs by individuals, this paper focuses on nationality of legal entities.

Nationality of legal entities has been widely examined by various distinguished legal scholars and also before the International Court of Justice (ICJ) in the 20th century, when States aimed to protect their nationals and legal entities by measures of diplomatic protection. This paper concludes that the principles of diplomatic protection are inapplicable for the needs of modern investment arbitration. However, in forming current international law tribunals often refer to conclusions of the ICJ regarding protection of shareholders.

The paper analyzes various tests for determining the nationality of a legal entity with particular emphasis on the control test as an exceptional method under Article 25 (2) (b) of the Convention. Different approaches taken by tribunals in determining foreign control over a locally incorporated entity are analyzed, with a conclusion that tribunals are ruling *in favorem jurisdictionis*, which means that the parties' will is decisive in determining jurisdiction.

Recently tribunals have significantly expanded their jurisdiction by allowing claims brought by shareholders for a wrong done to a legal entity. Although a shareholder is entitled to claim before the Centre if the parties have agreed on shares as the investment, in

practice tribunals do not distinguish a shareholder's right to claim separately from the company from a shareholder's claim brought on behalf of the company.

The concept of nationality must be interpreted within the scope of Article 25 and compatibly with the Convention's aims – to promote the economic development of States and the role of private international investment of nationals of other States therein. It is suggested that nationality should be applied functionally to fulfil its main function – to ensure that the dispute before the Centre is of international character.

It is concluded that tribunals should be less formalistic in applying the Convention's jurisdictional requirements, with a more cautious approach in accepting that jurisdiction is necessary to eliminate the imbalance in rights and obligations between investors and host States.

INTRODUCTION

Foreign direct investment is an important contribution for development of the countries of developing nations, and investment arbitration has become one of the most distinguished improvements in international law. Foreign direct investment started its expansion in the middle of the 19th century and reached its bloom in the middle of the 20th century, when capital from the USA and Great Britain flowed to all parts of the world. For centuries, protection of investors had been a complete competence of their home States; hence individuals and legal entities had no rights to bring claims directly against States. States had a right to exercise diplomatic protection on behalf of their nationals; however, most States did not have a constant position in exercising diplomatic protection, which merely depended on political considerations. Thus, due to its political nature, diplomatic protection was not a reliable instrument for safeguarding the interests of investors.

In the 1960s the World Bank, to encourage greater flows of capital to developing countries, initiated conversations on establishing a dispute settlement facility. Thus in March 1965 the Convention on the Settlement of Investment Disputes between States and Nationals of Other States¹ (the Convention) was drafted and entered into force on 14 October 1966 with a following ratification by twenty countries.

Under the Convention the International Centre for Settlement of Investment Disputes (ICSID, the Centre) was established as an autonomous, depoliticized institution, designed especially as a forum to administer foreign investment disputes, where investors could submit claims directly against States autonomously of their States of nationality. During the first thirty years of existence, only one case a year on average was submitted to the Centre,² but recently – up to 30 cases a year. This increase merely relates to the rapid growth of bilateral investment treaties (BITs). Since the first BIT in 1959, in 2006 this figure had grown to over 2 500³, involving more than 176 countries, with most treaties stipulating the Centre as the forum.

¹ Convention on the Settlement of Investment Disputes between States and Nationals of Other States (18 March 1965). Available on the Internet at http://icsid.worldbank.org/ICSID/StaticFiles/basicdoc_en_archive/ICSID_English.pdf. Last visited September 21, 2010.

² R.D. Bishop, J. Crawford, W.M. Reisman, *Foreign Investment Disputes, Cases Materials and Commentary*, London, Kluwer Law International, 2005, p. 1.

³ United Nations Conference on Trade and Development, *Recent Developments in International Investment Arbitration (2006-June 2007)*, International Investment Arbitration Monitor No.3 (2007). Available on the Internet at http://www.unctad.org/en/docs/webiteiia20076_en.pdf (last visited September 21, 2010). See also

The jurisdiction of the Centre is of a special nature. First, the consent of the parties forms the basis for jurisdiction, the dispute must arise directly out of an investment, and political and purely economical disputes are excluded from jurisdiction. Second, and most important, the Convention explicitly excludes disputes between States and its nationals. The drafters of the Convention, however, did not include definitions of the terms “investment” and “nationality” in the Convention; thus the Centre’s deliberation of investors’ and disputes’ qualities is very high.

Definitions of investment and nationality, which are of paramount importance to the Centre’s jurisdiction, are left to the parties, who mostly define these terms in BITs. It is argued that the broad discretion given to the parties to define the terms has often led to results which were beyond the outer jurisdictional limits of the Convention stipulated in Article 25. Thus, it is observed that, considering the parties’ discretion to define terms and the fact that the tribunal is the judge of its own competence, tribunal decisions on jurisdiction are frequently contrary to the aims of the Convention.

Indeed, being in a situation when tribunals must balance the competing interests of the investor and the sovereignty of the host State, tribunals have received criticism on being overly eager to favour investors’ interests than vice versa. “Favouring interests of the investors over States, bias towards corporations and misapplying investment treaty obligations”⁴ were a few of Bolivia’s arguments when in April 2007 it became the first country to denounce the Convention. In July 2009, “to prohibit the ceding of sovereign jurisdiction in disputes with private companies”,⁵ Ecuador was the second country to denounce the Convention. These denunciations are strong indications that the concepts established by the tribunals should be reviewed.

Although the decisions of tribunals are not precedents which could be binding on other tribunals, arbitrators in their decisions increasingly refer to the case-law of the Centre. Indeed, decisions of the most prominent forum of investment disputes should give more security and certainty both to foreign investors and States.

Braun, T.R., “Investitionsschutz durch Internationale Schiedsgerichte”, (2009) *89 TranState Working Papers*, pp. 6-9; Braun, T.R., Schonard, P., „Der neue deutsch-chinesische Investitionsförderungs-und-schutzvertrag” (2007) *8 Recht der Internationalen Wirtschaft*, p. 561.

⁴ F. Cabrera Diaz, “Bolivia Expounds On Reasons For Withdrawing From ICSID Arbitration System”, (2007) *Investment Treaty News (ITN)*, 27 May. Available on the Internet at http://www.iisd.org/pdf/2007/itn_may27_2007.pdf. Last visited September 21, 2010.

⁵ J.M. Robbins, S. Austin, “Ecuador Withdraws From ICSID Convention”, (2009) *Practical Law Company*, 12 August. Available on the Internet at <http://arbitration.practicallaw.com/2-422-1266>. Last visited September 21, 2010.

The purpose of the present research is to examine the concept of nationality as the main jurisdictional requirement of the Convention and to analyze the consequences of the lack of definitions of 'investment', 'nationality' and 'foreign control' in the Convention. The research examines whether the broad discretion given to the parties to define these terms has not led to results which are contrary to the aims of the Convention.

The present research is organized according to the following structure. Following the Introduction, Chapter I provides an overview of both requirements for jurisdiction of the Centre – *ratione materiae* and *ratione personae*. Chapter II then addresses the concepts of nationality of individuals and legal entities under international law and proceeds with an analysis of the jurisdictional requirements stipulated in the Convention. Following the analysis of nationality, Chapter III discusses the concept of foreign control as an exception for jurisdiction of the Centre for nationals of the host State. The present research concludes with an analysis of interpretation of the foreign control concept and further examines the distinction between indirect control and indirect claims in the Centre's recent case-law.

1 ICSID JURISDICTION

The concept of jurisdiction of the Centre is provided in Chapter II “Jurisdiction of the Centre” (Articles 25-27) of the Convention. Generally jurisdiction of the Centre is established by consent of the parties to submit their dispute to arbitration before the Centre, and parties’ consent is considered to be the “cornerstone”⁶ of jurisdiction.

No definition of “jurisdiction”, however, is given in the Convention. In relation to the Convention this term has been used to express “the limits within which the provisions of the Centre will be available for ... arbitration proceedings”.⁷

Under Article 25 the jurisdiction of the Centre extends to any legal dispute arising directly out of an investment between a Contracting State ... and a national of another Contracting State which the parties to the dispute consent in writing to submit to the Centre. Consent must be in writing and may not be withdrawn unilaterally. Consent to submit disputes to the Centre may be expressed in various ways, e.g. through agreement, in legislation, or in BITs. However, any Contracting State has the right to notify to the Centre of the class or classes of disputes which it would or would not consider submitting to the jurisdiction of the Centre, i.e., consent may be limited.⁸

Therefore three prerequisites for a dispute to fall within the jurisdiction of the Centre must be distinguished and all must be satisfied:

- 1) The dispute must be of a legal nature.
- 2) The dispute must arise directly out of an investment.
- 3) The dispute must be between a Contracting State and a national of another Contracting State.

The present chapter follows with an analysis of requirements for jurisdiction – *ratione materiae* and *ratione personae* together with their elements – the legal nature of the dispute, a definition of investment and the nature of the parties.

⁶ O. E. García-Bolívar, “Comments on Some ICSID Decisions on Jurisdiction”, (2004) *IBL (International Business Lawyer)*, August, p. 171. See also C. H. Schreuer, *The ICSID Convention: a Commentary*, Cambridge, University Press, 2001, p. 192.

⁷ Reports of Cases Decided under the Convention on the Settlement of Investment Disputes between States and Nationals of Other States, 1965, Rayfuse, R. (ed.), (1993) *1 ICSID Reports 172*, cited in Schreuer, *supra* note 6, p. 95.

⁸ E.g., relating to certain natural resources (Jamaica, Saudi Arabia).

1.1 Requirement of *ratione materiae* for jurisdiction

According to Article 25 of the Convention, jurisdiction *ratione materiae* (i.e., admissible subject matter) consists of two elements – the existing dispute must be of a legal nature and arise directly out of an investment.

As the International Court of Justice stated in *Mavrommatis Palestine Concessions* in 1924, “[a] dispute is a disagreement on a point of law or fact, a conflict of legal views or of interests between two persons”.⁹ Mere dissent on any issue or difference in opinions does not necessarily create a dispute. Generally a dispute comes into existence if one party has submitted a claim or request to the other party which has failed to react to this claim in a reasonable time or in the period prescribed in the BIT.

The issue of existence of a dispute, however, has been raised only in several cases before the ICSID. To illustrate, in *Asian Agricultural Products Ltd. (AAPL)* the tribunal found that AAPL was entitled to submit a claim to the Centre; hence the three month time limit, as prescribed in the BIT, had passed.¹⁰

Certainly, the most objections have been raised by the parties as to the nature of the dispute, which will be further analyzed.

1.1.1 Legal nature of dispute

The debate on including the definition of a legal dispute was raised several times during the drafting of the Convention, in particular to exclude purely political or commercial¹¹ or purely theoretical disputes. No definition, however, was included in the Convention, and the nature of the dispute must be determined by tribunals on a case-by-case basis.

Even more concerns appeared to exclude certain types of dispute from the jurisdiction of the Centre, namely those related to activities of a State’s “sovereign prerogatives”,¹² although no such limitations were included in the Convention. Alternatively

⁹ *Mavrommatis Palestine Concessions* (Greece / United Kingdom), (30.08.1924.), Judgment (1924), PCIJ, Ser.A, No.2, p. 12. See also *Case Concerning East Timor* (Portugal / Australia), (30.06.1995.), *1995 ICJ Reports*, p. 99.

¹⁰ *Asian Agricultural Products Limited v. Republic of Sri Lanka*, ICSID Case No. ARB/87/3, (1991) 6 *ICSID Rev. – FILJ (ICSID Review – Foreign Investment Law Journal)*, p. 529. See also *AGIP S.p.A. v. Congo*, ICSID Case No. ARB/77/1, (1993) 1 *ICSID Rep.* 306.

¹¹ Convention on the Settlement of Investment Disputes Between States and Nationals of Other States - Documents concerning the Origin and Formulation of the Convention (Convention History), Vol. II, Washington, ICSID, 1968, pp. 54, 83, 96, cited in Schreuer, p. 103.

¹² C.F. Amerasinghe, “The Jurisdiction of the International Centre for the Settlement of Investment Disputes”, (1979) 19 *IJIL (Indian Journal of International Law)*, pp. 173/4, 176, cited in Schreuer, *supra* note 6, p. 110.

the parties were given an opportunity to agree on the class or classes of dispute to be submitted to the Centre in two forms.

First, according to Article 25 (4) notification to submit a certain class or classes of dispute to the Centre may be given by any Contracting State. Notification may be given at the time of ratification, acceptance or approval of the Convention or at any time thereafter. To illustrate,

the Republic of Guatemala does not accept submitting to the Centre's jurisdiction any dispute which arises from a compensation claim against the State for damages due to armed conflicts or civil disturbances.¹³

In fact, only a minority of Contracting States has not filed a notification under Article 25 (4).

Second, parties may include the definition of a legal dispute in their agreement. The Centre has designed Model Clauses relating to the subject-matter of the dispute, and Clause 4 stipulates that "[t]he consent to the jurisdiction of the Centre ... shall [only] / [not] extend to disputes related to the following matters: ..."¹⁴

Tribunals have analyzed actions of the State which could fall under their sovereign prerogatives, e.g. seizure of premises, dissolution of companies, and others, while the political nature of the dispute has also been accentuated. The existence of political or governmental elements in disputes, however, does not change the nature of the dispute "as long as they [disputes] concern legal rights and obligations or the consequences of their breach".¹⁵ Thus the decisive criterion for tribunals has been only whether the dispute was based on agreement between the parties to the dispute.

Next, not every dispute related to a BIT is subject to the jurisdiction of the Centre. According to the wording of Article 25, the dispute must arise "directly out of an investment". To clarify the issue, the phrasing of the Article does not require the investment

¹³ Notifications concerning classes of disputes considered suitable or unsuitable for submission to the Centre. ICSID/8-D, p. 1. Available on the Internet at <http://icsid.worldbank.org/ICSID/FrontServlet?requestType=ICSIDDocRH&actionVal=ShowDocument&Measures=True&language=English>. Last visited September 21, 2010.

