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Eligible Juridical Person Investors in ICSID Arbitration

Hou Yutong[1,a,*]

[1]*Faculty of Law, The Chinese University of Hong Kong, Shatin, New Territories, Hong Kong, China*
a. yutonghou@outlook.com
**corresponding author*

Abstract: An investor's eligibility is a prerequisite for International Centre for Settlement of Investment Disputes (ICSID) tribunal to acquire jurisdiction over a case. There is no definite conclusion on whether an entity is an eligible investor, often leading to disagreement. In current international investment practice, arbitration tribunals usually consider the definition of investor in the bilateral investment treaties concluded by the parties to the dispute and use it as one of the bases for determining the investor's international status. Since the identification of juridical person investors is a controversial issue in practice, this essay will analyze the criteria for ICSID's decision in the Tokios Tokelės v. Ukraine as an example and examine the issue of "pierce the corporate veil" to explore the path to resolve related disputes.

Keywords: juridical investor, ICSID, pierce the corporate veil

1. Introduction

The purpose of this essay is to examine the determination of juridical investors' nationality. Since this issue often arises as a point of contention in international investment disputes, and there are currently no unified criteria to determine it, the essay argues that the ICSID arbitral tribunal and the states need to make joint efforts to solve this problem. The first part of the essay outlines the two different criteria for recognizing juridical investors in current ICSID arbitration practice. Because of the inconsistency in different cases, controversy continues to occur. In the second part, the essay analyzes the ICSID tribunal's decision in Tokios Tokelės v. Ukraine and Mr. Prosper Weil's objection to the court's decision. It is unavoidable to bring up the "piercing the corporate veil" issue while identifying the investors' nationality. It is important to explore whether and how the veil should be pierced because arbitral tribunals have expressed varying views on this matter in various circumstances. Therefore, the third part of the essay uses the examples of TSA Spectrum de Argentina S.A. (TSA) v. Argentina and Barcelona Traction to discuss the principle of piercing the corporate veil. Finally, this essay puts forward solutions to the problems in determining the nationality of juridical person investors to have enlightenment significance for international investment host countries and investment countries.

2. Juridical Person Investors' Nationality

2.1. Establishment Criteria

Establishment criteria refers to the nationality of a juridical person based on the country where the juridical person is established. In AMCO ASIA V. INDONESIA, Indonesia argued that AMCO

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ASIA's subsidiary should not be considered a "foreign corporation." The tribunal dismissed the claim and determined that it was unnecessary to look into the juridical person's real control since doing so would be inconsistent with the intent of the ICSID Convention. A juridical person should be measured by the established place of the juridical person and its place of business [1].

The place of establishment of a legal entity is usually easy to identify in practice and does not change due to changes in the control of the juridical person and its shareholders. Hence, using the criterion of the place of establishment is the easiest way to determine the juridical person's nationality. However, failure to take into account the actual operation and control may make the juridical person a tool to evade the law in a particular country and lead to many disagreements in arbitration cases.

2.2. Substantial Control Criteria

This criterion requires that the person's nationality in effective control of the legal entity be used as the nationality of the legal entity. The nationality of legal entities can also be determined in some Bilateral Investment Treaties (BITs) by "substantial control." Romania asserted in Rompetrol v. Romania that the Claimant's "real and effective" nationality was that of Romania based on ownership and control, effective seat, and source of funds, even though Romania acknowledged that the Claimant met the requirements of ICSID and the Netherlands-Romania BIT [2]. It is clear that even if the juridical person only satisfies the place of incorporation criterion, the actual controller and the place of business are both in the other Contracting State, there will still be a discrepancy in the actual criteria for identifying the juridical person.

3. The Identification of "Juridical Investor" in Tokios Tokelės v. Ukraine

Tokios Tokelės was established as a business enterprise under Lithuanian law and later established a subsidiary in Ukraine under Ukrainian law. Dissatisfied with the improper measures taken by the Ukrainian government against the subsidiary, Tokios Tokelės initiated arbitration, arguing that the Ukrainian government had violated the Ukraine-Lithuania BIT [3]. However, Ukraine objected to the jurisdiction of the ICSID tribunal in this case because Tokios Tokelės had no substantial business activities in Lithuania; on the contrary, it was primarily owned and controlled by Ukrainian nationals and, therefore, should not be considered a Ukrainian investor in Lithuania [4]. The following section analyzes the findings and objections of the ICSID tribunal concerning Tokios Tokelės, a juridical person investor in this case.

