

*Special Issue: International Investment Law*

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PROTECTED INVESTMENTS AND PROTECTED INVESTORS:  
THE OUTER LIMITS OF ICSID'S REACH

OMAR E. GARCÍA-BOLÍVAR\*

*There are International Center for Settlement of Investment Disputes (ICSID) protected investments and ICSID protected investors. What this means is that not all disputes on investments can be heard by ICSID. The same can be said about investors, i.e., not all investors are entitled to be heard by ICSID tribunals. Such is the case regardless of what the State parties have agreed in the relevant international investment agreements (LAAs). This note seeks to chart the outer limits of the ICSID, the purpose being to set up the limits beyond which the investment disputes could be heard by an ICSID tribunal and the limits beyond which a person cannot submit disputes to ICSID. References made to previous awards and to relevant ICSID documents suggest that there are criteria to define the jurisdiction of an ICSID tribunal *ratione materiae* and criteria to define the jurisdiction of an ICSID tribunal *ratione personae*. Therefore, tribunals should carefully consider such criteria in order to avoid abuse to the system of international law of foreign investment.*

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## I. INTRODUCTION

The International Center for Settlement of Investment Disputes (ICSID) is very unique among dispute resolution centers. For starters, ICSID is more than an arbitration center; it is a dispute resolution center where investment can be settled through mediation for example and not solely by arbitration.

More importantly, ICSID, as opposed to other dispute resolution centers, has been created by a multilateral instrument of public international law – the ICSID or the Washington Convention. Members to ICSID are States subject to their own laws and accountable to their citizens. And as sovereign States in the international arena they are also subject to public international law.

As ICSID has distinctive traits, not all types of disputes can be protected under the terms of the Convention. In other words, for a dispute to be able to reach an ICSID arbitral tribunal and be decided, the dispute needs to meet certain requisites.

These requirements, differing in nature, may be classified into *ratione materiae* and *ratione personae*. They have been dubbed as the *outer limits* of the ICSID;<sup>1</sup> that is, the point beyond which a tribunal is disabled to hear a claim on a dispute submitted to ICSID.

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<sup>1</sup> CENTRO INTERNACIONAL DE ARREGLO DE DIFERENCIAS RELATIVAS A INVERSIONES 2-1 HISTORY OF THE ICSID CONVENTION, 566 (International Centre for Settlement of Investment Disputes, 2001).

## II. REQUISITES FOR ICSID TO HAVE JURISDICTION

Article 25 of the ICSID Convention sets the requirements for the Centre to have jurisdiction over a dispute, enumerated as follows:

1. The dispute needs to be of legal nature. Disputes of non-legal nature although related to an investment are not covered by the Convention nor are within the boundaries of ICSID jurisdiction.
2. The dispute needs to arise directly out of an investment. Disputes arising out of matters that do not tantamount to an investment is excluded, e.g., disputes arising out of immigration.
3. The non-State party to the dispute needs to be a national of another Contracting State. However, since 1978 ICSID has had a set of additional facility rules that allow disputes in which either the State party to the dispute or the State whose national is party to the dispute is not a Contracting State or disputes that did arise directly out of an investment to be submitted to arbitration.
4. Consent to submit the dispute to ICSID needs to be granted by both parties in writing.

Setting aside the consent, an oversimplification of the jurisdiction of an ICSID arbitral tribunal can be as follows:

Type of dispute: Legal;

Nature: Arising directly out of an investment;

Parties: A contracting State and an investor of another contracting State.

## III. LIMITS ON *RATIONAE MATERIAE*

The first two categories can be subsumed into *ratione materiae*, meaning that for ICSID arbitral tribunals to hear a claim it needs to be: a) of legal nature, b) originating directly from an investment; c) concerning foreign investments.

### A. *Of Legal Nature*

Technical disputes, even if they are related to the investment — dimensions of a land plot or differences over a product's technical specifications, among others — are not covered by the Convention or within the limits of ICSID's jurisdiction. Likewise, commercial or political disputes are not within its jurisdiction.

Under certain circumstances, the Secretary-General of ICSID may reject a claim if, according to the arbitration request, it is not directly related to an

investment. An example of this occurred when ICSID rejected an arbitration request submitted in connection with a dispute that derived from a supply contract for the sale of goods.<sup>2</sup> Article 36(3) of the Convention bestows authority on the Secretary-General of ICSID to reject claims that are evidently outside the Centre's jurisdiction. For instance, a claim submitted to ICSID that does not clearly indicate the legal support of the dispute can be rejected immediately or its acceptance can be suspended until the claimant submits explanations whenever the Secretary-General asks for them.

Thus, not all investment disputes between an investor from an ICSID contracting State and a contracting host State can be subject to arbitration at the Center. The disputes need to be of legal nature, which implies that it needs to be about rights and duties of the investors or the States.

### B. *Originating From an Investment*

Disputes that do not arise directly out of an investment are beyond the realm of ICSID. The Convention does not have a definition of disputes arising directly out of an investment.

In the *CSOB* case,<sup>3</sup> Slovakia argued that the dispute had not arisen out of an investment but from a second-tier agreement that guaranteed obligations of another legal entity. In its first Decision on the objections, the Arbitration Tribunal quoted the *Fedax* case:

It is apparent that the term 'directly' relates in this Article to the 'dispute' and not to the 'investment'. It follows that jurisdiction can exist even in respect of investments that are not direct, so long as the dispute arises directly from such transaction....<sup>4</sup>

Furthermore, it stated that investments are usually operations composed of various inter-related transactions. The transactions by themselves might not qualify as an investment. However, when a dispute is brought before ICSID, the tribunal needs to look at the overall operation and not solely at the particular transaction. If the whole operation can be qualified as an investment, even if it is

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<sup>2</sup> Asian Express v. Greater Colombo Economic Commission, (1985) ICSID Annual Report 6; See I.F.I. Shihata & A. Parra, *The Experience of the International Centre for Settlement of Investment Disputes*, 14 ICSID REV.—FOREIGN INVESTMENT L. J. 299, 308 & n.27 (1999).