¹⁴ ICSID Model Clauses. Available on the Internet at <http://icsid.worldbank.org/ICSID/FrontServlet?actionVal=ModelClauses&requestType=ICSIDDocRH>. Last visited September 21, 2010.

¹⁵ Československa obchodní banka (CSOB), a.s. v. Slovak Republic, ICSID Case No.ARB/97/4, Decision on Objections to Jurisdiction, (1999) 14 *ICSID Rev. – FILJ (ICSID Review – Foreign Investment Law Journal)*, paragraph 61.

to be made directly. The adjective “directly” refers to the dispute, hence the investment may exist in a form that is not “direct”.¹⁶

The concept of directness of the dispute is “a matter for objective determination”¹⁷, fully for the tribunal’s consideration and does not depend on agreement between the parties. The issue of directness has been brought before tribunals several times. However, the most important in this matter is the tribunal’s reasoning in *AMCO*¹⁸, where the tribunal was asked whether an obligation to avoid tax fraud had arisen directly out of an investment. After stating that every natural or legal person has rights and obligations under State law and that rights and obligations of an investor are in particular a consequence of the investment agreement, the tribunal then continued with a conclusion that “tax fraud is clearly a general obligation of law”.¹⁹ Therefore the tribunal ruled that the dispute was not in the jurisdiction of the Centre, hence it did not meet the *ratione materiae* requirements.

Also important is the tribunal’s note in *CSOB*²⁰ that an investment may consist of several transactions and that a dispute must be considered as arising directly out of an investment even if such dispute arises from a single transaction.

In conclusion, the issue whether the dispute falls within the jurisdiction of the Centre mainly depends on the parties’ agreement, and with several exceptions determining the legal nature of the dispute has not caused significant problems for tribunals.

1.1.2 Definition of investment

The second and the most important element of jurisdiction *ratione materiae* relates to the meaning of investment; hence only disputes arising from an investment fall within the jurisdiction of the Centre. Again, the Convention does not define what is obviously the most important term of the Convention – investment. Therefore a broad discretion is given to the parties in defining this term. This definition, however, must be in accordance with “the need for international co-operation for economic development and the role of private international investment therein”, as stated in the Preamble of the Convention.

¹⁶ See *Fedax N.V. v. Venezuela*, ICSID Case No.ARB/93/3, Decision on Objections to Jurisdiction, (1998) 37 *ILM (International Law Materials)*, in which the Tribunal concluded that “jurisdiction can exist even in respect of investments that are not direct, so long as the dispute arises directly from such transaction” (p. 1378).

¹⁷ S. Manciaux, “Jurisdiction Ratione Temporis and Existence of a Dispute: Some Remarks about ICSID Recent Case Law”, (2006) 6 *IBLJ (International Business Law Journal)*, p. 790.

¹⁸ *AMCO Asia Corporation and others v. Indonesia*, ICSID Case No.ARB/81/1, Resubmitted case, Decision on Jurisdiction, (1988) 3 *ICSID Rev. – FILJ (ICSID Review – Foreign Investment Law Journal)*.

¹⁹ *Ibid.*, paragraph 126.

²⁰ *CSOB v. Slovak Republik*, *supra* note 15, paragraphs 72-76.

The parties may define investment either in an agreement between the Contracting State and the investor, or in the national law of the Contracting State, or in a clause of a treaty accepted by the investor.²¹

It is argued that only “definitions of investment [that] are so disconnected from meaningfully economic activity as to be absurd”²² should be prohibited. As acknowledged by Professor Hiscock, “there is not and never has been a single authoritative legal definition of investment”²³, which varies according to the text and context where it is found. In BITs investment is usually described as “every kind of asset”²⁴ and also contains a list of typical rights, e.g. property rights, participation in companies, money claims and rights to performance, intellectual property rights and concession or similar rights.²⁵

Investment may occur by various activities of the investor which may arise from many forms of contracts. Even loans or purchase of bonds may qualify as investments²⁶, but single commercial transactions will not. It is generally acknowledged that investment must contribute to development and must “make a positive impact on a host State”.²⁷

In *Fedax vs. Venezuela* the tribunal summarized five common characteristics for every investment, which are – certain duration, regularity of profit and return, risk, substantiality, and development of the State.²⁸ Legal scholars and tribunal members, however, do not always follow this concept. Thus two approaches can be distinguished – the objectivist approach, which follows the core elements of investment described in *Fedax*, and the subjectivist approach, which tends to respect the will of the parties in defining the investment.²⁹

Tribunals tend to interpret the notion of investment liberally, with more respect to the will of the parties. This has been the case in several disputes concerning construction

²¹ Schreuer, *supra* note 6, p. 126.

²² J. D. Mortenson, “The Meaning of ‘Investment’: ICSID’s Travaux and the Domain of International Investment Law”, (2010) 51 *Harv. Int’l L.J. (Harvard International Law Journal)*, p. 261.

²³ M. E. Hiscock, “The Emerging Legal Concept of Investment”, (2009) 27 *Penn St. Int’l L. Rev. (Penn State International Law Review)*, p. 769.

²⁴ E.g., see Article 1 (a) of the Agreement on promotion and protection of investments between the Government of the Kingdom of Bahrain and the Government of the Kingdom of the Netherlands (5 February 2007). Available on the Internet at

<http://www.mof.gov.bh/showdatafile.asp?rid=1722&ftype=file1>. Last visited September 21, 2010.

²⁵ *Ibid.*

²⁶ See, in particular, *Fedax v. Venezuela*, *supra* note 16.

²⁷ Schreuer, *supra* note 6, p. 90.

²⁸ *Fedax v. Venezuela*, *supra* note 6, p. 1378.

²⁹ F. Yala, “The Notion of ‘Investment’ in ICSID Case Law: A Drifting Jurisdictional Requirement?” (2005) 2 *J.Int’l Arb. (Journal of International Arbitration)*, p. 106.

contracts. In *Salini*³⁰ the tribunal was asked whether a single construction contract can be considered as an investment for the purposes of ICSID jurisdiction. The tribunal analyzed the definitions of investment included in the contract and the BIT and recognized that the investor had made contributions in money, in kind, and in industry and skill for thirty-six months, and that both the investor and the State assumed risks. The tribunal then concluded that it had jurisdiction to hear the dispute, thus the construction constituted an economic development of the State and the contract created a “contractual benefit having an economic value”.³¹ This decision was upheld by the tribunal in *Bayindir v. Pakistan*³², a case concerning a straightforward highway, where the tribunal made exact reference to *Salini*.

In *Joy Mining* the contract was for supply of mining equipment, and the tribunal found it “a normal commercial transaction”.³³ The tribunal followed the objectivist approach and concluded that the contract did not constitute any risks for those normally associated with a sale transaction, nor was it a significant commitment.

A very liberal definition of investment was also rendered by the tribunal in *LESI*, where the tribunal decided that the investment’s contribution to the economic development of the host State was not “an essential prerequisite to being characterized as a protected investment within the meaning of the ICSID Convention”.³⁴

Liberalization of investment, however, did not go that far to qualify pre-investment expenditures as investment, as could have happened in *Mihaly*³⁵. Although the tribunal based its argumentation on documents exchanged by the parties, and they did not qualify unilaterally incurred expenditures as an “investment”, it did not examine the criteria of investment established in ICSID case-law.

The tribunal’s decision in *Mihaly* demonstrates that the “border” of the definition of an investment is not that far as investors could wish. Not surprisingly, the decision not to

³⁰ *Salini Costruttori S.p.A. and Italstrade S.p.A. v. The Hashemite Kingdom of Jordan*, ICSID Case No.ARB/02/13, Decision of the Tribunal on Jurisdiction, (2005) 20 *ICSID Rev. – FILJ (ICSID Review – Foreign Investment Law Journal)*.

³¹ *Salini v. Jordan*, *supra* note 30, p. 49.

³² *Bayindir Insaat Turizm Ticaret Ve Sanayi A.S. v. Islamic Republic of Pakistan*, ICSID Case No. ARB/03/29. Available on the Internet at

http://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=showDoc&docId=DC523_En&caseId=C27. Last visited September 21, 2010 (paragraph 127 *et seq.*).

³³ *Joy Mining Machinery Limited v. Arab Republic of Egypt*, ICSID Case No.ARB/03/11, (2004) 19 *ICSID Rev.—FILJ (ICSID Review – Foreign Investment Law Journal)*, p. 486.

³⁴ *LESI, S.p.A. and Astaldi, S.p.A. v. People's Democratic Republic of Algeria*, ICSID Case No. ARB/05/3, cited in W. Ben Hamida, E. Cabrol, F.Horchani, “International Investments: Law and Practice”, (2009) 5 *IBLJ (International Business Law Journal)*, pp. 645-646.

³⁵ *Mihaly International Corporation v. Democratic Socialist Republic of Sri Lanka*, ICSID Case No.ARB/00/2, (2002) 17 *ICSID Rev. – FILJ (ICSID Review – Foreign Investment Law Journal)*, p. 142.

consider “significant expenditures ... to prepare for consortium ... in reliance on the letter of intent and its two renewals” as an investment was severely criticized by J.M. Robinson, one of the representatives of Mihaly Corporation.³⁶

It is a common situation that a shareholding is also considered as an investment for the purposes of Article 25 of the Convention, usually by referring to “a company or shares of stock or other interests in a company or interests in the assets thereof”³⁷ as an investment. It may very often be the case that a locally incorporated company becomes bankrupt, or its property is being expropriated; then under this clause in a BIT a shareholder is entitled to bring a claim in his own name. In other words, the shareholder and not the entity is an investor in this situation, and this approach has been widely accepted by tribunals.³⁸

In conclusion, it is highly likely that many transactions may be qualified both as commerce and as investment; thus the tribunal should examine every definition of an investment with the greatest caution so as not to extend the definition of investment to any transaction an investor may have. If the parties have not agreed on something absurd as an investment, it is highly likely that the tribunal will decide that it has jurisdiction.

A simple commercial transaction should not constitute an investment for the purposes of ICSID jurisdiction, so that tribunals in defining investments should not limit their analysis to the broad definition in BITs, e.g. every kind of asset, but rather carefully examine whether the definition given in the BIT meets the requirements of Article 25 of the Convention. Thus J.M. Robinson’s assertion that “investment is intended to be construed expansively, to suit current needs and practices”³⁹ will hopefully be interpreted by tribunals with the utmost caution.

1.2 Requirement of *ratione personae* for jurisdiction

The requirement *ratione personae* (i.e., the parties have standing before the Centre) is perhaps the most important and the most problematic jurisdictional condition in the practice of the Centre. This requirement consists of two elements – one party to the dispute must be a

³⁶ M. J. Robinson, “ICSID Cases on its Jurisdiction: a Serious Problem for Public/Private Partnerships for Infrastructure in Developing Countries”, (2004) *Int’l. Bus. Law. (International Business Lawyer)*, December, pp. 263-265.

³⁷ Treaty between the United States of America and the Republic of Ecuador Concerning the Encouragement and Reciprocal Protection of Investment (27 August 1993). Available on the Internet at <http://www.state.gov/documents/organization/43558.pdf>. Last visited September 21, 2010.

³⁸ See, e.g., *American Manufacturing & Trading, Inc. v. Zaire*, ICSID Case No.ARB/93/1, Award, (1997) 36 *ILM (International Law Materials)*, p. 1531; *Alex Genin and others v. Republic of Estonia*, ICSID Case No.ARB/99/2, (2002) 17 *ICSID Rev.—FILJ (ICSID Review – Foreign Investment Law Journal)*, p. 395.

³⁹ Robinson, *supra* note 36, p. 265.

Contracting State or any constituent subdivision or agency of a Contracting State designated to the Centre by that State, and on the other side, there must be a national of another Contracting State.

This chapter aims to highlight the general principles in identifying the Contracting State party, since the nationals of another Contracting State will be analyzed in the next chapters.

1.2.1 Identifying the Contracting State party

The Convention, as specified in Article 25, is exclusively designed for mixed disputes or disputes between a State and an individual; thus it does not provide a forum for disputes between States, or between individuals.

The Convention, as stated in Article 67, is open for signature on behalf of States members of the International Bank for Reconstruction and Development (IBRD) and parties to the Statute of the International Court of Justice, if the Administrative Council of the Centre, by a vote of two-thirds of its members, has invited the party to the Statute to sign the Convention. Thus the Convention is open for signatures of 186 countries, and 144 countries have already become Contracting States of the Convention.⁴⁰

The list of Contracting States of the Convention is regularly updated and available on the Centre's website; therefore identifying a Contracting State causes no difficulties in the practice of the Centre.

A State may become a party to a dispute before the Centre only after it has ratified the Convention; thus "*ad hoc* use of Convention procedures by States that have not ratified the ICSID Convention is not possible".⁴¹ However, a State may agree to the jurisdiction of the Centre before it has signed the Convention, if it becomes a Contracting State at the moment of institution of proceedings.

Investment agreements are very often concluded by public companies or other public bodies, but identifying these bodies and determining their legal capacity to enter into an agreement is a more complex issue. The name and legal capacity of the public body which

⁴⁰ From 155 signatory states, 144 states have also deposited their instruments of ratification, acceptance or approval of the Convention and have become Contracting States. See Member States of the ICSID Convention. Available on the Internet at http://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=ShowHome&pageName=MemberStates_Home. Last visited September 21, 2010.

⁴¹ Schreuer, *supra* note 6, p. 142.

the Contracting State designates to the Centre⁴² would depend on the national law of the Contracting State, but the body should “perform public functions on behalf of the Contracting State or one of its constituent subdivisions”.⁴³

These bodies must be designated to the Centre, merely for purposes of legal certainty and to assure the investor that disputes arising out of an agreement are in the Centre’s jurisdiction. Designation of an entity to the Centre would certainly preclude the Contracting State from raising later objections on jurisdiction on the ground that that entity is not to be considered as a constituent subdivision or agency of the Contracting State. The status of an entity in any case is still an issue for the tribunal’s exclusive competence; hence only the tribunal itself may rule on its jurisdiction.