3.1. Tribunal's Decision

The ICSID Convention leaves the Contracting Parties to choose how to determine the nationality of legal entities [5]. Instead of limiting the tribunal's authority to hear the matter, Article 25(2)(b) of the ICSID Convention grants the parties a wide-ranging, unlimited freedom to discuss the nationality of a juridical person [6]. So it is necessary to judge the nationality of Tokios Tokelės according to the Ukraine-Lithuania BIT. The tribunal held that the object and the purpose of the Ukraine-Lithuania BIT is to offer comprehensive protection for investors and their assets. It would be contrary to the Treaty's goal and purpose for the Respondent to suggest that the range of covered investors be limited by a control-test [7]. Although Ukraine mentioned that Tokios Tokelės had no substantive business activities in Lithuania and that the actual controller was Ukrainian national, the tribunal held that according to BIT, the parties did not have any special provisions on the definition of juridical person nationality other than the requirement that juridical persons should be established in Lithuanian territory and under Lithuanian law. Therefore, to respect the parties' consent to the greatest extent, substantive business activities do not need to be considered since Tokios Tokelės can be considered a qualified juridical person investor solely on the basis that Tokios Tokelės is established in Lithuania

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and established under Lithuanian law [8]. However, there is no evidence that Tokios Tokelės has committed any fraud or evasion of legal obligations, so this principle does not apply in the present case [9].

3.2. Dissenting Opinion

Mr. Prosper Weil believed that although the BIT signed by the parties should be respected when considering the nationality of juridical investors, the premise is that it should not go beyond the jurisdiction of the ICSID Convention. Considering that the Convention was created as a tool for resolving "international investment issues, not conflicts between States and their Nationals." The ICSID procedure and remedy should not be construed as a means for parties to escape the jurisdiction of their home courts and the application of their national law. Instead, it should be used to encourage and protect foreign investment [10]. However, the tribunal determined that Tokios Tokelės' nationality belonged to Lithuania solely based on the BIT, which is beyond the purpose and scope of the ICSID Convention. There can be no eluding the fact that Tokios Tokelės is unquestionably and entirely under the authority of Ukrainian citizens and interests. Tokios Tokelės was an investor in Ukraine and a national of that country, not a "national of another Contracting State." Mr. Prosper Weil regretted and worried about the Tribunal's decision [11].

3.3. Analysis

In ADC Affiliate Limited and ADC & ADMC Management Limited (ADC) v. Hungary, the arbitral tribunal made a similar decision to Tokios Tokelės v. Ukraine. Hungary considers ADC a shell company controlled by Canadians and, therefore, not a juridical investor in Cyprus. The tribunal rejected Hungary's argument because, under the bilateral investment treaty between Cyprus and Hungary, a "genuine link" is not required to determine the nationality of juridical persons [12]. The essay argues that it is unreasonable to judge the nationality of a juridical investor based solely on the BITs without considering the purpose of establishing the ICSID mechanism. In practice, if a juridical person is incorporated in the host State, but all the controllers are nationals of another State, it may be difficult for the defendant to defend its legitimate interests in the event of a dispute. Therefore, many academics claimed that the logic used by the majority of the Tribunal in Tokios Tokelės was legally and politically faulty [13].

4. The Issue of "Piercing the Corporate Veil"

4.1. Principle of "Piercing the Corporate Veil"

The fundamental criterion for identifying the nationality of juridical investors is to use the establishment place or major place of activity as the basis. However, in some instances, arbitral tribunals used a different approach, known as the "control test," to ascertain the nationality of juridical persons after the parties asked the courts to pierce the corporate veil by rejecting the corporate veil and holding the shareholders behind the juridical person accountable. Essentially, piercing the corporate veil implies ignoring the division between organizations set up in corporate form with restricted responsibility of shareholders [14]. The purpose of the corporate veil under the ICSID mechanism is to find out whether the investor who is the party to the complaint satisfies the requirements of ICSID jurisdiction [15].

4.2. TSA Spectrum de Argentina S.A. v. the Argentine Republic

In TSA v. Argentina, the arbitral tribunal pierced the corporate veil to find the genuine controller of the juridical person. TSA is a company incorporated in Argentina and wholly owned by a Dutch

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corporation (TSI), a company registered in the Netherlands. On the grounds that the Netherlands controlled TSI, TSA filed an arbitration case against Argentina. The government of Argentina claims that Mr. Jorge Justo Neuss was in charge of TSI. Additionally, the TSA's genuine investors utilize TSI as a vehicle to carry out investments even though it has no significant commercial operations in the Netherlands. Argentina therefore considers that TSA's investments involve fraud and bribery and should not benefit from the Argentina-Netherlands BIT. The tribunal eventually agreed with Argentina's position, piercing the corporate veil to see if there was real foreign control, and concluding that an Argentine person was the TSA's true controller. Therefore, the ICSID tribunal lacked jurisdiction to consider the merits of the issue since there was no foreign control [16].

4.3. Decision in Barcelona Traction

The Barcelona Traction was a company incorporated in Canada with shareholders made up of Belgian nationals. Belgium considered that Spain had prejudiced the rights of corporations as well as shareholders and had therefore sought diplomatic protection from the International Court of Justice (ICJ). One of the main issues, in this case, was whether the Barcelona Traction could acquire Belgian nationality by virtue of the nationality of its shareholders, thereby entitling Belgium to institute diplomatic protection. The Court thus commented that in some circumstances, in order to safeguard third parties like a creditor or buyer, to avoid the abuse of legal personality rights, as in some instances of fraud or wrongdoing, or to stop the circumvention of legal responsibilities or requirements, piercing the corporate veil can be adopted. The ICJ ultimately found that there were not sufficiently "exceptional" to pierce the corporate veil and that Belgium was, therefore, not entitled to institute diplomatic protection [17].