<sup>3</sup> Ceskoslovenska Obchodni Banka, A.S. (CSOB) v. Slovakia, ICSID Case No. ARB/97/4 (May 24, 1999).

<sup>4</sup> Fedax N.V. v. Venezuela, I Decision on Objections to Jurisdiction (July 11, 1997), 37 I.L.M. 1378 (1998), ¶ 24.

not a direct investment, and the dispute arises directly out of that operation through the particular transaction, then ICSID will have jurisdiction.

In the second Decision on jurisdiction in this case,<sup>5</sup> the Tribunal pointed out that, although it had jurisdiction over a dispute that arose directly out of an investment through a specific transaction, the jurisdiction extended only to the dispute as per the terms of the consent of the parties. Therefore, the Tribunal did not acquire jurisdiction with regard to each agreement concluded to implement the wider investment operation.

There are occasions in which the parties to an investment dispute can be parties to another dispute. However, if one of the disputes does not arise directly out of the investment, ICSID does not have jurisdiction. In *Amco v. Indonesia*<sup>6</sup> the State submitted a counter claim arguing that the investor had committed a tax fraud. The Tribunal rejected the counter claim, stating that the obligation not to commit tax fraud was a general obligation in Indonesian law which had not been specified in the investment agreement between the home State and the host State. Therefore, as concluded the Tribunal, the dispute did not arise directly out of the investment.

Thus, there needs to be a direct causation link between the investment and the dispute. To make States liable for disputes that arise only indirectly out of an investment is a non-desired effect of the creators of the ICSID Convention. Hence, disputes arising indirectly out of the investment will not be protected under ICSID.

A dispute may thus arise directly out of a business but if the business is not an investment, ICSID shall not have jurisdiction.

### C. Concerning Foreign Investment

International businesses can take different and complex forms. Some can look as an investment but have another nature in reality. From the outset it seems apparent that in some cases tribunals can define an investment by what it is not. For example, investment and trade are two different ways of doing business. However, investment and trade can be inter-related, as occurs when the investment has been made in order to trade, i.e. to import or to export.

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<sup>5</sup> *Ceskoslovenska Obchodni Banka, A.S. (Csob) v. Slovakia*, ICSID Case No. ARB/97/4 (Dec.1, 2000).

<sup>6</sup> *Amco Asia et al. v. Indonesia*, Resubmitted Case, Decision on Jurisdiction, (May 10, 1988), 1 ICSID Reports 543, 565.

In cases in which the dispute arises out of an investment related to trade, ICSID would have jurisdiction. In the *Pope & Talbot, Inc. v. Canada* case,<sup>7</sup> the Tribunal dealt with this issue. Canada admitted that an investment had taken place but argued that the measure against which the investor was claiming was directed toward a commercial operation, not toward an investment. The Tribunal held that its jurisdiction emerged from the dispute which was *prima facie* an investment dispute and had been submitted as investment dispute. It also pointed out that there was no provision in the North American Free Trade Agreement (NAFTA) according to which investments and trade in goods should be treated separately from one another. It also said, responding to one of Canada's arguments, that trade measures could be applied to a particular company because a measure is fundamentally related to trade of goods does not necessarily mean that it is not related to the investment or the investor.

In *S. D. Myers Inc. v. Canada*,<sup>8</sup> faced with similar circumstances the Tribunal sustained that a measure about goods could affect those who are involved in the trade in goods and those who have made investments related to those goods.

Be that as it may, the ICSID Convention does not define investment willfully and has left it to the States to deal with the definition of what is an investment entitled to international protection in separate legal instruments. However, although the States have certain flexibility to define what is a foreign investment, for an investment to be considered ICSID protected investment certain requirements still need to be met.

In *Joy Mining v. Egypt*, the Tribunal noted: “[t]he fact that the Convention has not defined the term investment does not mean, however, that anything consented to by the parties might qualify as an investment under the Convention.”<sup>9</sup>

The parties to a dispute cannot by contract or treaty define as investment, for the purpose of ICSID jurisdiction, something which does not satisfy the objective requirements of Article 25 of the Convention. Otherwise Article 25 and its reliance on the concept of investment, even if not specifically defined, would be turned into a meaningless provision.<sup>10</sup>

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<sup>7</sup> *Pope & Talbot, Inc. v. Canada*, Award on Motion to Dismiss Claim, UNCITRAL (NAFTA) (Jan. 26, 2000).

<sup>8</sup> *S.D. Myers, Inc v. Canada*, Partial Award, 40 I.L.M. 1408, (Nov.12, 2000).

<sup>9</sup> *Joy Mining Machinery Limited v. Arab Republic of Egypt*, Award on Jurisdiction ICSID Case No. ARB/03/11, (Aug. 6, 2004), ¶ 49.

<sup>10</sup> *Id.* ¶ 50.

As was observed by the annulment Committee in *Patrick Mitchell v. DRC*: “The parties to an agreement and the States which conclude an investment treaty cannot open the jurisdiction of the Centre to any operation they might arbitrarily qualify as an investment.” It is thus repeated that, before ICSID arbitral tribunals, the Washington Convention has supremacy over an agreement between the parties or a BIT.<sup>11</sup>

Professor Schreuer writes:

The fact that most of the proposed definitions for the objective criteria for jurisdiction were not adopted was motivated less by the feeling that they were redundant than by an inability to agree on them. It would be inaccurate to assume that the general phrasing of these objective criteria in Art. 25 gives the parties complete freedom to determine, by the terms of their consent, which disputes they wish to submit to the Centre. This fact is borne out by the Report of the Executive Directors:

“While consent of the parties is an essential prerequisite for the jurisdiction of the Centre, consent alone will not suffice to bring a dispute within its jurisdiction. In keeping with the purpose of the Convention, the jurisdiction of the Centre is further limited by reference to the nature of the dispute and the parties thereto.”<sup>12</sup>

Consequently, it is necessary to take a closer look at the meaning of the objective jurisdictional requirements set out in Art. 25. The interpretation by the parties of these objective requirements is given great weight. Nevertheless, there are outer limits to the Centre’s jurisdiction that are not subject to the parties’ disposition.<sup>13</sup>

Thus, for ICSID to have jurisdiction it cannot be any type of foreign investment. The States, of course, are free to consent submission of disputes on investments that do not fall within ICSID to other dispute resolution centers.