The tribunal found that it had no jurisdiction in *Cable TV v. St. Kitts and Nevis*⁴⁴, where the signatories were an investor and the Nevis Island Administration (NIA). St. Kitts and Nevis had not designed NIA as its agency or constituent subdivision; thus the dispute was outside the Centre’s jurisdiction.

In conclusion, identifying the State party in the Centre’s practice has not caused many difficulties. Investment agreements with States or their constituent divisions or agencies may contain an ICSID clause even before the State has ratified the Convention or designated the entity to the Centre. Such an agreement on ICSID arbitration will be valid if ratification or designation occurs before institution of proceedings.⁴⁵ The parties may not, however, bind the tribunal with any agreement regarding the status of a State entity: this issue is the tribunal’s exclusive competence.

If identifying the State party is relatively simple, tribunals have experienced much more difficulty in identifying the investor party, which without hesitation may be called the core problem of determining the Centre’s jurisdiction and which as the central issue of this thesis will be analyzed in detail in the next chapters.

⁴² E.g., Madagascar has designated Enterprise Nationale d’Hydrocarbure. A list of designations is available in Contracting States and Measures Taken by Them for the Purpose of the Convention. Available on the Internet at <http://icsid.worldbank.org/ICSID/Index.jsp>. Last visited September 21, 2010.

⁴³ C.F. Amerasinghe, “Jurisdiction Ratione Personae under the Convention on the Settlement of Investment Disputes between States and Nationals of Other States”, (1974/75) 47 *BYIL* (*British Year Book of International Law*), pp. 233/4, cited in Schreuer, *supra* note 6, p. 151.

⁴⁴ *Cable Television of Nevis, Ltd. and Cable Television of Nevis Holdings, Ltd. v. Federation of St. Kitts and Nevis*, ICSID Case No.ARB/95/2, Award, (1997) 13 *ICSID Rev.—FILJ* (*ICSID Review – Foreign Investment Law Journal*), p. 328.

⁴⁵ Schreuer, *supra* note 6, p. 156.

2 DETERMINING THE INVESTOR'S NATIONALITY

Although nationality forms the most important jurisdictional requirement, again no definition of nationality is given in the Convention, which often forms a basis for objections to jurisdiction for host States. The Convention in Article 25 (1) only states that the dispute must be between a Contracting State and “a national of another Contracting State”. Article 25 (2) then continues with a description of the qualities of an investor (person which implements an investment in the host State) to qualify as “a national of another Contracting State”.

Article 25 prescribes two situations – either an investor has a nationality of a Contracting State other than the State party to the dispute, or the parties have agreed to treat the investor as a national of another Contracting State because of foreign control.

As evidenced in the Centre's practice, the nationality of an investor, even if a definition of an investor is included in the BIT, may be a very complex issue for the tribunal to solve. The concept of foreign control has caused even more difficulties, and tribunals have applied this concept differently.

The present chapter analyses the concept of nationality under international law and describes the theories of determining nationality for individuals and legal entities. The chapter then addresses the specific requirements of nationality under the Convention and draws special attention to the exact wording of Article 25 of the Convention.

2.1 Nationality under international law

As the Permanent Court of International Justice (PCIJ) stated in *Mavrommatis Palestine Concessions*, a general principle of international law is that a State of which a national has suffered wrong in another State has a right to exercise diplomatic protection to protect its subjects.⁴⁶ Thus, as expressed by Brownlie,

a normal and important function of nationality is to establish the legal interest of a state when nationals, and legal persons with a sufficient connection with the state, receive injury or loss at the hands of another state.⁴⁷

Accordingly, questions of nationality fall within the jurisdiction of a State.⁴⁸

⁴⁶ *Mavrommatis Palestine Concessions Case*, *supra* note 9, pp. 6, 12.

⁴⁷ I. Brownlie, *Principles of Public International Law, Seventh Edition*, Oxford, University Press, 2008, pp. 477-478.

⁴⁸ Nationality Decrees Issued in Tunis and Morocco (Tunis / Morocco), (08.11.1921.), (1923) PCIJ, Ser. B, No.4, p. 24.

This reasoning was re-affirmed by the PCIJ in *Panevezys-Saldutiskis Railway*, where the Court emphasized that “by taking up a case on behalf of its nationals a State is in reality asserting its own right”.⁴⁹ However, the Court continued, this right is based upon “the bond of nationality”.⁵⁰

The bond of nationality must be real, in other words, a national must have an effective link with its country of nationality. The question whether an individual has a real and effective connection, a genuine link with its country of nationality, was the central issue in *Nottebohm*⁵¹, in which the Court denied Liechtenstein’s rights to enforce diplomatic protection. The Court found that a genuine connection with a State conferring nationality may be evidenced by the fact that the individual is “closely attached by his tradition, his establishment, his interests, his activities, his family ties”⁵² to that State, to form a nationality as

a legal bond having as its basis a social fact of attachment, a genuine connection of existence, interests and sentiments, together with the existence of reciprocal rights and duties.⁵³

However, when a dispute arises on nationality questions, the court cannot exclusively decide it in accordance with the national law of one of the parties to the dispute.⁵⁴ Instead, the court is entitled to carry out its analysis on whether there is a genuine link between the individual and the State and whether the nationality has not been acquired illegally. Article 41 of the Convention states that the tribunal is the judge of its competence; thus the tribunal also has powers to examine nationality issues.

The paper will proceed with a few remarks on nationality of individuals and then continue with a thorough analysis on nationality of legal persons.

⁴⁹ *Panevezys – Saldutiskis Railway Case* (Estonia / Lithuania), (28.02.1939.), (1939) PCIJ Series A/B, No. 76, p. 16. Braun, T.R. “Investor-State Mediation: Is There a Future?”, in Rovine, A.W. (ed.), *Contemporary Issues in International Arbitration and Mediation: The Fordham Papers*, Brill Academic Publishers, 2010, Vol. 3, pp. 374-375.

⁵⁰ *Ibid.*, p. 16.

⁵¹ *Nottebohm Case* (Liechtenstein / Guatemala), (06.04.1955.), (1955) ICJ Reports, p. 4.

⁵² *Ibid.*, p. 24.

⁵³ *Ibid.*, p. 23.

⁵⁴ *Award in the Arbitration Case between the Government of the United States of America and the Government of His Majesty the King of Egypt concerning the Claim of George J. Salem* (Egypt / The United States of America), (08.06.1932.), 2 *RIAA* (*Reports of International Arbitral Awards*), p. 1184. See also *Flegenhiemer Claim* (The United States of America / Italy), (1958) 25 *ILR* (*International Law Reports*), p. 149.

2.1.1 Nationality of individuals

Two general principles⁵⁵ are commonly recognized in international law for acquisition of nationality of individuals – *jus sanguinis* and *jus soli*. According to the *jus sanguinis* principle nationality is acquired by birth from a national of that particular country, and nationality by *jus soli* is acquired by birth within the territory of a particular country, or a combination of both principles is possible. The principle *jus sanguinis* exists in several modalities, regarding the status of father, or either parent, or the unmarried mother.⁵⁶

The principle *jus soli* is rather simple in comparison with *jus sanguinis*. As J.B. Scott points out, *jus soli* is an objective principle, thus it applies naturally, without regard to the nationality of the parents.⁵⁷ However, it is presumed that this principle should not apply automatically, e.g., to children of persons enjoying diplomatic immunity.⁵⁸

2.1.2 Nationality of legal entities

Domestic laws of the vast majority of States are silent⁵⁹ on issues regarding nationality of legal entities; thus the rules determining the nationality of legal entities have very much derived from those regarding the nationality of individuals, which in turn developed because of growing application of diplomatic protection. In essence, the nationality of a legal entity serves the same purpose as that of individuals, i.e. the entity should also have a genuine connection, a real and effective link with a State, especially for diplomatic protection purposes.

In 1919 E.M. Borchard pointed out that “[a] corporation may be attached to a territory by three elements”,⁶⁰ which are place of foundation, centre of administration, and place of exploitation. He then acknowledges that the majority of European countries follow the centre of administration (*siège social*), but the United States of America adheres to the principle of the place of incorporation.⁶¹

⁵⁵ See, e.g., Brownlie, *supra* note 47, p. 388.

⁵⁶ D. V. Sandifer, “Comparative Study of Laws Relating to Nationality at Birth and to Loss of Nationality”, (1935) 29 *Am. J. Int’l L. (American Journal of International Law)*, pp. 254, 255, 258. Available on the Internet at HEIN ONLINE database. Last visited October 10, 2010.

⁵⁷ J. B. Scott, “Nationality: Jus Soli or Jus Sanguinis”, (1930) 24 *Am. J. Int’l L. (American Journal of International Law)*, Issue 1, p. 59. Available on the Internet at HEIN ONLINE database. Last visited October 10, 2010.

⁵⁸ Article 12 of The Hague Convention on Certain Questions Relating to the Conflict of Nationality Laws (1930). League of Nations, 179 *Treaty Series*.

⁵⁹ Brownlie, *supra* note 47, p. 420.

⁶⁰ E.M. Borchard, *The diplomatic protection of citizens abroad or the law of international claims*, New York, The Banks Law Publishing Co., 1919, p. 617.

⁶¹ *Ibid.*, pp. 617-619.

The nationality of a legal entity was an issue of paramount importance in *Barcelona Traction*⁶², in which the International Court of Justice (ICJ) formulated several criteria for determining corporate nationality. The Court acknowledged that for purposes of diplomatic protection generally recognized criteria are the place of incorporation and the place of the registered office.⁶³ It further held that, although “no absolute test of the ‘genuine connection’ has found general acceptance”⁶⁴, different links are required by States to form an effective link with the State whose nationality is conferred. Thus, the nationality of a legal entity may be determined by applying several tests – test of incorporation, test of seat (*siège social*), and test of control.

According to the incorporation test, a legal entity acquires nationality by way of incorporation. This test obviously is the most applied and the simplest of all previously mentioned. However, it is very likely that for the purposes of diplomatic protection⁶⁵ this test would not create a genuine link with the State of incorporation, especially if the State is chosen only for its tax regime. The incorporation test is also criticized for being artificial and without practical significance; thus in reality a company is only a subject of national law.

The *siège social* or real seat test states that a legal entity possesses the nationality of its place of principal administration. Under this theory, establishing an administrative office within a State’s territory is a condition of incorporation, which creates a more effective link with the country of incorporation.⁶⁶

Another method to identify the nationality of a legal entity is the control test, which was developed to identify an effective link between a legal entity and a State. According to this test a legal entity has the nationality of its controlling shareholders, in other words, the control test “is an instance of ‘lifting the corporate veil’”.⁶⁷ Thus, when applying the control test, the nationality of the shareholders prevails over the nationality of the company. This test is becoming more and more popular and may be the most appropriate choice for identifying the nationality of multinational enterprises, and will be examined in detail in Chapter 3.

⁶² *Barcelona Traction, Light and Power Co., Ltd. (Belgium / Spain)*, (05.02.1970), (1970) ICJ Reports 1970, p. 4.

⁶³ *Ibid.*, paragraph 70.

⁶⁴ *Ibid.*, paragraph 70.

⁶⁵ See Staker, Ch., “Diplomatic Protection of Private Business Companies: Determining Corporate Personality For International Law Purposes”, (1990) *61 BYIL (British Yearbook of International Law)*, p. 161.

⁶⁶ P. Muchlinski, “The Diplomatic Protection of Foreign Investors: a Tale of Judicial Caution”, in C. Binder, U.Kriebaum, A.Reinisch, S.Wittich (eds), *International Investment Law for the 21st Century. Essays in Honour of Christoph Schreuer*, Oxford, University Press, 2009, p. 349.

⁶⁷ *Ibid.*, p. 350.

Application of the genuine link theory for the purposes of nationality of legal entities is criticized by R. Sloane, who suggests that nationality should be determined in terms of its functions.⁶⁸ Another approach in determining the nationality of legal entities was introduced by Linda A. Mabry, who created “an economic commitment test”, consisting of such factors as the geographic location of assets, the nature of those assets, the legal entity’s organizational structure and whether the entity is controlled by a foreign government.⁶⁹ This test has been created to protect national interests in the global economy and to recognize truly national companies mainly on economic terms. Both of these tests suggest that nationality should be determined according to economic realities, not just on artificial bonds.

In conclusion, nationality is a legal bond between an individual or a legal entity, and a State. To avail of being a national of a particular State, an effective link must exist between the State and the person claiming nationality of that State. Three main concepts for determining corporate nationality, based either on legal or factual connections between legal entities and States, have developed in international law – the test of incorporation, the real seat test, and the control test.

2.2 Nationality requirements under the Convention

According to Article 25 (1), only a dispute between a Contracting State and a national of another Contracting State qualifies for jurisdiction of the Centre, and several statements can be made from this wording. First, as previously mentioned,⁷⁰ the Centre is not a forum for disputes between nationals or between States but exclusively between a national and a State. Second, accordingly “a national” must possess the nationality of any Contracting State other than the party to the dispute; thus the Convention precludes stateless persons and dual nationals⁷¹ having a nationality of the host State from arbitration before the Centre.

Lastly, a national must be either a physical person or a legal entity; thus the Convention also precludes fully state-owned companies from arbitration with other Contracting States. This is evidenced also from the Preamble of the Convention, which states that the Contracting States in drafting the Convention have taken into consideration “the role of private international investment”.

⁶⁸ R. Sloane, “Breaking the Genuine Link: the Contemporary International Legal Regulation of Nationality”, (2009) 50 *Harv. Int'l L.J.* (*Harvard International Law Journal*), p. 1.

⁶⁹ L.A. Mabry, “Multinational Corporations and U.S. Technology Policy: Rethinking the Concept of Corporate Nationality”, (1999) 87 *Geo. L.J.* (*Georgetown Law Journal*), pp. 593-594.

⁷⁰ See Chapter 1.2.1. *supra*.

⁷¹ Schreuer, *supra* note 6, p. 271.

This chapter examines the exact wording of Article 25 of the Convention and aims to analyze the application of this article in the practice of tribunals.

2.2.1 The individual as a national of 'another Contracting State'

The Convention states different criteria for natural and legal persons to qualify as nationals of a Contracting State. As stated in Article 25 (2) (a), "national of another Contracting State" means any natural person who had the nationality of a Contracting State other than the State party to the dispute on the date on which the parties consented to submit such dispute to conciliation or arbitration as well as on the date on which the request was registered pursuant to paragraph (3) of Article 28 or paragraph (3) of Article 36, but does not include any person who on either date also had the nationality of the Contracting State party to the dispute.

Individuals have appeared as parties to the dispute before the tribunal only in relatively few cases, namely because private international investment in almost all cases is made by legal entities. As a result of the stricter criteria (two critical dates when the nationality requirements must be met) for natural persons than for legal entities, in some cases the Centre has denied jurisdiction. However, issues of *ratione personae* have not been examined in most of the cases involving individuals.

In *Soufraki v. The United Arab Emirates* the tribunal re-affirmed that States may decide who their nationals are, but "when, in international arbitral or judicial proceedings, the nationality of a person is challenged, the international tribunal is competent to pass upon that challenge".⁷² Article 25 (2) requires a national person to be a national of another Contracting State both at the moment of consent to the arbitration and at the moment of registering the dispute at the Centre. The tribunal ruled that Mr Soufraki had lost his Italian nationality under Italian law by acquisition of Canadian nationality while having residence there. The tribunal also noted that, had Mr Soufraki had both Italian and Canadian nationalities, it still would not have had jurisdiction; hence Italian nationality would not be considered as his "dominant nationality".⁷³

The tribunal is not bound by an agreement on nationality between parties. It is presumed that an agreement on nationality would create "a strong presumption in favour of

⁷² Hussein Nuaman Soufraki v. United Arab Emirates, ICSID Case No. ARB/02/7, (2005) 17 *World Trade and Arbitration Materials*, No.1, paragraph 55.

⁷³ *Ibid.*, paragraph 42. See also A.C. Sinclair, "Nationality of Individual Investors in ICSID Arbitration", (2004) 7 *ILR (International Law Review)*, pp. 192-193.

the existence of the stipulated nationality”;⁷⁴ however, it obviously would not create a nationality that does not exist.

In *Champion Trading Co.*⁷⁵ dual nationals of the United States of America and Egypt brought claims against Egypt on their behalf and on behalf of companies in which they owned shares. The tribunal stated that generally “the real and effective nationality was indeed relevant ‘unless an exception is clearly stated’”⁷⁶ and, since Article 25 (2) (a) explicitly excludes dual nationals the individuals had no *jus standi* in this case due to their Egyptian nationality. Interestingly, the tribunal ruled that claims brought by these individuals as shareholders were within the jurisdiction of the Centre, which is contrary to the Centre’s later decision in *Tokios Tokelés*.⁷⁷ It is argued by O.E. García – Bolívar that

if faced with the same issue *Tokios* addressed, i.e. a national investor disguised as a foreigner, the *Champion* Tribunal would have used the argument of unreasonable result and would have explored the purpose of the ICSID Convention in depth to declare that it did not have jurisdiction over a dispute between a national and its State.⁷⁸

No evidence, however, supports the argument that if the individuals were nationals of Egypt only this would have led to rejection of jurisdiction. In addition, Egypt did not raise any objections concerning the fact that, if the American nationality of the individuals had been disregarded, the dispute in reality would have been between Egypt and its own nationals.

Furthermore, the nationality requirement on two critical dates is not related to the concept of continuous nationality, known as a generally recognized prerequisite⁷⁹ for execution of diplomatic protection. The wording of the Convention, however, does not require continuity of nationality for a certain period, but rather relates to two distinct points in time. Thus, hypothetically an individual may acquire different nationalities between consent to arbitration and registration of the dispute.

⁷⁴ Schreuer, *supra* note 6, p. 269.

⁷⁵ *Champion Trading Company and Ameritrade International, Inc. v. The Arab Republic of Egypt*, ICSID Case No.ARB/02/9, Decision on Jurisdiction, (2004) 19 *ICSID Rev.—FILJ (ICSID Review – Foreign Investment Law Journal)*.

⁷⁶ *Ibid.*, p. 288.

⁷⁷ See *Tokios Tokelés v. Ukraine*, *infra* note 99.

⁷⁸ O.E. García-Bolívar, “The Issue of a Foreign Company Wholly Owned by National Shareholders in the Context of ICSID Arbitration”, (2006) 2 *TDM (Transnational Dispute Management)*, Issue 5. Available on the Internet at http://works.bepress.com/cgi/viewcontent.cgi?article=1009&context=omar_garcia_bolivar. Last visited October 10, 2010, p. 7.

⁷⁹ *Panevezys –Saldutiskis Railway Case*, *supra* note 49, p. 16. See also M.S. Duchesne, “The Continuous Nationality of Claims Principle: Its Historical Development and Current Relevance to Investor – State Investment Disputes”, (2004) 36 *Geo. Wash. Int’l L. Rev. (George Washington International Law Review)*, p. 788.

2.2.2 The legal entity as a national of ‘another Contracting State’

Nationality of legal entities in the arbitration of the Centre has been a highly debated issue between legal scholars for its inconsistent application by tribunals. Nationality requirements applicable to persons having legal personality⁸⁰ are prescribed in Article 25 (2) (b), which states that a national of another Contracting State shall be any juridical person which had the nationality of a Contracting State other than the State party to the dispute on the date on which the parties consented to submit such dispute to conciliation or arbitration and any juridical person which had the nationality of the Contracting State party to the dispute on that date and which, because of foreign control, the parties have agreed should be treated as a national of another Contracting State for the purposes of this Convention.

The second clause of Article 25 (2) (b) provides an exception that host State nationals are considered as nationals of another Contracting State if they are foreign controlled. The wording of Article 25 (2) (b) leaves open the question of which tests for determining corporate nationality are allowed under the Convention, and exactly whether the control test may be applied as a general rule in determining the nationality of a legal entity. This issue will be analyzed in the last chapter of this paper.

Regarding determination of corporate nationality, the tribunal in *SOABI*⁸¹ drew the same conclusion as the ICJ in *Barcelona Traction*⁸² by stating that “[a] s a general rule, States apply either the head office or the place of incorporation criteria in order to determine nationality”.⁸³ Hence the Convention does not define nationality; this question is left to the parties.

Also the Convention does not require an investor’s nationality to be specified in the agreement; however, for clarity parties may include Model Clause 6 in their agreement, stating that “[i] t is hereby stipulated by the parties that the Investor is a national of [name of another Contracting State]”.⁸⁴ Again, such an agreement cannot create a nationality that does not exist. As acknowledged by one commentator, any “reasonable criterion” of nationality should be accepted.⁸⁵ This opinion was tacitly upheld by the tribunal’s decision in *MINE v.*

⁸⁰ Schreuer, *supra* note 6, p. 459.

⁸¹ *Société Ouest Africaine des Bétons Industriels (SOABI) v. Senegal*, ICSID Case No.ARB/82/1, (1994) 2 *ICSID Reports*, cited in Schreuer, *supra* note 6, p. 280.

⁸² *Barcelona Traction Case*, *supra* note 62, paragraph 70.

⁸³ *SOABI v. Senegal*, *supra* note 81, pp. 180-181.

⁸⁴ ICSID Model Clauses, *supra* note 14, Article 6.

⁸⁵ C.F. Amerasinghe, “Submissions to the Jurisdiction of the International Centre for Settlement of Investment Disputes”, (1973/74) 5 *Journal of Maritime Law and Commerce*, p. 228, cited in Schreuer, p. 281.

Guinea,⁸⁶ where the tribunal accepted its jurisdiction, although the parties because of control had agreed to treat MINE as a Swiss company, notwithstanding the fact that it actually was incorporated in Liechtenstein, a non-signatory of the Convention. Thus the parties may also specify an investor's nationality according to the control test.

The three most popular approaches for defining foreign investors in the domestic legislation of the host State or in BITs are:

1) nationality is determined by the incorporation test

E.g. Article 1 (d) of the BIT between the United Kingdom and Uganda states that 'companies' are:

(i) in respect of the United Kingdom: corporations, firms and associations incorporated or constituted under the law in force in any part of the United Kingdom or in any territory to which this Agreement is extended in accordance with the provisions of Article 12;

(ii) in respect of Uganda: companies, firms, associations, partnerships, clubs incorporated or constituted under the law in force governing formation of companies in Uganda.⁸⁷

2) nationality is determined by the incorporation and *siège social* test

E.g. Article 1 (2) of the BIT between China and Portugal states that in respect of Portugal 'investor' means

legal entities, including companies, associations, partnerships and other organizations, incorporated or constituted under its laws and regulations and have their seats in Portugal.⁸⁸

3) nationality is determined by incorporation, *siège social* and control tests

E.g. Article 1 (b) of the BIT between Venezuela and the Netherlands states that 'nationals' are:

i. natural persons having the nationality of that Contracting Party;

ii. legal persons constituted under the law of that Contracting Party;

iii. legal persons not constituted under the law of that Contracting Party but controlled, directly or indirectly, by natural persons as defined in (i) or by legal persons as defined in (ii) above.⁸⁹

⁸⁶ Maritime International Nominees Establishment v. Republic of Guinea, ICSID Case No.ARB/84/4, (1997) 4 *ICSID Reports*, p. 61.

⁸⁷ Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Republic of Uganda for the Promotion and Protection of Investments (24.04.1998.). Available on the Internet at http://www.fco.gov.uk/resources/en/pdf/pdf17/fco_ref_ts33-98_uganda. Last visited October 10, 2010.

⁸⁸ Agreement between the People's Republic of China and the Portuguese Republic on the encouragement and reciprocal protection of investments (04.02.2010.). Available on the Internet at <http://tfs.mofcom.gov.cn/aarticle/h/au/201002/20100206775363.html>. Last visited October 10, 2010.

⁸⁹ Agreement on encouragement and reciprocal protection of investments between the Kingdom of the Netherlands and the Republic of Venezuela. Available on the Internet at

In conclusion, parties are free to determine the nationality of investors, and these agreements on nationality will be recognized by tribunals as long as they constitute any reasonable connection with the State whose nationality is conferred. Moreover, contrary to the requirements of the Convention relating to natural persons, nationality of legal entities is of relevance only at the date of consent; thus a hypothetical change of nationality cannot affect the company's access to the Centre.

3 NATIONALITY OF A LEGAL ENTITY 'BECAUSE OF FOREIGN CONTROL'

Countries, besides the general tests of incorporation and *siège social* used for determining the nationality of legal entities, in certain circumstances have tried to interpret the concept of nationality functionally. Nationality was relevant especially during the World Wars, when it was of great importance to determine the enemy character of corporations and property.

This approach was used by the English House of Lords⁹⁰ and also by the United States,⁹¹ and especially because of his German nationality, Friedrich Nottebohm acquired his nationality of Liechtenstein “to substitute ... his status as a national of a belligerent State that of ... a neutral State, with the sole aim of thus coming within the protection of Liechtenstein”.⁹²

The concept of foreign control, however, was introduced in the Convention for different motives. As a common practice, investors are often required to conduct their business through a locally organized entity, usually for reasons of control and supervision. By the fact of incorporation the legal entity acquires the nationality of the host State and thus the investor would lose standing before the Centre; hence without any agreement all the disputes between a State and its nationals fall within the jurisdiction of national courts. Therefore the drafters of the Convention agreed not to exclude foreign investors from the jurisdiction of the Centre for the fact that they have invested in the host State through a locally incorporated entity.⁹³ Actually Article 25 (2) (b) is of vital importance for investors; thus it gives them access to the Centre as a neutral forum.

“To pierce or not to pierce” the corporate veil – that has been a dilemma for tribunals many times, when it is argued by either of the parties that an investor actually, because of the nationality of its shareholders or management, is a national of another State, not that of incorporation. The dilemma has existed both in cases when either of the parties aims to extend jurisdiction, and to delimit the jurisdiction of the Centre, and tribunals have solved this dilemma controversially.

⁹⁰ See, e.g., *Daimler Co. Ltd. V. Continental Tyre and Rubber Co (Great Britain) Ltd.*, (1916) 2 AC 307 (HL), cited in Brownlie, *supra* note 47, p. 406.

⁹¹ See, e.g., *Clark v. Uberse Finan – Korporation AG*, (1947) 322 US 480, 488, cited in Muchlinski, *supra* note 66, p. 350.

⁹² *Nottebohm Case*, *supra* note 51, p. 26.

⁹³ *Schreuer*, *supra* note 6, p. 276.

Historically unsophisticated, the concept of foreign control has become one of the most controversial issues before tribunals, and so far no uniform practice of tribunals exists in determining and interpreting foreign control.

The chapter will begin with an overview of the concept of foreign control, and will continue with an analysis of tribunal practice in applying the foreign control concept with a particular emphasis on the distinction between direct and indirect control. The chapter will proceed with an in-depth analysis on interpretation of indirect control in tribunal decisions on jurisdiction.

3.1 The concept of foreign control

The Centre's jurisdiction, as expressed above,⁹⁴ extends only to disputes between a Contracting State and a 'national of another Contracting State'. Clause 1 of Article 25 (2) (b) expressly states that to qualify as a 'national of another Contracting State', a legal entity must have the nationality of a Contracting State other than the State party to the dispute on the date on which the parties consented to submit such dispute to conciliation or arbitration. However, an exception is included in Clause 2 of Article 25 (2) (b), which provides that in certain exceptions disputes between a Contracting State and legal entities of that State may also fall within the jurisdiction of the Centre. According to the wording of this Article, to bring disputes between a Contracting State and legal entities having the nationality of that same Contracting State, an agreement must be concluded between the parties to the dispute to treat the legal entity of the host State as a national of another Contracting State "because of foreign control", i.e. because of control by nationals of another Contracting State.

It is argued⁹⁵ that only tests of incorporation and *siège social* may be used to determine whether the investor is a legal entity incorporated in the host State. According to the author of the commentary on the Convention, Professor C.H. Schreuer, the control test cannot be used to determine the nationality of a legal entity; hence "control" is provided as an exception in Clause 2 of Article 25 (2) (b).⁹⁶ This reasoning has found tribunals' acceptance in several cases where the nationality of investors was determined by analyzing a legal entity's place of incorporation or the place of its head office. To illustrate, in *LETCO* the tribunal ruled that LETCO was a Liberian company; hence it was "incorporated under the laws of the

⁹⁴ See Chapter 1 *supra*.