ICSID Tribunals have been in need of criteria to determine what an investment is and what is not. Their reliance on academic writings has typically identified the following as constituents of investment:

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<sup>11</sup> *Patrick Mitchell v. Democratic Republic of the Congo*, Decision on the Application for Annulment of the Award ICSID Case No. ARB/99/7, (Nov. 1, 2006), ¶ 31.

<sup>12</sup> Executive Directors, International Bank for Reconstruction and Development, *Report on the Convention on the Settlement Of Investment Disputes Between States And Nationals Of Other States*, ¶ 25 (hereinafter IBRD Directors’ Report on ICSID Convention).

<sup>13</sup> CHRISTOPH SCHREUER, *THE ICSID CONVENTION: A COMMENTARY* 90-91 (Cambridge Univ. Press 2001) (hereinafter SCHREUER).

1. The project must have a certain duration;
2. There must be a certain regularity in the earnings and the return;
3. There is a typical element of risk on both sides;
4. There is a substantial commitment to develop certain activities; and
5. The operation must be significant for the development of the host State, as stated in the Convention's preamble.<sup>14</sup>

In *Salini Costruttori SpA and Italstrade SpA (Salini) v. Kingdom of Morocco (Morocco)*,<sup>15</sup> two Italian companies claimed compensation for damages from the Kingdom of Morocco under the Treaty between the Government of the Kingdom of Morocco and the Government of the Republic of Italy for the reciprocal promotion and protection of investments due to a dispute that arose out of the construction contract related to a section of a highway joining Rabat to Fés. Morocco objected the tribunal jurisdiction based on different grounds, one of which referred to the argument that construction contracts did not qualify as investments under the ICSID Convention. On considering that objection the Tribunal pointed out that although the ICSID Convention does not define the term investment there were criteria generally identified to determine what is an ICSID protected investment: *existence of contribution, certain duration and risk participation*. It also added that the operation should contribute to the development of the host State, as provided by the Convention's preamble.<sup>16</sup> The Tribunal found that the construction contract fulfilled the criteria. Even in the risk aspect, the Tribunal indicated that a construction project that lasts several years, for which total costs cannot be established with certainty in advance, created a risk for the contractor. Thus, a construction operation could be qualified as an investment, and the disputes that arose directly out of it were susceptible to be heard by ICSID. In connection with the economic development requirement the Tribunal mentioned that in most countries construction of infrastructure falls under the tasks to be carried out by the State or by other public authorities. It then mentioned that the highway in question served the public interest and that the claimant companies were also able to provide the host State with know-how in relation with the work.<sup>17</sup>

In *Salini* the Tribunal also mentioned that all the elements to be taken into account for defining when there is an investment in the context of the

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<sup>14</sup> *Id.* at art. 25, ¶ 86.

<sup>15</sup> *Salini Costruttori SpA and Italstrade SpA v. Kingdom of Morocco*, Decision on Jurisdiction 42 I.L.M. 609 (2003), (July 23, 2001) (hereinafter *Salini Costruttori SpA and Italstrade SpA v. Morocco*).

<sup>16</sup> *Id.* ¶ 52.

<sup>17</sup> *Id.* ¶ 57.

Washington Convention may be interdependent. Thus, had the investment failed the test of any of the elements, for example, the one on economic development, the Tribunal would have had to reject the claim and declare that it did not have jurisdiction.

The criteria set forth by *Salini* has given origin to what is now known as the “*Salini* test”, which some tribunals have accepted with subtle changes,<sup>18</sup> while others have disregarded partially; particularly in connection with the criterion on economic development.

*Salini* defined at least two of the criteria needed for an investment to contribute to the economic development of the host State: a) beneficial to public interest and b) know-how transfer. Specifically the Tribunal said: “[i]t cannot be seriously contested that the highway shall serve the public interest. Finally, the Italian companies were also able to provide the host State of the investment with know-how....”<sup>19</sup> Thus, the Tribunal implied that for an investment to contribute to economic development, at least it needed to serve the public interest and provide the host country with know-how. The Tribunal could have gone further and set up the criteria to measure the contribution to economic development of an investment. But the facts of the case in review seemed to have been strong enough to discard an elaborate analysis of all the relevant factors.

For the Tribunal to reach the conclusion that economic development was one of the elements to take into account in order to determine the existence of an investment according to the Washington Convention, it looked at the purpose of that treaty as mentioned in its preamble where references to the economic development impact of the investment are predominant. For example, textual reference to economic development in its preamble where it states: “[c]onsidering the need for international cooperation for economic development, and the role of private international investment therein.”<sup>20</sup>

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<sup>18</sup> See *Joy Mining Machinery Limited v. The Arab Republic of Egypt*, Decision on Jurisdiction, ICSID Case No. ARB/03/11 (July 23 2001), ¶ 53; *Jan de Nul N.V. v. Arab Republic of Egypt*, Decision on Jurisdiction, ICSID Case No. ARB/04/13 (June 16, 2006), ¶ 91; *Helnan International Hotels A/S v. The Arab Republic of Egypt*, Decision on Objection to Jurisdiction, ICSID Case No. ARB/05/19 (Oct. 17, 2006), ¶ 77; *Malaysian Historical Salvors SDN, BHD v. The Government of Malaysia*, Award on Jurisdiction, ICSID Case No. ARB/05/10 (May 17, 2007), ¶¶ 73-74.

<sup>19</sup> See *Salini Costruttori SpA and Italstrade SpA v. Morocco*, *supra* note 15, ¶ 57.

<sup>20</sup> Convention on the Settlement of Investment Disputes between States and Nationals of Other States, Mar. 18, 1965, 575 U.N.T.S. 159 (hereinafter ICSID Convention). The full text of the ICSID Convention, Regulations and Rules are available on the World Bank website: <http://www.worldbank.org/icsid/basicdoc/basicdoc.htm>.