⁹⁵ Schreuer, *supra* note 6, p. 292.

⁹⁶ *Ibid.*, p. 301.

Republic of Liberia”.⁹⁷ Similarly, in *Vacuum Salt* the tribunal found a legal entity to be “a corporation organized under the Companies Code, 1963 (Act 179), of Ghana”.⁹⁸

The approach of ignoring the control test in determining nationality was highly debated after Mr. Prosper Weil’s dissenting opinion in *Tokios Tokelés*.⁹⁹ In this case a dispute arose between Ukraine and Tokios Tokelés, a company incorporated in Lithuania, but 99% owned by Ukrainians. Ukraine and Lithuania in their BIT agreed that an investor is “any entity established in the territory of Ukraine [and Lithuania, respectively] in conformity with its laws and regulations”.¹⁰⁰

The company made investments in Ukraine through its subsidiary, Taki spravy. Ukraine argued that the dispute was actually between a State and its nationals; therefore it proposed that the tribunal should “disregard the Claimant’s state of incorporation and determine its nationality according to the nationality of its predominant shareholders and managers”.¹⁰¹ This argument was rejected by a majority of the tribunal, which stated that the parties have a broad discretion to define corporate nationality, and limitation of the definition by the test of incorporation is within the free will of the parties, which the tribunal must respect. The decision in this case again highlights that the control test is an exception to the general rules for determining the nationality of a legal entity, and it can be applied only by agreement between the parties.

The relationship between foreign control and agreement between the parties was examined by the tribunal in *LETCO*, where the tribunal found that

it must be presumed that where there exists foreign control, the agreement to treat the company in question as a foreign national is ‘because’ of this foreign control.¹⁰²

Therefore two requirements must be distinguished for valid existence of foreign control for the purposes of Article 25 of the Convention: objective presence of foreign control and host State approval of that presence in the form of an agreement on the Centre’s jurisdiction between the host State and the investor.

⁹⁷ Liberian Eastern Timber Corporation (LETCO) v. Liberia, ICSID Case No.ARB/83/2, (1994) 2 *ICSID Reports*, p. 346, cited in M.L. Moreland, “‘Foreign Control’ and ‘Agreement’ Under ICSID Article 25 (2) (b): Standards for Claims Brought by Locally Organized Subsidiaries Against Host States”, (2000) 9 *Currents: International Trade Law Journal*, p. 19.

⁹⁸ Vacuum Salt Products Ltd. v. Republic of Ghana, ICSID Case No.ARB/92/1, (1997), 9 *ICSID Rev.—FILJ (ICSID Review – Foreign Investment Law Journal)*, p. 73.

⁹⁹ Tokios Tokelés v. Ukraine, ICSID Case No.ARB/02/18, Decision on Jurisdiction, (2005) 20 *ICSID Rev.—FILJ (ICSID Review – Foreign Investment Law Journal)*, pp. 245-258.

¹⁰⁰ *Ibid.*, paragraph 18.

¹⁰¹ *Ibid.*, paragraph 22.

¹⁰² LETCO v. Liberia, *supra* note 97, paragraph 516.

3.1.1 Agreement on foreign control

Article 25 (2) (b) requires not only foreign control as a prerequisite to treat a locally incorporated entity as a national of another Contracting State, but also explicitly states that the parties must have an agreement on that. Thus, as the decision in *Tokios Tokelés* shows, without an agreement on nationality tribunals in determining nationality will use the traditional incorporation and *siège social* tests only. Furthermore, it is argued that “a causal connection must exist between the control and the agreement and ... that control is an objective requirement that may not be replaced by mere agreement”.¹⁰³

The Convention is silent on the form of agreement and does not state whether it should be explicit or implicit. For an explicit agreement Model Clause 7 suggests the parties agree that “although the Investor is a national of the host State, it is controlled by nationals of [name(s) of other Contracting State(s) and shall be treated as a national of [that]/[those] State[s] for the purposes of the Convention”.¹⁰⁴ E.g. Article 9 (5) of the BIT between Netherlands and Brazil states that

a legal person which is an investor of one Contracting Party and which before such a dispute arises is controlled by investors of the other Contracting Party shall in accordance with Articles 25 (2) (b) of the ICSID Convention for the purposes of the Convention be treated as a national of the other Contracting Party.¹⁰⁵

Notwithstanding the fact that the Convention categorically does not require an explicit agreement, the tribunal in *Holiday Inns* stated that

[S]uch an agreement should therefore normally be explicit. An implied Agreement would only be acceptable in the event that the specific circumstances would exclude any other interpretation of the intention of the parties.¹⁰⁶

In other cases¹⁰⁷ tribunals have found that the existence of an ICSID clause in the agreement is sufficient enough to conclude that the host State actually considered the investor as a foreign national. Therefore mere consent to the Centre’s jurisdiction in certain cases may be interpreted as recognition of foreign control.

¹⁰³ C.H. Schreuer, “Commentary on the ICSID Convention Articles 25 (cont), 26 and 27”, (1997) 12 *ICSID Rev.—FILJ (ICSID Review – Foreign Investment Law Journal)* p. 113, cited in Moreland, *supra* note 97, p. 22.

¹⁰⁴ ICSID Model Clauses, *supra* note 14, Article 7.

¹⁰⁵ Agreement on encouragement and reciprocal protection of investments between the Kingdom of the Netherlands and the Federative Republic of Brazil (25.11.1998.). Available on the Internet at http://www.sice.oas.org/Investment/BITSbyCountry/BITS/BRA_Netherlands.pdf. Last visited October 10, 2010.

¹⁰⁶ *Holiday Inns S.A. and others v. Morocco*, ICSID Case No.ARB/72/1. Unpublished, cited in Schreuer, *supra* note 6.

¹⁰⁷ See, e.g., *LETCO v. Liberia*, *supra* note 97.

However, no exact nationality need be indicated in the agreement. In fact, a company may be controlled by nationals from several Contracting States other than the host State but the nationality of the controlling company must be identified at the moment when the dispute is submitted to the Centre.

3.1.2 Existence of foreign control

Although the Convention does not define foreign control, the term has been explained in decisions of tribunals. As Schreuer points out,

the existence of foreign control is a complex question requiring the examination of several factors such as equity participation, voting rights and management. In order to obtain a reliable picture, all these aspects must be looked at in connection. There is no simple mathematical formula based upon shareholding or votes alone.¹⁰⁸

Foreign control, like nationality, is also an objective requirement¹⁰⁹ for the Centre's jurisdiction and cannot be replaced by agreement between the parties. Thus the tribunal is competent to examine whether foreign control over a local company exists. Tribunals have determined foreign control in various ways.

First, the most common way of controlling a locally incorporated entity is through ownership of shares in it. In *LETCO*¹¹⁰ the tribunal concluded that foreign control was established by the fact that the company was 100% owned and effectively controlled by French nationals. The tribunal added that "apart from French shareholdings, French nationals dominated the company decision making structure",¹¹¹ which resulted in the tribunal's finding that LETCO had standing before the Centre.

Tribunals have also exercised jurisdiction where foreign control constituted less than 100%. For instance, in *Klöckner v. Cameroon*¹¹² only 51% of shares were owned by Klöckner Industrie-Anlagen GmbH, but 49% by the Government of Cameroon. The tribunal also paid attention to the structure of management in the company, stating that it was comprised "almost exclusively of individuals recommended by Klöckner".¹¹³

¹⁰⁸ Schreuer, *supra* note 103, pp. 79-80. See also Amerasinghe, *supra* note 43, pp. 227, 264-265, cited in Vacuum Salt, *supra* note 98, paragraph 43.

¹⁰⁹ See Schreuer, *supra* note 6, p. 308.

¹¹⁰ *LETCO v. Liberia*, *supra* note 97, p. 351.

¹¹¹ *Ibid.*

¹¹² *Klöckner Industrie – Anlagen GmbH and others v. United Republic of Cameroon and Société Camerounaise des Engrais*, ICSID Case No. ARB/81/2, (1984) 1 *Journal of International Arbitration*, p. 145, cited in Schreuer, p. 309. See also *Cable TV v. St. Kitts and Nevis*, *supra* note 44, p. 369.

¹¹³ *Klöckner*, *supra* note 112, p. 14.

Another famous case is *Vacuum Salt v. Ghana*,¹¹⁴ where the claim was submitted by a minority shareholder owning only 20% of shares. The tribunal started its reasoning by noting that there is no particular percentage of shares that should constitute foreign control, and continued that 100% ownership “almost certainly would result in foreign control, and that a total absence of foreign shareholding would virtually preclude the existence of such control”.¹¹⁵ By denying jurisdiction because the claimant, a Greek national, in fact had more a technical than an administrative role in the company, not “capable of strongly influencing critical decisions on important corporate matters”,¹¹⁶ the tribunal cited Amerasinghe, who has asserted that

the concept of ‘control’ is broad and flexible... [T]he question is... whether the nationality chosen represents an exercise of a reasonable amount of control to warrant its choice on the basis of reasonable criterion.¹¹⁷

Moreland points out that to constitute foreign control for the purposes of the Convention a company should “probably own not less than 15% of the shares”,¹¹⁸ and that several steps might be taken by companies to establish direct foreign control, as “the inclusion of a ‘veto’ power or of an approval right of the majority shareholder in the local entity’s organizational documents” or “the appointment of members to the board of directors with some control over the local entity’s decision-making process”.¹¹⁹ However, it seems that no general formula exists in determining foreign control, and no evidence supports that 15% should be the minimum requirement of shares for foreign control purposes. In a joint venture, for example, several partners may hold an equal amount of shares; thus effective control may be found in, e.g. management.

Although foreign control should not be identified with exclusive control, undoubtedly 100% ownership would be recognized as foreign control. Conversely, foreign control could not be constituted without any ownership.

Second, foreign control may be realized indirectly, “through the control of a corporation of convenience”,¹²⁰ i.e. when an investor, controlling a locally incorporated entity, is controlled by nationals of other States. Tribunals have reached different conclusions

¹¹⁴ *Vacuum Salt v. Ghana*, *supra* note 98.

¹¹⁵ *Ibid.*, paragraph 43.

¹¹⁶ *Vacuum Salt v. Ghana*, *supra* note 98, paragraph 53.

¹¹⁷ Amerasinghe, C.F., *supra* note 43, pp. 227, 264-265.

¹¹⁸ Moreland, *supra* note 97, p. 20.

¹¹⁹ *Ibid.*, p. 20.

¹²⁰ *Ibid.*

on whether indirect control also constitutes foreign control for the purposes of Article 25 (2) (b).

In 1983 the tribunal in *AMCO Asia*¹²¹ delivered an opinion that indirect control does not constitute foreign control for the purposes of the Centre's jurisdiction. In this case AMCO Asia Corporation was the controller of locally incorporated P.T. Wisma Kartika, but AMCO Asia itself, as argued by Indonesia, was controlled by a Dutch citizen, through a company established in Hong Kong of which he was the main shareholder. The tribunal made a highly valuable remark by stating that the tribunal should not "take care of a control at the second, and possibly third, fourth, or fifth degree"¹²² of the person controlling the local entity. Regarding application of the control test to the controlling entity the tribunal explained that

the concept of nationality [under ICSID] is a classical one, based on the law under which the juridical person has been incorporated, the place of incorporation and the place of the social seat. An exception is brought to this concept in respect of juridical persons having the nationality, thus defined, of the Contracting State Party to the dispute, where said juridical persons are under foreign control. But no exception to the classical concept is provided for when it comes to the nationality of the foreign controller.¹²³

In this case, however, determining the controlling nationality was not of importance, hence all the countries involved were signatories of the Convention. Still unsupported, however, is the tribunal's argument that

the true nationality of the controller would have to be taken into account where, for political or economic reasons, it matters for the host State, had it known this nationality, would not have agreed to the arbitration clause.¹²⁴

Less than 10 years later, in 1994, the tribunal in *SOABI*,¹²⁵ with Aron Broches acting as president, reached a converse decision, i.e. that foreign control may be indirect. In this case SOABI, a locally incorporated entity, was controlled by Flexa, a company incorporated in Panama (a non-contracting State of the Convention), which in turn was controlled by Belgian nationals. Furthermore, there was at least one Belgian national in Flexa's management.

The tribunal acknowledged that limiting foreign control to direct control only would be contrary to the purpose of Article 25 (2) (b), i.e. "to reconcile, on the one hand, the desire of States hosting foreign investments to see those investments managed by companies as established under local law and, on the other hand, their desire to give those companies

¹²¹ *AMCO Asia v. Indonesia*, *supra* note 18.

¹²² *Ibid.*, p. 396.

¹²³ *Ibid.*

¹²⁴ *Ibid.*

¹²⁵ *SOABI v. Senegal*, *supra* note 81, p. 389.

standing in ICSID proceedings".¹²⁶ The tribunal then continued that Flexa actually had no resources to effectively control SOABI and that, just as the host State may require investment through a locally incorporated company, the investor would also like

to invest their funds through intermediary entities while retaining the same degree of control over the national company as they would have exercised as direct shareholders of the latter.¹²⁷

Certainly, foreign control must exist at the moment when the parties have agreed to treat the locally incorporated entity as a national of another Contracting State because of that control. However, the situation of foreign control may change after concluding the agreement, e.g. by transfer of shares. Theoretically this could raise the question whether the changes influence the status and standing before the Centre of the foreign controlled entity, compared to what the parties have agreed before.