Also, although the report from the executive directors states that the primary purpose of the Convention is to stimulate international investment flows, the report further underlines the body's desire to address the interests of both investors and States:

While the broad objective of the Convention is to encourage a larger flow of private international investment, the provisions of the Convention maintain a careful balance between the interests of investors and those of host States.<sup>21</sup>

Further the fifth preambular paragraph of the ICSID Convention states: “[d]esiring to establish such facilities under the auspices of the International Bank for Reconstruction and Development.”<sup>22</sup>

Consequently, it may be presumed that ICSID's purpose cannot be divorced from those of the IBRD, specifically stated to be, among others, facilitating and encouraging of international investment for: a) productive purposes; b) for the development of the productive resources of countries to increase productivity, standards of living and conditions of labor.<sup>23</sup> Hence, investments not devoted to productive purposes, such as those undertaken for speculative purposes and those that do not develop the productive resources of the host State without positive impact on the productivity or increase the standards of living or labor conditions, could be considered to be beyond the outer limits of ICSID.

In addition, it is publicly known that ICSID is part of the World Bank Group along with IBRD and other multilateral institutions. As portrayed by the World Bank Group in its website, the ICSID complements the overall mission of the group on helping “[p]eople help themselves and their environment by providing resources, sharing knowledge, building capacity and forging partnerships in the public and private sectors”.<sup>24</sup>

Further, the level of cooperation between ICSID and World Bank Group exceeds that of just sharing premises (which is stated in Art.2 of the ICSID

<sup>21</sup> IBRD Directors' Report on ICSID Convention, *supra* note 12, ¶ 13.

<sup>22</sup> Preamble, ICSID Convention, *supra* note 20.

<sup>23</sup> International Bank for Reconstruction and Development (IBRD), Articles of Agreement (As amended February 16, 1989), art. I, *available at* : <http://web.worldbank.org/WBSITE/EXTERNAL/EXTABOUTUS/0,,contentMDK:20049563~pagePK:43912~menuPK:58863~piPK:36602,00.html#I1> (last visited Feb. 1, 2010).

<sup>24</sup> The World Bank – About Us, *available at*: <http://web.worldbank.org/WBSITE/EXTERNAL/EXTABOUTUS/0,,pagePK:50004110~piPK:36602~theSitePK:29708,00.html> (last visited Feb. 1, 2010).

Convention). There exists a financial linkage as any excess in the expenditure which the ICSID cannot meet is to be borne by the Bank,<sup>25</sup> while operational linkage is evident as the President of the Bank is also the Chairman of the Administrative Council of ICSID,<sup>26</sup> having authority, *inter alia*, to appoint arbitrators in given circumstances.<sup>27</sup>

Thus, ICSID is not another arbitration center. It is a very special arbitration center; one with a purpose that exceeds the mere resolution of disputes between investors and States. It has a purpose set up by the parties to the Convention, but it also has a mission that needs to be consistent with the multilateral entities to which it is associated. And that purpose cannot be detached from economic development.

In the words of the dissenting opinion in the annulment decision of MHS:

An ICSID investment might indeed be made in favour of private entities but not for their own enrichment exclusively: only on the basis that, though made in favour of private entities, such an investment would – not might – promote the economic development of the host State.<sup>28</sup>

The importance of economic development for an ICSID protected investment cannot be underestimated for:

It is not merely that 'international investment plays a role in economic development' of the host State: international investment must play a role in the economic development of the host State if the investment is to rank as an ICSID investment and be entitled to the protection of the ICSID settlement procedures; that requirement is a condition of an ICSID investment.<sup>29</sup>

In *Malaysian Historical Salvors*, subsequently annulled by the ad-hoc committee, the sole arbitrator found that a positive and significant contribution to the economic development of the host country was a requirement for the investment to be ICSID protected. Significantly, the Tribunal pointed out to enhancing the Gross Domestic Product of an economy as the factor that determined the

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<sup>25</sup> ICSID Convention, *supra* note 20, art. 17.

<sup>26</sup> ICSID Convention, *supra* note 20, art. 5.

<sup>27</sup> ICSID Convention, *supra* note 20, art. 38.

<sup>28</sup> MHS v. Malaysia, Decision of the application for annulment: Dissenting Opinion by Judge Mohamed Shahabuddeen, ICSID Case No. ARB/05/10 (Apr. 16, 2009), ¶ 17.

<sup>29</sup> Malaysian Historical Salvors SDN BHD v. THE Government of Malaysia, ICSID Case No. ARB/05/10, Decision on the Application for Annulment Dissenting Opinion of Judge Mohamed Shahabuddeen: (Apr.16, 2009), ¶ 29.

criterion of economic development. The Tribunal then qualified that factor and interpreted that the enhancement of Gross Domestic Product could not be by a small amount for the investment to be ICSID protected. The Tribunal said:

The weight of the authorities cited above swings in favour of requiring a significant contribution to be made to the host State's economy. Were there not the requirement of significance, any contract which enhances the Gross Domestic Product of an economy by any amount, however small, would qualify as an 'investment'.<sup>30</sup>

In *CSOB*, it was concluded that the investment had to have a positive impact on the host State's development. The tribunal considered that the phrase found in the Preamble to the ICSID Convention "permits an inference that an international transaction which contributes to cooperation designed to promote the economic development of a Contracting State may be deemed to be an investment as that term is understood in the Convention".<sup>31</sup>

Somehow, this had been previously recognized by the Tribunal in *Amco v. Indonesia* when it concluded: "[t]he Convention is aimed to protect, to the same extent and with the same vigour, the investor and the host State, not forgetting that to protect investments is to protect the general interest of development and of developing countries."<sup>32</sup>

Thus, combining the criteria for determining a contribution to economic development used by *Salini*, *MHS* and *CSOB*, points out to the need that the investment: a) *be made for public interest*; b) *to transfer know-how*; c) *enhance the Gross Domestic Product of the host country*; d) *make a positive impact on the host State's development*.

Other tribunals have taken a different approach regarding the criterion of contribution to economic development. Noticeably, most of these cases have been similar in one thing: *they have rejected the criterion of economic development due to difficulty or impossibility to ascertain it*.

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<sup>30</sup> Malaysian Historical Salvors SDN, BHD v. The Government of Malaysia, Award on Jurisdiction, ICSID Case No. ARB/05/10, (May 17, 2007), ¶ 123.

<sup>31</sup> Československa obchodni banka, a.s. v Slovak Republic, Decision of the Tribunal on Objections to Jurisdiction, ICSID Case No. ARB/97/4, (May 24, 1999), ¶ 64 (hereinafter *Československa obchodni banka*).

<sup>32</sup> Amco Asia Corporation and others v. Republic of Indonesia, Decision on Jurisdiction, ICSID Case No. ARB/81/1 (Sept. 25, 1983). See also *id.*, Award (Nov. 20, 1984).

For example in *Pey Casado v. Chile*, the Tribunal stated that the requirement of contribution to economic development was referred in the preamble but as a consequence not as a condition. Given the difficulty to establish a contribution to economic development, the Tribunal considered that that requirement was included within the others:

The requirement of a contribution to the development of the host State, which is difficult to establish, would pertain more to the merits of the dispute than to the Centre's jurisdiction. An investment may prove to be useful or not to a host State without losing his quality of investment. It is correct that the Preamble of the ICSID Convention evokes a contribution to the economic development of the host State. This reference is however presented as a consequence, not as a condition of the investment: in protecting the investments, the Convention promotes the development of the host state. This does not mean that the development of the host State is a constitutive element of the notion of investment. This is the reason why, as noted by some arbitral tribunals, this fourth condition is in fact encompassed by the three others.<sup>33</sup>

Further, the ad-hoc Committee of *Mitchell* stated:

The existence of a contribution to the economic development of the host State as an essential— although not sufficient — characteristic or unquestionable criterion of the investment, does not mean that this contribution must always be sizable or successful; and, of course, ICSID tribunals do not have to evaluate the real contribution of the operation in question. It suffices for the operation to contribute in one way or another to the economic development of the host State, and this concept of economic development is, in any event, extremely broad and also variable depending on the case.<sup>34</sup>

The annulment Committee also mentioned that the concept of investment was somewhat broadened in some cases, but it added that this would do nothing to alter the fundamental nature of that characteristic.<sup>35</sup>

In *L.E.S.I. S.p.A. et ASTALDI S.p.A. v. Algeria* the Tribunals considered that it did not seem necessary that the investment contributed to the economic

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<sup>33</sup> Víctor Pey Casado and President Allende Foundation v. Republic of Chile, ICSID Case No. ARB/98/2, Decision (Sept.25, 2001), ¶ 232.

<sup>34</sup> Patrick Mitchell v. The Democratic Republic of Congo, Decision on the Application for the Annulment of the Award, ICSID Case No. ARB/99/7, Nov. 1, 2006), ¶ 33.

<sup>35</sup> *Id.* ¶ 30.

development of the country, a condition that it considered difficult to establish and that was implicitly covered by the previous three elements.<sup>36</sup>

However, in *Phoenix*, though the Tribunal did not deny that contribution to economic development was a criterion to define an ICSID protected investment; it rejected the criterion's applicability for other reasons. It stated: "[i]t is the Tribunal's view that the contribution of an international investment to the development of the host State is impossible to ascertain – the more so as there are highly diverging views on what constitutes development."<sup>37</sup>

But subsequently the Tribunal did acknowledge that the object of the Washington Convention was to encourage and protect international investment made for the purpose of contributing to the economy of the host state.<sup>38</sup>

Thus, the Tribunal did agree that the purpose of the ICSID Convention was to encourage foreign investment for economic development. Being so, it would have followed that for investments to be protected under the ICSID system they would have needed to contribute to the economic development of the host country. However, the Tribunal refused to enter that analysis.

In sum, there is a general acceptance that contribution to economic development of the host State is an element that defines an ICSID protected investment. The disagreement is on how to establish that requirement. Many tribunals have decided to include the requirement of economic development within the others or disregard the requirement at all due to the difficulty or impossibility of determine when an investment has contributed to the economic development of the host country. However, a hermeneutic analysis of the ICSID law shows that there are ways to ascertain the contribution to economic development of a foreign investment. If an investment is contrary to public interest, has not left any knowledge to the host country, has not enhanced the economy or its productivity or has not increased the standards of living of the host country or the labor conditions, it has probably made no contribution to the economic development of that country. Given specific references in the relevant IIAs, such investment should be denied protection either at a preliminary jurisdictional stage or at a final merits stage.

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<sup>36</sup> L.E.S.I. S.p.A. et ASTALDI S.p.A. v. Algeria, ICSID Case No. ARB/05/3 (July 12, 2006) (French), ¶ 73(iv).

<sup>37</sup> *Phoenix Action, Ltd v. The Czech Republic*, ICSID Case No. ARB/06/5, (Apr.15, 2009), ¶ 85.

<sup>38</sup> *Id.* ¶ 87.

So far most debates on economic development have been centered to a large extent around the ICSID Convention. However, since many other IIAs also contain references to economic development as the *leit motif* of States to enter into them, it is foreseeable that tribunals could be exposed to circumstances where interpretation of the intention of the States would have to be considered. In those cases, it would inevitably turn into an analysis of the economic development criterion of the investment. Of course, in the absence of any reference to economic development in the IIAs the task of the tribunals will be harder.

In cases to be tried in fora different than the ICSID, for example under the UNCITRAL, the so-called economic development defense to object jurisdiction will probably not be possible. Only if the relevant IIA has made references to economic development as the reason for the parties to grant international protection to foreign investments could that argument be submitted. But in that hypothetical circumstance, the tribunals would most likely consider the defense in the merits. For now, it seems that cases under ICSID will dominate the discussion on the analysis of economic development as an outer limit of a protected investment.

#### IV. LIMITS ON *RATIONAE PERSONAE*

The issue of nationality of the investor has been a common one in the context of international investment disputes. For ICSID to have jurisdiction the legal investment dispute needs to be between a Contracting State and a national of another Contracting State. If the dispute is between a national of the Contracting State involved in the dispute and the state of nationality itself, ICSID will not have jurisdiction. That is why the criteria to determine when a person or a juridical person is a national of a State are crucial.