Literally not, and this statement is supported by the tribunals,¹²⁸ since according to Article 25 (2) (b) foreign control must exist at the time of consent, but, as observed by one commentator,

it would seem somewhat anomalous to sustain ICSID jurisdiction if all objective elements for the investor's foreign nationality have disappeared by the time the proceedings are instituted.¹²⁹

A subsequent change of foreign control to nationals of non-Contracting States or to nationals of the host State may lead to a situation when, again, the dispute is between a State and its nationals, or between a State and nationals of non-signatory States. In both cases access to the Centre will then be given to persons to whom the Centre is not provided for. This situation, as one commentator observes, "would be contrary to the purposes of the Convention".¹³⁰

Although currently there is no case in which tribunals have dealt with the issue of decisive transfer of control after consent, a notable remark on critical dates of foreign control for the purposes of Article 25 (2) (b) was made by the tribunal in *Vacuum Salt*¹³¹ with Sir Robert Y. Jennings as the president. In its reasoning the tribunal upheld the interpretation of Article 25 (2) (b) that control must exist only at the date of consent, but raised doubts that a dispute before the Centre between a State and a previously foreign controlled locally

¹²⁶ *Ibid.*, paragraph 182.

¹²⁷ *Ibid.*

¹²⁸ *Ibid.*, p. 183.

¹²⁹ Schreuer, *supra* note 6, p. 325.

¹³⁰ W.M. Tupman, "Case Studies in the Jurisdiction of the International Centre for Settlement of Investment Disputes", (1986) 35 *ICLQ (The International and Comparative Law Quarterly)*, No.4, p. 836.

¹³¹ *Vacuum Salt v. Ghana*, *supra* note 98.

incorporated entity, all of whose shares have been transferred to nationals of that host State, would “lead to a result which is manifestly absurd or unreasonable”.¹³²

Thus, the real question which tribunals must solve is whether piercing or lifting the corporate veil or abstention from piercing the corporate veil creates a result that is reasonable and compatible with aims of the Convention.

As the tribunal in *Tokios Tokelés* noted, parties are free to agree on nationality, since the Convention is silent on this definition. And the majority ruling in both *AMCO*¹³³ and *Tokios Tokelés*¹³⁴ was exactly that – the parties had used the broad limits given to them in Article 25 of the Convention, and the parties had done it properly.

Similar arguments to Ukraine were raised by Romania in *Rompetrol*,¹³⁵ arguing that the dispute was in fact between a State and its own national, but only through a shell company incorporated in the Netherlands. The decision that the tribunal has jurisdiction, however, was taken unanimously. The tribunal’s ruling in this case also supports the opinion that Contracting States should be given the greatest latitude possible to define the nationality of investors for the purposes of the Convention. Thus it is the sole authority of the Contracting States to define the class of persons and entities which should enjoy the protection of a BIT. Furthermore, the tribunal asserted that

there is nothing illogical in looking first of all to whether the nationality criteria set forth in the [bilateral investment treaty] are satisfied before going on to examine whether there is anything in Article 25 of the Convention which stands in the way of giving effect to that.¹³⁶

Tribunals in their rulings have not taken into account that the Convention was drafted to promote the role of private international investment in economic development; thus disputes which in essence are between a State and its nationals should be left outside the jurisdiction of the Centre.

It is very likely that the strong dissenting voice of Mr. Prosper Weil in *Tokios Tokelés* would not have appeared if the company had been controlled by nationals of, for instance, Germany. What Mr. Weil was actually trying to say was that it was apparent in this case that the agreed nationality does not face economic reality.

¹³² *Ibid.*, p. 84.

¹³³ *AMCO Asia v. Indonesia*, *supra* note 18.

¹³⁴ *Tokios Tokelés v. Ukraine*, *supra* note 99.

¹³⁵ *The Rompetrol Group N.V. v. Romania*, ICSID Case No. ARB/06/3, (2008). Available on the Internet at http://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=showDoc&docId=DC697_En&caseId=C72. Last visited October 10, 2010.

¹³⁶ *Ibid.*, paragraph 82.

In December 2008, two years after the decision in *Rompetrol*, the tribunal in *TSA*¹³⁷ rendered a contrary decision to *Tokios Tokelés* and *Rompetrol*. The tribunal confirmed that, although nationality should basically be determined by using the traditional tests of incorporation and *siège social*, this literal interpretation may be contrary to common sense, which was exactly the issue in the two abovementioned decisions. The tribunal distinguished piercing the corporate veil under the first and second clauses of Article 25 (2) (b), stating that the text of the second clause itself authorizes the parties to agree to pierce the corporate veil.¹³⁸

The central issue in this case, however, was not the nationality of foreign control but the mere existence of foreign control, which last was examined by the tribunal in *Vacuum Salt* in 1994. In this case TSA was 100% controlled by TSI, a legal entity incorporated in the Netherlands. Conversely, Argentina claimed that TSI was controlled by an Argentinean national who directly or indirectly owned the majority of shares. TSA admitted that TSI was controlled by THOP, which in turn was controlled by an Argentinean national. Although TSA argued that another French national had rights to 75% of THOP's shares through a "fiduciary encumbrance"¹³⁹, it could not provide corroborating evidence on this issue. Therefore the tribunal concluded that it had no jurisdiction, since no real control by Dutch nationals was proven.

Importantly, the tribunal concluded that piercing the corporate veil is justified to identify the "ultimate" controllers of the legal entity by stating that

[i]t would not be consistent with the text, if the tribunal, when establishing whether there is foreign control, would be directed to pierce the veil of the corporate entity national of the host State and to stop short at the second corporate layer it meets, rather than pursuing its objective identification of foreign control up to its real source, using the same criterion with which it started.¹⁴⁰

Therefore it is highly likely that tribunals should be allowed to pierce the corporate veil even if the parties have agreed on nationality because of incorporation. As previously observed, agreement on nationality may only create a presumption, but still determining the nationality of a legal entity will be the tribunals' competence. Certainly tribunals should take

¹³⁷ *TSA Spectrum de Argentina S.A. v. Argentine Republic*, ICSID Case No. ARB/05/5, (2008). Available on the Internet at <http://www.arbitration.fr/resources/ICSID-ARB-05-5-Award-English.pdf>. Last visited October 10, 2010. A dissenting opinion by G. D. Aldonas and a concurring opinion by Professor G. M. Abi-Saab are attached to the Decision.

¹³⁸ *TSA v. Argentina*, *supra* note 137, paragraphs 140 *et seq.*

¹³⁹ *Ibid.*, paragraph 161.

¹⁴⁰ *Ibid.*, paragraph 147.

into account parties' submissions as to jurisdiction, especially when there is strong evidence that the investor is actually being controlled by nationals of the State party to the dispute. No single formula, however, in piercing the corporate veil should be created.

In conclusion, the economic realities of nationality and respecting the will of the parties are the two main issues between which tribunals must choose when piercing the corporate veil. As acknowledged by K. E. Lyons, "[i]t will only be a matter of time before the international community realizes the value in hearing cases where the parties are truly foreign nationals".¹⁴¹ However, in many cases it may be very complicated for the tribunal to find the exact controlling national through many degrees of control; thus piercing the corporate veil to the bottom would not always be possible and sometimes it may turn into a never-ending story.

Thus, first of all, jurisdiction should be determined according to the Convention and only then should the wording of the BIT be taken into account; this approach was taken by the tribunal in *TSA*.

Contracting States are free to impose stricter conditions for the requirement of foreign control in their BITs, but this does not much help the tribunal when the agreement contains no such restriction. Presumably, not every change of foreign control is of importance for the purposes of Article 25 (2) (b), but the tribunal should rather examine whether at the moment of registering the dispute the company is actually not effectively controlled by nationals of (a) the host State, or (b) nationals of a non-Contracting State.

The tribunal's lifting of the corporate veil is supported by Amerasinghe, who suggests that

the search [for nationality] should be pursued until foreign control by nationals of a Contracting State can be established. Once the appropriate foreign control has been found, the search should end.¹⁴²

This suggestion and the tribunal decision in *SOABI* are strong evidence that tribunals actually rule *in favorem jurisdictionis*, thus extending their jurisdiction.¹⁴³ The argument that

¹⁴¹ K.E. Lyons, „Piercing the Corporate Veil In the International Arena”, [2006] 33 *Syracuse J. Int'l L. & Com.* (*Syracuse Journal of International Law and Commerce*), p. 547. Available on the Internet at WESTLAW database. Last visited October 10, 2010.

¹⁴² C.F. Amerasinghe, “Interpretation of Article 25 (2) (b) of the ICSID Convention”, in Lillich, R.B., Brower, Ch.N. (eds), *International Arbitration In the 21st Century: Towards Judicialization and Uniformity?* Transnational Publishers, Inc., 1994, p. 236, cited in Schreuer, *supra* note 6.

¹⁴³ In fact, as observed by K. Mc Arthur and P.A. Ormachea, “during the first twenty-six years of ICSID's existence, there was not a single denial of jurisdiction, on any ground”, in K. Mc Arthur, P.A. Ormachea, “International Investor – State Arbitration: an Empirical Analysis of ICSID Decisions on Jurisdiction”, (2009) 28

jurisdiction should be upheld in every case before the Centre lacks justification because such extension of jurisdiction may be contrary to the Convention's aims, namely to promote and protect private international investment.

Although it is argued that the decision in *Tokios Tokelés* is supported by the majority of legal scholars,¹⁴⁴ it is doubtful whether a single approach can be used in every case in determining the nationality of a legal entity. Hypothetically, if all the Contracting States, or even two of them, conclude BITs and agree that the nationality "of another Contracting State" is determined according to the incorporation test, would not that allow nationals of host States to establish a "foreign" company and invest in their own host States and also claim the Centre's jurisdiction? At that moment the Centre as an international forum would completely lose its meaning. In the words of E.O. García-Bolívar, the formalistic approach taken by the tribunal in *Tokios Tokelés*

not only constituted an abuse of the legal personality of the Lithuanian company but also created a risk for the entire international investment arbitration system... As a result, the decision of *Tokios* not only failed to protect a truly foreign investment, it also failed to foster the economic development of the respondent state by opening a venue for local investors to sue their own countries.¹⁴⁵

It may be concluded that the tribunal in *SOABI* with its president Mr. Aron Broches actually created a double standard for determining foreign control. In its *favorem jurisdictionis* decision the tribunal did not address what would be the case if Flexa had been a Belgian company controlled by nationals of Panama.

In conclusion, no exact formula exists for determining whether a locally incorporated entity is under foreign control for the purposes of Article 25 (2) (b); thus the concept of foreign control must be applied flexibly and indirect control must be determined on a case-by-case basis.

3.2 Indirect control v. indirect claim

As examined previously, Article 25 establishes the outer limits of the Centre, which cannot be extended by agreement between the parties, e.g. the parties cannot agree on the

Rev. Litig. (University of Texas School of Law Publications Inc.). Available on the Internet at WESTLAW database. Last visited October 10, 2010.

¹⁴⁴ E.g., G. Wisner, N. Gallus, see in R.L. Astorga, "The Nationality of Juridical Persons in the ICSID Convention in Light of Its Jurisprudence", (2007) 11 *MPYUNL (Max Planck Yearbook of United Nations Law)*, p. 472.

¹⁴⁵ O.E. García – Bolívar, „Investor – State Disputes in Latin America: a Judgment on the Interaction Between Arbitration, Property Rights Protection, and Economic Development”, (2007) 13 *LBUSRAM (Law and Business Review of the Americas)*, p. 88. Available on the Internet at WESTLAW database. Last visited October 10, 2010.

nationality of an investor if there is no connection with the State whose nationality is conferred. Also, it is argued¹⁴⁶ that the parties cannot agree to consider every commercial activity as an investment. However, the parties can narrow the limits given in Article 25 of the Convention, e.g. by restricting the term “investment”. In other words, the jurisdiction of the Centre cannot extend across the borders stipulated in Article 25 of the Convention.

It is a common situation that investment occurs through a legal entity, frequently established in the host State. Indeed, a locally established entity is often convenient both for the host State and the investor. Thus very often a dispute may arise between a host State and its national, which precludes parties’ access to the Centre unless an agreement is concluded between the parties to treat the investor as a national of another Contracting State under Article 25 (2) (b).

For these reasons and bearing in mind that a shareholding may be covered by the term “investment” for the purposes of Article 25 of the Convention, the central question arises whether Article 25 of the Convention also covers indirect claims, i.e. claims

in which a shareholder requests compensation for damages resulting from a measure that was directed exclusively against the rights of the company in which it holds shares.¹⁴⁷

Recent case-law of the Centre shows strong inclinations to grant access to the Centre to shareholders in cases where a wrong has been done to the company. Thus this chapter aims to analyze the Centre’s jurisprudence on interpreting indirect claims. Due to significant application of ICJ decisions in the Centre’s decisions on jurisdiction, the paper will proceed with a general overview of indirect claims in ICJ jurisprudence.

3.2.1 Indirect claims in ICJ jurisprudence

Indirect claims have been the central issue before the ICJ in several cases – *Barcelona Traction*,¹⁴⁸ *ELSI (Elettronica Sicula S.p.A.)*,¹⁴⁹ and *Diallo*.¹⁵⁰ These cases are frequently cited by tribunals in their decisions on jurisdiction. The citations from these ICJ decisions, however,

¹⁴⁶ Schreuer, *supra* note 6, p. 131.

¹⁴⁷ G. Bottini, “Indirect Claims under the ICSID Convention”, (2008) 29 *U. Pa. J. Int’l L. (University of Pennsylvania Journal of International Law)*, p. 565. It should be noted that Dr. Bottini as a representative of Argentina was involved in several cases mentioned here before the Centre with Argentina as respondent, e.g., *CMS v. Argentina*, *infra* note 167; *Enron v. Argentina*, *infra* note 168; *Camuzzi v. Argentina*, *infra* note 169; *Sempra Energy v. Argentina*, *infra* note 170, and others.

¹⁴⁸ *Barcelona Traction Case*, *supra* note 62.

¹⁴⁹ *ELSI Case*, *infra* note 156.

¹⁵⁰ *Diallo Case*, *infra* note 158.

do not always reflect an idea which the tribunal is willing to affirm. Thus a general overview of these cases must be given before analysis of the Centre's jurisprudence.

In 1970 the ICJ heard a claim brought by Belgium against Spain on behalf of Belgian nationals who were shareholders of a company incorporated in Canada, which, in turn, was a shareholder of Barcelona Traction, Light and Power, Co., Ltd., a company incorporated in Spain. The Court's decision that it did not have jurisdiction in the case was considered a stroke for protection of shareholders under international law. However, this argument is incorrect.