##### *A. The Non State Party Must be a Contracting Party National From Other Than the Host State*

Both the host State and the home State must be signatories of the Convention. Additionally, the investor must be from a State other than the one against which the investment dispute has arisen.

However, since 1998 ICSID has incorporated the Rules of the Additional Facility, which allow disputes that do not comply with the former requisite to be submitted to arbitration before the Centre. Therefore, disputes in which the State party to the dispute or the State whose national is party to it—but not both—is not a party to the Convention can be arbitrated by ICSID according to these

rules. The Convention provides hints as to who is a national of another Contracting State:<sup>39</sup>

1. Any natural person who had the nationality of a Contracting State other than the State party to the dispute at the time of the consent as well as on the date on which the request was registered;
2. Any juridical person which had the nationality of a Contracting State other than the State party to the dispute; and
3. Any juridical person which had the nationality of the Contracting State party to the dispute at the time of the consent and which, because of foreign control, the parties have agreed should be treated as a national of another Contracting State.

*B. Disqualifying State Entities from ICSID Arbitration*

ICSID handles disputes between investors and States, neither disputes between investors nor disputes between States. But in many cases, the parties to the dispute can be complex and the determination of the nationality is not a task that can be performed without difficulties. For that reason the tribunals have faced the need to determine when and if the dispute is between parties to which ICSID can extend protection. The principles of this task were clearly defined in *BANRO*, where the Tribunal stated:

[I]n general, ICSID tribunals do not accept the view that their competence is limited by formalities, and rather they rule on their competence based on a review of the circumstances surrounding the case, and, in particular, the actual relationships among the companies involved. This jurisprudence reveals the willingness of ICSID tribunals to refrain from making decisions on their competence based on formal appearances and to base their decision on a realistic assessment of the situation before them....<sup>40</sup>

In the *CSOB* case,<sup>41</sup> the Arbitral Tribunal analyzed the issue of a dispute submitted by a State-owned company. The Slovak Republic alleged that *CSOB* was acting as an agent of the Czech Republic and the claim had to be dismissed because the dispute was one between States over which ICSID could not have jurisdiction.

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<sup>39</sup> ICSID Convention, *supra* note 20, art. 25(2).

<sup>40</sup> *Banro American Resources, Inc. and Société Aurifère du Kivu et du Maniema S.A.R.L. v. Democratic Republic of Congo*, ICSID Case No. ARB/98/7 (Sept. 1, 2000).

<sup>41</sup> *Ceskoslovenska obchodni banka*, *supra* note 31.

The Tribunal, according to a Convention commentator,<sup>42</sup> determined that a mixed-economy company or a government-owned corporation is not disqualified per se as a national of another Contracting State unless it is acting as an agent of its Government or performing governmental functions. It also asserted that a State-owned corporation is not performing State functions when it takes advantage of a free-market economy or privatization policies and restructures itself to be competitive nor when it takes measures to achieve those objectives. That was the case with *CSOB*. Therefore, it was not considered an agent of the Czech Republic and could not be disqualified to initiate proceedings before ICSID.

In the *Maffezini v. Spain*,<sup>43</sup> the Tribunal analyzed the issue from a different point of view. In this case, Spain alleged that ICSID lacked jurisdiction because the dispute was not between an individual (*Maffezini*) and a State (Spain) but between an individual and a corporation (SODIGA), *i.e.* a legal entity. The Tribunal held that to determine if an entity was a State organ and its doings attributable to the latter two tests were required: structural and functional. If, on analyzing the structure of an entity, it seems that it is not a State organ because the State has used a corporate veil, the analysis needs to be turned to the function of the entity. If the entity is in charge of State functions, then it will be considered an organ of the State. SODIGA met both the structural test of State creation and capital ownership and the functional test of performing activities of a public nature. Thus, the Tribunal rejected the objection to jurisdiction based on this argument because the claimant had shown *prima facie* that the dispute was between an individual and an organ of the State.

### C. *The Requirement of Foreign Control*

Similarly, disputes to be heard by ICSID tribunals cannot be between a contracting State and one of its nationals, unless the national is a juridical person subject to foreign control.

Article 25(2)(b) of the ICSID Convention states that any juridical person with the nationality of the Contracting State party to the dispute can have the treatment of a national of another Contracting State for purposes of the Convention if that juridical person is under foreign control and the parties have agreed to such treatment. But that exception aside, ICSID tribunals cannot be

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<sup>42</sup> The Tribunal quoted A. Broches, *The Convention on the Settlement of Investment Disputes between States and Nationals of Other States*, 135 HAGUE RECUEIL DES COURS 331, 354-355 (1972).

<sup>43</sup> *Emilio Agustín Maffezini v. Spain*, ICSID Case No. ARB/97/7, (Jan. 25, 2000).

used to settle disputes between a State and its subjects. In the words of Prof. Schreuer:

The basic idea of the Convention, as expressed in its title, is to provide for dispute settlement between States and foreign investors... Disputes between a State and its own nationals are settled by that State's domestic courts... The Convention is designed to facilitate the settlement of investment disputes between States and nationals of other States. It is not meant for disputes between States and their own nationals. The latter type of dispute is to be settled by domestic procedures, notably before domestic courts.<sup>44</sup>

But in many cases, there are grey areas where the tribunals need to grasp the facts and determine the real nationality of an investor, mainly when Art.25(2)(b) of the ICSID Convention is involved. Because the ICSID Convention does not provide for definition of foreign control, some Tribunals have had to address that issue. The tribunals are therefore inclined to adopt a realistic attitude in looking for the actual foreign investor and not restrict operation of the ICSID by a narrow interpretation of the investor's identity.<sup>45</sup>

For example in *SOABI v. Senegal*,<sup>46</sup> the Tribunal went beyond direct control to determine the real nationality of an investor. SOABI was a Senegalese incorporated company, controlled by a Panamanian company which in turn was controlled by Belgian citizens. Panama was not a Contracting State of the Convention when the arbitration consent was given, but Belgium was. Senegal objected to jurisdiction, arguing that Panama was not part of the ICSID system. Thus, SOABI could be considered a local company under foreign control but the foreigners who controlled SOABI were not nationals of a Contracting State of the Convention and therefore could not use ICSID arbitration. The Tribunal found that the purpose of Article 25(2)(b) of the Convention was to facilitate foreign investments through locally incorporated companies so that they could qualify before ICSID. As a consequence of this interpretation, the Tribunal went beyond direct control and found that Belgian nationals in effect controlled *SOABI*.