The ICJ in its decision stated that it is an overall recognized doctrine of international law that a company has a distinct personality from its shareholders and only in exceptional cases is a legal entity not independent from its shareholders, for instance when legal personality is used for fraudulent purposes.¹⁵¹ In these cases, the ICJ acknowledged, disregarding the legal personality

has been found justified and equitable in certain circumstances or for certain purposes. The wealth of practice already accumulated on the subject in municipal law indicates that the veil is lifted, for instance, to prevent the misuse of the privileges of legal personality, as in certain cases of fraud or malfeasance, to protect third persons such as creditor or purchaser, or to prevent the evasion of legal requirements or of obligations,¹⁵²

or, in other words, the corporate veil may be lifted in exceptional circumstances.

According to this separation of personalities, a company cannot be held responsible for the actions of its shareholders, and shareholders cannot be made liable for the activities of their company, while the shareholders do not have access to the company's assets so long as the company is in existence. Generally, the status of a shareholder allows participation in management in the company and to a profit proportionally to the amount of shares each shareholder has. Actually, as acknowledged by one commentator,

[a] shareholder's only obligation is to pay for his shares; there is no other obligation, whether to contribute to the company, to participate in the management of the company, or even to participate in the election of the managers of the company.¹⁵³

Thus, as acknowledged by the ICJ, it would be only normal to grant a shareholder a right to claim for violation of its direct rights,

¹⁵¹ Barcelona Traction Case, *supra* note 62, paragraph 56.

¹⁵² *Ibid.*, paragraphs 56-57.

¹⁵³ V. Lowe, "Shareholders' Rights to Control and Manage: From Barcelona Traction to ELSI" in Ando, N., McWhinney, E., Wolfrum, W., (eds), *Liber Amicorum Judge Shigeru Oda*, London, Kluwer Law International, 2002, Vol. 1, p. 278.

distinct from those of the company, including the right to any declared dividend, the right to attend and vote at general meetings, the right to share in the residual assets of the company on liquidation.¹⁵⁴

The ICJ confirmed that

a wrong done to company frequently causes prejudice to its shareholders. But the mere fact that damage is sustained by both company and shareholder does not imply that both are entitled to claim compensation... Thus whenever a shareholder's interests are harmed by an act done to the company, it is to the latter that he must look to institute appropriate action; for although two separate entities may have suffered from the same wrong, it is only one entity whose rights have been infringed.¹⁵⁵

Protection of shareholders was also the key issue in *ELSI (Elettronica Sicula)*.¹⁵⁶ Here, as in *Barcelona Traction*, a claim was brought by a State before the ICJ on behalf of its nationals. The United States brought a claim against Italy on behalf of American shareholders of an Italian company ELSI, and the ICJ found that, contrary to its decision in *Barcelona Traction*, it had jurisdiction to hear the dispute.

However, *ELSI* should not be regarded as a change of practice in interpreting indirect claims established in *Barcelona Traction* for several reasons. First, Italy did not raise objections to the jurisdiction of the ICJ, and, second, Italy had violated shareholders' direct rights stipulated in the BIT. Third, the ICJ extended the term "interests" to property and disregarded Italy's argument that United States nationals owned nothing more than the shares of the entity, but property belonged to the legal entity itself.¹⁵⁷

Protection of shareholders under international law was also the issue in *Diallo (Republic of Guinea v. Republic of Congo)*,¹⁵⁸ where Guinea brought a claim before the ICJ on behalf of its national Mr Ahmadou Sadio Diallo, who was conducting business in Congo through two locally incorporated entities. The Court noted that in fact

Guinea seeks through its action to exercise its diplomatic protection on behalf of Mr. Diallo for the violation, alleged to have occurred at the time of his arrest, detention and expulsion, or to have derived therefrom, of three categories of rights: his individual personal rights, his direct rights as associé in Africom-Zaire and Africontainers-Zaire and the rights of those companies, by 'substitution'.¹⁵⁹

¹⁵⁴ *Barcelona Traction Case*, *supra* note 62, paragraph 47.

¹⁵⁵ *Ibid.*, paragraph 44.

¹⁵⁶ Case concerning the Elettronica Sicula S.p.A. (ELSI) (United States of America / Italy), (20.07.1989), ICJ Reports 1989.

¹⁵⁷ *ELSI Case*, *supra* note 156, paragraph 132.

¹⁵⁸ *Diallo Case (Guinea / Congo)*, Preliminary Objections, (24.05.2007). Available on the Internet at <http://www.icj-cij.org/docket/files/103/13856.pdf>. Last visited October 10, 2010.

¹⁵⁹ *Ibid.*, paragraph 31.

Although Guinea argued that “in fact and in law it was virtually impossible to distinguish Mr. Diallo from his companies”,¹⁶⁰ the Court, after recalling its decision in *Barcelona Traction*, ruled that Guinea lacked standing regarding the rights of the two companies.

The Court affirmed once again that protection of shareholders is not governed by customary law and referred to BITs as sources governing the protection of shareholders.¹⁶¹ Thus, it may be concluded that BITs do not contain customary law regarding protection of shareholders. A legal entity has its own rights which are separate from those of its shareholders; thus while a company exists, even if “paralyzed”, its shareholders have no access to company assets.

The crucial issue here is actually whether the State by its actions has violated direct shareholder rights or rights of the company and whether shareholders are entitled to claim for both violations.

3.2.2 Indirect claims in ICSID jurisprudence

As ruled in *Barcelona Traction*,¹⁶² customary international law does not allow indirect claims by shareholders, nor does the Convention. Under Article 25 (2) (b) of the Convention, which forms its “outer limits”, shareholders are entitled to bring a claim before the Centre only in exceptional cases, i.e. when there is consent that a locally incorporated entity is treated as a national of another State for the purposes of the Convention. During the drafting of the Convention the possibility to grant shareholders of locally incorporated entities access to the Centre on behalf of the entity was completely discarded;¹⁶³ therefore Article 25 (2) (b) was introduced.

Certain direct rights are granted to shareholders in BITs, e.g. the right to be treated fairly and equitably, and disputes arising from infringement of these rights lie within the jurisdiction of the Centre. It is very likely that shareholders will also be willing to submit to the Centre disputes which affect the rights of the company. However, BITs are not capable of extending the Centre’s jurisdiction, as stipulated in Article 25 of the Convention.

Exceptions are possible under the North America Free Trade Agreement (NAFTA), but under strict conditions only. E.g., Article 1117 prescribes that the controlling (directly or indirectly) investor in certain cases is entitled to bring a claim on behalf of a legal entity, but

¹⁶⁰ *Ibid.*, paragraph 56.

¹⁶¹ *Ibid.*, paragraph 88.

¹⁶² *Barcelona Traction*, *supra* note 62.

¹⁶³ Convention History, *supra* note 11, pp. 360, 396, 397, 446, 447, 449, 538, 705, 709, 871.

in any case restitution of property or monetary damages and interest would be made to the legal entity.¹⁶⁴

It may be concluded that indirect claims by shareholders are incompatible with the Convention, thus falling beyond the “outer limits” of the Convention stipulated in Article 25. BITs cannot broaden the limits of jurisdiction prescribed in Article 25 of the Convention. However, tribunals have not reached this conclusion unanimously.

After the Centre’s first decision on indirect control in *AMCO* in 1983,¹⁶⁵ which stated that control should not be examined beyond the first level, and the decision in *SOABI*¹⁶⁶ that control may be indirect when it is performed through a company of convenience, tribunals have reached controversial decisions on indirect control issues. Moreover, it is likely that the tribunal in *AMCO* denied that foreign control might be indirect only because it had already found jurisdiction to hear the case. Acceptance of indirect control and piercing the corporate veil in the next level might have led to a decision that the tribunal had no jurisdiction. On the contrary, what if the *SOABI* tribunal pierced the veil in the second, or third, or fourth level if it had determined that the dispute was within its jurisdiction after piercing the veil at the first level, or even without piercing the veil at all? It is highly likely that the tribunal would have refrained from piercing the veil if it had found that the dispute was within its jurisdiction. However, tribunal decisions are still controversial on this matter.

Objections to jurisdiction were raised by Argentina in a series of cases which arose before the Centre after Argentina’s crisis in 2001-2002. With Argentina as the respondent, in most of the cases the investment was made through locally incorporated entities and claims were submitted by investors mainly on the basis that Argentina’s actions had significantly decreased the value of companies in which they held shares.

Thus claims before tribunals were brought by shareholders of locally incorporated entities and Argentina raised objections to shareholders’ *jus standi*. To illustrate, a closer examination of *CMS v. Argentina*,¹⁶⁷ *Enron v. Argentina*,¹⁶⁸ *Camuzzi v. Argentina*,¹⁶⁹ and *Sempra*

¹⁶⁴ North America Free Trade Agreement. Available on the Internet at <http://www.nafta-sec-alena.org/en/view.aspx?conID=590>. Last visited October 10, 2010. See also, e.g., Article 10.16 of the United States of America – Peru Trade Promotion Agreement (12.04.2006.). Available on the Internet at <http://www.ustr.gov/trade-agreements/free-trade-agreements/peru-tpa/final-text>. Last visited October 10, 2010.

¹⁶⁵ *AMCO v. Indonesia*, *supra* note 18.

¹⁶⁶ *SOABI v. Senegal*, *supra* note 81.

¹⁶⁷ *CMS Gas Transmission Company v. Argentine Republic*, ICSID Case No.ARB/01/8, Decision on Objections to Jurisdiction, (2003) 7 *ICSID Reports*.

¹⁶⁸ *Enron Corporation and Ponderosa Assets, L.P. v. Argentine Republic*, ICSID Case No.ARB/01/3, Decision on Jurisdiction (Ancillary Claim). Available on the Internet at http://ita.law.uvic.ca/documents/Enron-Jurisdiction_000.pdf. Last visited October 10, 2010.

*v. Argentina*¹⁷⁰ will be further provided. Notably, the president appointed by the Centre in all these cases was the former president of the Administrative Tribunal, Professor Dr. Francisco Orrego Vicuña, and in three of these cases (except Enron) the Honorable Marc Lalonde appeared as an arbitrator. Decisions on jurisdiction were taken unanimously and no dissenting opinion was submitted by any member of the tribunals.

In three of these cases (except *Camuzzi*) the Argentina–U.S. BIT¹⁷¹ (the Treaty) was involved. According to Article 1 of the Treaty,

a) "investment" means every kind of investment in the territory of one Party owned or controlled directly or indirectly by nationals or companies of the other Party, such as equity, debt, and service and investment contracts; and includes without limitation:

(i) tangible and intangible property, including rights, such as mortgages, liens and pledges;

(ii) a company or shares of stock or other interests in a company or interests in the assets thereof;

(iii) a claim to money or a claim to performance having economic value and directly related to an investment;

(iv) intellectual property which includes, inter alia, rights relating to: literary and artistic works, including sound recordings, inventions in all fields of human endeavour, industrial designs, semiconductor mask works, trade secrets, know-how, and confidential business information, and trademarks, service marks, and trade names; and

(v) any right conferred by law or contract, and any licenses and permits pursuant to law.¹⁷²

In these cases claims were brought by shareholders, who claimed that their capability to claim independently from locally incorporated entities arose directly from the Treaty, since shareholding is an investment under Article 1 (a) (ii) of the Treaty. However, in neither of these cases were shareholders parties to the contract.

In *CMS*,¹⁷³ the first case before the Centre against Argentina after its financial crisis, CMS Gas Transmission Company (CMS) owned 29.42% of Transportadora de Gas del Norte (TGN), which had a license for transportation of gas issued by Argentina. Various measures taken by Argentina "led to the devaluation of currency and the adoption of additional

¹⁶⁹ *Camuzzi International S.A. v. Argentine Republic*, ICSID Case No. ARB/03/2, Decision on Objections to Jurisdiction. Available on the Internet at <http://ita.law.uvic.ca/documents/camuzzijurisdiction.pdf>. Last visited October 10, 2010.

¹⁷⁰ *Sempra Energy International v. Argentine Republic*, ICSID Case No. ARB/03/7, Decision on Objections to Jurisdiction (2005). Available on the Internet at http://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=showDoc&docId=DC509_En&caseId=C8. Last visited October 10, 2010.

¹⁷¹ Treaty between the United States of America and the Argentine Republic Concerning the Reciprocal Encouragement and Protection of Investment (14.11.1991). Available on the Internet at http://www.unctad.org/sections/dite/ia/docs/bits/argentina_us.pdf. Last visited October 10, 2010.

¹⁷² *Ibid.*, Article 1.

¹⁷³ *CMS v. Argentina*, *supra* note 167.

financial and administrative measures also alleged to have an adverse impact on investors".¹⁷⁴ CMS claimed that the measures taken by Argentina "have significantly affected the value of its investment".¹⁷⁵ CMS stressed that the measures were not of a general nature and that its claim

is not founded on the devaluation of the peso, but rather on the loss in value of its investment due to Argentina's dismantling of the dollar-based tariff regime.¹⁷⁶

Argentina argued that CMS was not a party to the license agreement, but only a minority shareholder of the licensee, TGN, thus only TGN was entitled to claim.¹⁷⁷ However, since TGN was an Argentinean company, it did not have *jus standi* before the Centre; thus CMS was claiming for indirect damage. Nonetheless, CMS stressed that it had "a right of action independently from TGN",¹⁷⁸ since its participation in TGN qualified as an investment under the BIT.

The tribunal then examined the ICJ decision in *Barcelona Traction*,¹⁷⁹ which was used by both parties in support of their arguments. By noting that *Barcelona Traction* was merely concerned with issues of diplomatic protection and that the ICJ in *ELSI* had accepted the diplomatic protection of shareholders, the tribunal then concluded that there is

no bar in current international law to the concept of allowing claims by shareholders independently from those of the corporation concerned, not even if those shareholders are minority or non-controlling shareholders.¹⁸⁰

Argentina's most important objection to jurisdiction was that

an investment in shares is indeed a protected investment under the Treaty, but this would only allow claims for measures affecting the shares as such, for example, expropriation of the shares or interference with the political and economic rights tied to those shares.¹⁸¹

It was argued by Argentina that the Treaty does not allow indirect claims; otherwise this would be stipulated in it as in other treaties.

CMS, however, mistakenly interpreted this argument brought up by Argentina by stating again that it had a right to claim independently from TGN. By CMS's reasoning, the real affected interests were those of CMS, hence Argentina had "expressly invited CMS to

¹⁷⁴ *Ibid.*, paragraph 20.

¹⁷⁵ CMS v. Argentina, *supra* note 167, paragraph 24.

¹⁷⁶ *Ibid.*, paragraph 30.

¹⁷⁷ *Ibid.*, paragraph 36.

¹⁷⁸ *Ibid.*, paragraph 40.

¹⁷⁹ *Barcelona Traction*, *supra* note 62.

¹⁸⁰ CMS v. Argentina, *supra* note 167, paragraph 48.

¹⁸¹ *Ibid.*, paragraph 59.

participate in local companies”.¹⁸² According to the tribunal, whether the investor is a party to an agreement is immaterial for the purposes of finding jurisdiction, since there is a direct right of action of shareholders.¹⁸³

Thus the tribunal did not make a distinction between indirect rights and indirect claims. In other words, the fact that investors have a right to claim independently from the company does not indicate under which circumstances shareholders will have *jus standi* under the BIT.

In *CMS*, there was no agreement to treat TGN as a foreign national because of foreign control. Thus CMS claimed that it had the right to claim for compensation “in the case of a dispute that arises directly out of its investment in those [29.42%] shares”.¹⁸⁴ CMS was claiming for its own losses which resulted from unlawful reduction of CMS’s earnings.

In its Annulment Memorial Argentina asserted that

in its process of decision, the Tribunal was trying to determine whether shareholders have a direct right of action, when it should have considered (and never did) whether CMS was *invoking it [sic!] own rights in the proceedings*. In order to determine the latter, it is obviously material whether the investor is a party to a concession agreement or a license agreement with the host State. The Tribunal had limited jurisdiction over that part of the investment dispute that concerned CMS’ rights as shareholder; it did not have jurisdiction over any part of any investment dispute concerning the rights of the party to the concession agreement or License”.¹⁸⁵

Argentina stressed that “CMS was concerned not with its rights as shareholder, but with the alleged ‘dismantling’ of a tariff regime that granted rights to TGN, not to CMS”.¹⁸⁶ The CMS Annulment tribunal, however, by stating that CMS was an investor under the BIT which had made an investment in TGN, ruled that the tribunal had not manifestly exceeded its powers in determining CMS’s *jus standi*.¹⁸⁷ Again, by stating that shareholders in general are entitled to claim under the BIT the Annulment tribunal did not address the issue whether CMS was invoking its or TGN’s rights in the proceedings. Moreover, it is unquestionable that shareholders are entitled independently to invoke their own rights and not those of the company.

¹⁸² *Ibid.*, paragraph 60.

¹⁸³ *Ibid.*, paragraph 65.

¹⁸⁴ *CMS v. Argentina*, *supra* note 167, paragraph 67.

¹⁸⁵ *CMS Gas Transmission Company v. Argentine Republic*, ICSID Case No. ARB/01/8, Decision of the *ad hoc* committee on the application for annulment of the Argentine Republic, (2007). Available on the Internet at http://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=showDoc&docId=DC687_En&caseId=C4, paragraph 64. Last visited October 10, 2010.

¹⁸⁶ *Ibid.*, paragraph 65.

¹⁸⁷ *Ibid.*, paragraph 76.

As argued by Bottini,

the Tribunal confused the issues of whether shares can be an investment under Article 25 of the ICSID Convention and whether ICSID's jurisdiction can extend to indirect investments, with the determination of which rights a shareholder can claim. The fact that shares can constitute an investment under the ICSID Convention and that ICSID's jurisdiction can extend to indirect investments, does not alter (and does not even relate to) the fact that under the ICSID Convention shareholders are not allowed to claim for damages suffered by the company.¹⁸⁸

Thus, in reality the tribunal did not discuss whose rights had been invoked.

In *Enron*, Enron Corporation and Ponderosa Assets, L.P. brought actions before the Centre in two cases in February 2001 and March 2003 concerning "certain tax assessments allegedly imposed ... in respect to a gas transportation company in which the Claimants participated through investments in various corporate arrangements",¹⁸⁹ and an ancillary claim to the first one.

Here, Enron was not a direct but an indirect shareholder, since through various companies it held 35.263% of shares in gas company Transportadora de Gas del Sur (TGS). Again, one of Argentina's objections to jurisdiction was that the actions taken by Argentina directly affected only its national, TGS. Therefore, as argued by Argentina,¹⁹⁰ Enron as a minority shareholder of TGS might be affected only indirectly, and the BIT does not support claims for indirect damages. Moreover, Argentina acknowledged that

claims can only be made in respect of measures affecting *the shares qua shares* [emphasis added], as in the event of expropriation of the shares or other measures affecting directly the economic rights of the shareholders.¹⁹¹

The tribunal with Professor Francisco Orrego Vicuña as the president, however, once again referred to shareholders' rights to claim separately from the company and that the broad definition of investment given in the BIT favoured Enron's *jus standi* before the Centre. The tribunal was also not confused by Argentina's argument that

if minority shareholders can claim independently from the affected corporation, this could trigger an endless chain of claims, as any shareholder making an investment in a company that makes an investment in another company, and so on, could invoke a direct right of action for measures affecting a corporation at the end of the chain.¹⁹²

¹⁸⁸ Bottini, *supra* note 147, p. 596.

¹⁸⁹ Enron Corporation v. Argentina, *supra* note 168.

¹⁹⁰ *Ibid.*, paragraph 34.

¹⁹¹ Enron v. Argentina, *supra* note 168, paragraph 35.

¹⁹² *Ibid.*, paragraph 50.

The tribunal acknowledged that “there is indeed a need to establish a cut-off point beyond which claims would not be permissible as they would have only a remote connection to the affected company”.¹⁹³ The tribunal placed emphasis on the consent to arbitration of the host State, by stating that consent given in respect of an investor and an investment is an indicator that claims brought by that investor are admissible under the BIT.¹⁹⁴ Here, the tribunal stressed that the fact that Argentina had explicitly invited Enron and Ponderosa Assets to participate in the privatization of TGS was decisive to conclude that both claimants had *jus standi* before the Centre.

In September and November 2002 and April 2003 Camuzzi International S.A.¹⁹⁵ and Sempra Energy International¹⁹⁶ commenced arbitrations against Argentina concerning their investment in two gas distribution companies – Camuzzi Gas del Sur S.A. (CGS) and Camuzzi Gas Pameana S.A. (CGP). Decisions on objections to jurisdiction were taken separately by the same members of the tribunal with Professor Francisco Orrego Vicuña acting as president.

Sempra and Camuzzi together owned 100% of Sodigas Sur S.A. and Sodigas Pampeana S.A., companies incorporated in Argentina, where Sempra owned 43.09% and Camuzzi owned 56.91%. Sodigas Sur S.A. and Sodigas Pampeana S.A., in turn, were shareholders of CGS CGP with 90% and 86.09% ownership, respectively.¹⁹⁷

Argentina raised several objections to the *jus standi* of Sempra and Camuzzi, by asserting that the actions taken by Argentina could have only have affected CGS and CGP as holders of licenses, not as its shareholders. Moreover, as argued by Argentina, the claimant could only have a right to claim if there was a legal dispute arising directly out of the investment, i.e.

if it could prove that a legal right it possessed in its capacity as shareholder had been violated, causing it a direct loss. If it were a matter of a mere interest affected as a result of a measure that affects the company in which it is a shareholder, it is then the company that is entitled to claim and not the shareholder.¹⁹⁸

Argentina continued its objection by stating that

¹⁹³ *Ibid.*, paragraph 52.

¹⁹⁴ *Ibid.*

¹⁹⁵ Camuzzi v. Argentine, *supra* note 169.

¹⁹⁶ Sempra Energy v. Argentina, *supra* note 170.

¹⁹⁷ *Ibid.*, paragraph 19; Camuzzi, *supra* note 169, paragraph 9.

¹⁹⁸ Sempra Energy v. Argentina, *supra* note 170, paragraph 59; Camuzzi v. Argentina, *supra* note 169, paragraph 45.

in this case ... no right of [Sempra / Camuzzi] has been expropriated or treated unjustly and, if there had been such a violation, only the licensees could consider themselves the holders of the right entitling them to claim; [Sempra's / Camuzzi's] claim is based solely on the decrease of the company's value and how that impacts the proportional part owned by it as a shareholder.¹⁹⁹

The tribunals, however, did not discuss the issue of whose rights the claimants in reality were invoking, but rather in upholding their jurisdiction mainly focused on the broad definitions of investment given in the BITs.

In conclusion, it is a common situation that shareholders are given access to the Centre by including shares in the definition of an investment in BITs. Thus by bringing their claims to the Centre shareholders are in reality asserting their own rights under BITs. If a BIT does not include shares in the definition of investment, a shareholder would not have *jus standi* before the Centre. Nonetheless, a shareholder would not be entitled to receive benefits provided for the company and without an additional agreement would not be held liable for, e.g. non-performance of a contract.

Tribunals, however, have been rather torpid in examining whether every action against a company automatically results in a violation of shareholder rights. Hypothetically, if it is presumed that a company is incorporated in the host State to gain profit and a host State violates an agreement concluded between the company and the host State, then, as a result, the company would gain less profit. If the ICJ in *Barcelona Traction*²⁰⁰ acknowledged that shareholders may claim only in exceptional cases, e.g. in case of expropriation of shares, tribunals have very much extended shareholders' rights to bring claims for a wrong done to the company, thus extending their jurisdiction beyond the outer limits of the Convention.

It is very likely that claims brought by shareholders will create a situation of double recovery, since not only shareholders but also the company would claim compensation. This issue has been highlighted by tribunals but no one has addressed this question in essence by merely stating that

neither is there any evidence for believing there could be an endless chain of indirect claims, as in fact has not happened, nor could there be a double recovery for damages or the rights of creditors become subordinated to shareholders' claims.²⁰¹

Thus double recovery could become the most acute problem of a too broad interpretation of shareholders' rights to bring claims for a wrong done to their 'investment'.

¹⁹⁹ *Ibid.*, paragraph 60; *Camuzzi v. Argentina*, *supra* note 169, paragraph 46.

²⁰⁰ *Barcelona Traction*, *supra* note 62.

²⁰¹ *Sempra Energy v. Argentina*, *supra* note 170, paragraph 65.

In conclusion, shareholders are entitled to bring claims if shares are included in the definition of investment in BIT and if the host State has violated shareholders' rights. However, tribunals in their decisions on jurisdiction have not made a distinction between indirect control and indirect claims.

CONCLUSION

The freedom given to the parties to define what qualities an investor must meet to qualify as a national of another Contracting State is a significant accomplishment of the Convention's drafters. The only limitation to application of this freedom is that it must meet the outer jurisdictional limits stated in Article 25 of the Convention.

The Centre's case-law demonstrates that the jurisdictional requirements prescribed in Article 25 of the Convention have not been a serious barrier to tribunals in acceptance of jurisdiction over a dispute. An excessive application of the principle *in favorem jurisdictionis* in some cases has led to a result which is incompatible with Convention aims – to promote the economic development of States and the role of private international investment of nationals of other States therein.

The extreme rarity of declining jurisdiction and tendentious inclination to decide in favour of investors has created an imbalance in rights and obligations between investors and host States. The Convention was drafted in the interests of both investors and States; thus it should not be interpreted in a one-sided manner and a more balanced approach to accepting jurisdiction should be taken by tribunals.

Nationality must be applied functionally and in a manner that meets the fundamental goals of the Convention. The principal goal of the concept of nationality for reasons of the Convention is to ensure that the dispute is of international character. Although tribunals are not bound by the parties' agreement, the jurisdiction of the Centre is embraced by provisions of the Convention and of the BIT; however, the treaty cannot enlarge the scope of the Convention.

Globalization processes have intensely influenced investment arbitration; thus obviously concepts of nationality in investment law must be reviewed so that they meet the economic realities of foreign investment. The test of incorporation to determine the nationality of an investor should not be applied in cases where nationals of the host State or a non-contracting State have incorporated a legal entity in another Contracting State to enjoy treaty protection for their investments. Thus piercing the corporate veil as an alternative in determining nationality should be applied by tribunals to avoid making the Centre an exclusive forum available to persons for whom it is not designed, and to prevent submitting purely national claims before the Centre. Unless the investor is not a national of the host

State or a non-contracting State, there is no justification why tribunals should stick by traditional concepts of incorporation and real seat, and to disregard economic reality.

Shareholders' rights to claim separately from the legal entity in which they own shares, if the parties have agreed on shares as an investment, are incontestable. The Centre's recent case-law shows that the tribunal does not examine whether shareholders are asserting their own rights or those of the company affected by the host State. In their decisions on jurisdiction tribunals should draw a strict line between the argument of the host State that investors may claim for measures affecting their *shares qua shares*, and the argument of the investor that every measure taken by the host State against a locally incorporated entity causes a loss in value of its investment. In cases where a wrong has been done to the company, not directly against shares as such, tribunals should particularly state reasons for accepting jurisdiction.

A too broad interpretation of investment, i.e. that a wrong done to company is a violation of shareholders' rights under the BIT, has expanded the Centre's jurisdiction far beyond the will of the Convention's drafters, who explicitly excluded the possibility to grant shareholders the right to bring claims before the Centre on behalf of entities in which they own shares.

Acceptance of indirect claims creates a risk of multiple claims and may result in double recovery for the same wrong. It is likely that global and local economic recessions will increase the number of indirect claims before the Centre; thus further research is required in the field of indirect claims brought by shareholders for wrong done to the company.

A new, less formalistic approach must be taken by tribunals in determining nationality in order that the result does not abuse the Convention. To balance both the interests of investors and host States, a more cautious approach is needed when accepting jurisdiction for claims brought by shareholders.