#### *D. The Requirement of Real and Effective Nationality*

In other cases the claim to real and effective nationality has imposed on tribunals the burden of looking for facts beyond the external facade.

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<sup>44</sup> SCHREUER, *supra* note 13, at p. 158, ¶ 165, & p. 290, ¶ 496.

<sup>45</sup> *Id.* at p. 178.

<sup>46</sup> *Soabi v. Senegal*, Decision on Jurisdiction, 2 ICSID Reports 182-183 (Aug. 1, 1984).

In *Champion Trading Company, Ameritrade International, Inc., James T. Wahba, John b. Wahba, Timothy T. Wahba v. Arab Republic of Egypt (Champion)*,<sup>47</sup> the Claimants, all of whom were shareholders of an Egyptian cotton trading company, alleged that the government of Egypt violated the terms of the U.S.-Egypt BIT and filed a claim through ICSID arbitration. Egypt objected to ICSID jurisdiction based on the argument that some of the individual Claimants had Egyptian nationality. The Claimants alleged that their real and effective nationality was American.

The individual claimants alleged that the real and effective nationality was American, but there were two underlying American corporations that had also filed for arbitration, *Champion Trading Company, Ameritrade International, Inc.* By looking at the issue of real and effective nationality, the Tribunal analyzed the *Nottebohm* ICJ decision and the *A/18* decision from the IRAN-United States Claims Tribunal. The Tribunal quoted the *A/18* decision and noted that “real and effective nationality was indeed relevant unless an exception is clearly established”. The Tribunal found that such an exception existed in Art.25(2)(a) of the ICSID Convention which expressly provides that a national of another Contracting State does not include any person who, on either the date of the consent or on the date when the request was registered, had the nationality of a Contracting State party to the dispute. The Tribunal found that the individual Claimants had mentioned their Egyptian nationality in the documents establishing the investment vehicle without any reference to their U.S nationality. The Tribunal declared that it did not have jurisdiction in the dispute as presented by the individual Claimants. However, while the individual Claimants were forbidden from bringing a claim against Egypt due to their Egyptian nationality, the Claimants were also American nationals and shareholders of the corporate Claimants both of which were American companies. The Tribunal held that the corporate Claimants were considered foreign investors for purposes of the arbitration and rejected the Respondent’s objection to jurisdiction for the corporate Claimants.

#### *E. The Nationality of Investors*

In certain cases, it is possible that local investors may take advantage of the ICSID system by appearing to be foreigners.

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<sup>47</sup> *Champion Trading Company, Ameritrade International, Inc., James T. Wahba, John b. Wahba, Timothy T. Wahba v. Arab Republic of Egypt*, (Oct. 21, 2003), available at: <http://www.worldbank.org/icsid/cases/champion-decision.pdf> (last visited Feb. 12, 2010) (hereinafter *Champion Trading v. Egypt decision*).

In *Tokios Tokeles v. Ukraine*<sup>48</sup> (*Tokios*), a firm incorporated in Lithuania but with the majority of its shares owned by Ukrainian nationals, initiated arbitration against Ukraine, alleging the Ukrainian government breached the Ukraine-Lithuania BIT. Ukraine objected the Tribunal's jurisdiction, arguing, *inter alia*, that the Claimant was not a foreign investor. Hence the dispute was between a State and its own subjects and not a matter for ICSID arbitration.

The Ukraine-Lithuania BIT defined foreign investors as those entities incorporated in the other State party. Based on that the majority of the Tribunal stated that the parties to a BIT were free to determine the criteria used to determine nationality<sup>49</sup> and set the definition of investor and foreign control of a local entity for purposes of article 25(2)(b) of the ICSID Convention. It was not up to the Tribunal to question the criteria used therein.

The Tribunal stated that:

...Contracting Parties are free to define their consent to jurisdiction in terms that are broad or narrow; they may employ a control-test or reserve the right to deny treaty protection to claimants who otherwise would have recourse under the BIT. Once that consent is defined, however, tribunals should give effect to it, unless doing so would allow the Convention to be used for purposes for which it clearly was not intended.<sup>50</sup>

Thus the majority concluded that *Tokios* was a foreign investor under the terms of the BIT and rejected the Ukraine's objection to jurisdiction, stating:

In our view, however, neither the text of the definition of 'investment', nor the context in which the term is defined, nor the object and purpose of the Treaty allow such an origin-of-capital requirement to be implied. The requirement is plainly absent from the text...the origin-of-capital requirement is inconsistent with object and purpose of the Treaty, which ...is to provide broad protection to investors and their investment on the territory of the other party.<sup>51</sup>

The majority also stated that, "the ICSID Convention contains no inchoate requirement that the investment at issue in a dispute have an international character in which the origin of the capital is decisive."<sup>52</sup> Regarding the

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<sup>48</sup> *Tokios Tokeles v. Ukraine*, ICSID Case No. ARB/02/18, (Apr. 29, 2004) (hereinafter *Tokios Tokeles*).

<sup>49</sup> *Id.* ¶ 24.

<sup>50</sup> *Id.* ¶ 39.

<sup>51</sup> *Id.* ¶ 77.

<sup>52</sup> *Id.* ¶ 82.

Convention's purpose, the majority considered that the decision had not allowed, "the Convention to be used for purposes for which it clearly was not intended."<sup>53</sup>

The dissenting arbitrator said that disputes between a State and its nationals are outside the scope of ICSID:

It appears that the ICSID arbitration mechanism is meant for international investment disputes, that is to say, for disputes between States and foreign investors. It is because of their international character, and with a view to stimulating private international investment, that these disputes may be settled, if the parties so desire, by an international judicial body. The ICSID mechanism is not meant for investment disputes between States and their own nationals.<sup>54</sup>

Accordingly, it was opined that the silence of the Convention on the criterion of corporate nationality does not leave the matter to the discretion of the Parties. According to Article 31 of the Vienna Convention on the Law of Treaties, 1969 (VCLT), parts of which the International Court of Justice has repeatedly described as the expression of customary international law, a treaty must be interpreted by giving ordinary meaning to its text in light of its objective and purpose.<sup>55</sup>

On analyzing the purpose of the ICSID Convention from a different perspective the dissenting arbitrator stated that the purpose of the convention was to govern international investment implying a transborder flux of capital.<sup>56</sup>

Highlighting the importance of the origin of the capital in the circumstantial determination of an investment,<sup>57</sup> the dissenting arbitrator also objected to the right of Contracting Parties to extend the Convention's jurisdiction, explaining that:

....[I]t is within the limits determined by the basic ICSID Convention that the BITs may determine the jurisdiction and powers of the ICSID tribunal, and it is not for the Contracting Parties in their BITs to extend the jurisdiction of the ICSID tribunal beyond the limits determined by the basic ICSID Convention.<sup>58</sup>

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<sup>53</sup> *Id.* ¶ 39.

<sup>54</sup> *Id.* ¶ 5.

<sup>55</sup> *Id.*

<sup>56</sup> *Id.* ¶ 11.

<sup>57</sup> *Id.* ¶ 20.

<sup>58</sup> *Id.* ¶ 13.

*Champion*<sup>59</sup> and *Tokios*<sup>60</sup> are but two cases that seemingly dealt with similar issues. They deserve attention to stress the striking differences between them. First, in *Champion* the shareholders of the corporate claimants had Egyptian and American Nationality. A factor that was not present in *Tokios*. Second, the references made by the tribunal to *Nottebohm* and *A/18* decisions in terms of real and effective nationality would have been useful to dismiss the argument that the corporate claimant was an Egyptian investor, because the real and effective nationality of the individual shareholders was American. Third, the reference of Art.25(2)(a) of the Convention which excludes dual nationals from invoking the protection of the Convention against the host country to which they are also nationals, only applies to individuals, not to companies of the other Contracting State when individuals with dual nationality are shareholders. Fourth, the Tribunal in *Champion*, made a specific reference to Art.32 of VCLT, which states that supplementary means of interpretation including the preparatory work of the treaty and the circumstances of its conclusion, can be used for interpretation in cases of ambiguity or unreasonable results. That provision could have allowed the Tribunal to look at supplementary means of interpretation of the ICSID Convention to disregard the applicability of Article 25 (2)(a) if it led to an absurd or unreasonable result, such as the confirmation of ICSID jurisdiction to settle disputes between a State and a domestic investor. So, for example by looking at the ICSID Convention preamble or the report from the executive directors on the ICSID Convention it would have been clear that that the primary purpose of the Convention is to stimulate international investment flows. Therefore only legal disputes between foreign investors and host States arising out of foreign investments could have fallen upon the jurisdictional turf of the arbitral Tribunal.

Thus, it is likely that if faced with the same issue *Tokios* addressed, *i.e.*, a national investor disguised as a foreigner, a Tribunal may use the unreasonable results theory to explore the purpose of the ICSID Convention in depth to declare that it does not have jurisdiction over a dispute between a national and its State.

## V. CONCLUSION

The ICSID system was thought of for international investment disputes. Its theoretical rationale has been that on providing investors with a neutral and independent body where they could settle disputes with host States, investors would be better protected and that in turn would attract more investments to the countries that committed themselves to settle investment disputes through an international center. Furthermore, it was assumed that foreign investments would be a means for economic development of the attracting countries.

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<sup>59</sup> *Champion Trading v. Egypt decision, supra* note 47.

<sup>60</sup> *Tokios Tokeles, supra* note 48.

Thus, there are ICSID protected investments and ICSID protected investors. What that means is that not all disputes on investments can be heard by ICSID. The same can be said about investors, *i.e.*, not all investors are entitled to be heard by ICSID tribunals. Such is the case regardless of what the State parties have agreed in the relevant IIAs.

ICSID has been created by a multilateral agreement and its tribunals owe respect to that document and to the intention of the parties. Moreover, the nature of the parties to the ICSID Convention and the surrounding circumstances relevant for interpretation should be considered. In that vein the preamble and *travaux préparatoires* of the ICSID Convention should be analyzed, but also the *raison d'être* of States and the context upon which ICSID exists should be considered.

That would allow tribunals the opportunity to issue decisions that are more balanced and adjusted to the true intention of the States. Investors in turn will be endowed with more certainty and the possibility of devising the investments in a different way or of submitting the dispute to a different forum.

The ICSID system cannot allow abusive practices where prevalence of the forms of investment is imposed over economic reality. For example, on accepting that the exception provided by second part of Art.25(2)(b) of the Convention is meant to circumvent the formality of local incorporation of a foreign controlled wholly owned subsidiary, the rationale of the system should be taken into account when analyzing facts in which there is doubt about the foreign nature of the investors.

To allow disputes between national investors, although disguised under the form of foreign and their own States to be settled before ICSID arbitral tribunals not only jeopardizes the ICSID system and opens the door to judicial chaos, but also damages the reputation and development of international law of foreign investment.

ICSID tribunals have the right tools to deal with issues such abuse of legal personality. For instance, a cost-benefit analysis of the concept of corporation and legal personality could determine that the cost of protecting the legal personality of the subsidiary is higher than the benefits it provided to the society. Consequently, tribunals might disregard the legal personality of the claimant corporation controlled by nationals of the host State but with appearance of foreign investor. On doing that the subsidiary could be considered equal to the parent company, not so much for purposes of protecting the investor, as is the

case under Art.25(2)(b) of the ICSID Convention, but to avoid reaching conclusions based on abusive conducts and false facts.

Future ICSID arbitral tribunals confronting the issues of what investments and what investors are entitled to be protected would do a great service if they look at the rationale and purpose of the ICSID Convention and all concomitant circumstances to keep a reality seeking non-formalistic approach. That would clearly demarcate the outer limits of ICSID and define ICSID protected investments and ICSID protected investors.