4.4. Evaluation

The ICJ has strict requirements for the application of the corporate veil doctrine, but it is not necessary for ICSID arbitral tribunals to follow the practice of the ICJ exactly. While ICSID aims to promote foreign investment, the ICJ's objective of upholding world peace and security is significantly more comprehensive. Since the ICJ is reluctant to determine a corporation's nationality based on the nationality of its owners and management, it might be claimed that ICSID is better positioned to pierce the corporate veil in order to facilitate global economic transactions [18]. From another perspective, the writer argues that the standard for piercing the corporate veil in international investment arbitration should not be too low. It is improper to deny the form of the existence of the company. Furthermore, the nationality of the juridical person is judged in arbitration without considering the company's independence and solely on the composition of the shareholders behind it. The advantages of the corporate structure are significantly diminished when the corporate veil is pierced. Corporations won't want to take business risks that might expose their owners' corporate or personal assets to liability, making it more difficult for creditors to keep track of assets [19].

5. Problems in Identifying Juridical Investors

Since there is still no uniform standard for determining the nationality of juridical person investors, the ICSID arbitral tribunal has made entirely different decisions in different cases, such as Tokios Tokelės v. Ukraine, the arbitral tribunal refused to pierce the corporate veil, holding that the nationality of a juridical person was based on its place of incorporation [20]. However, in TSA v. Argentina, the arbitral tribunal advocated piercing the corporate veil completely and rejected the case's jurisdiction. The discretion of the arbitral tribunal almost determines the determination of qualified investors, and the arbitral tribunal's decision depends entirely on the judgment of different judges. Since arbitrators are now passing judgment on various national policies, many academics

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have questioned the legitimacy of the arbitral tribunal's decision in international practice. They assert that "international investment arbitration now requires a substantial amount of public scrutiny [21]." In addition, the arbitrator's personal prejudice, including cognitive and cultural bias, may have a conscious bias that distorts the arbitrator's judgment [22]. A large number of international investment arbitration practices show that for the same type of case, the arbitral tribunal is very likely to give an opposite ruling, which can be very uneasy for the host State and foreign investors.

6. Possible Solutions

6.1. Clarify in the BIT

When determining the nationality of Tokios Tokelės, the arbitral tribunal determined its nationality to be Lithuania entirely based on the company established in Lithuania. Even if Ukraine argued that the company was lack of substantial commercial links with Lithuania, the tribunal did not adopt this counterargument. It can be seen that BIT has a crucial position in international investment arbitration disputes and may be the primary basis for the arbitral tribunal to make an award. Therefore, during the drafting or negotiation stage of the BIT, host countries and foreign investors should try to be specific and clear about the definition of "qualified investor." For example, an investor must meet both the establishment criteria and "substantial commercial activity" criteria [23]. With relation to corporation nationality, this is the definition that is the restrictive. To effectively claim the nationality of a signatory State, a company must meet three cumulative requirements [24].

6.2. Dealing with "Shell Companies"

Tokios Tokelės v. Ukraine, TSA v. Argentina, and many other cases have involved the identification of shell companies. If there is no meaningful business relationship between a corporation and its country of nationality, it may be regarded as a shell company in practice. Investors usually establish shell companies to realize the interests of the treaty. If parties do not curb this phenomenon, investors may maliciously manipulate the company's nationality, which is not conducive to protecting international investment. Therefore, denial of benefits clauses can be applied in BITs. In the past, they sought to keep "enemy firms" out of treaty protection during hostilities. This provision is still utilized today to prevent treaty shopping. Benefit denial clauses apply where the investor has the nationality of a contracting state but has no substantial commercial connection with that state, and the contracting state may deny the investor the benefit of the treaty. Such clauses help ensure that the company becomes a genuine investor and avoids the formation of shell companies, which are supposed to be protected by international investment treaties.

6.3. Discretion Fairly

In Tokios Tokelės v. Ukraine, the arbitral tribunal respected the principle of "party autonomy" to the greatest extent possible in making the award and advocated the expansion of the ICSID's jurisdiction. However, such an expanded interpretation may damage to the rights and interests of the host State. If arbitrators are free to exercise their discretion, ICSID may have no scruples about expanding its jurisdiction, which is also a flaw in the ICSID arbitration mechanism. The ICSID Arbitration Rules should address this lack of transparency. In international relations theory, "principal-agent theory" and "principal-trust theory" are mainly used to explain the position of international arbitral tribunals. The former emphasizes the entrustment of the parties, and the tribunal should act according to the intentions of the parties; the latter pays more attention to credibility and independence, emphasizing that the arbitral tribunal should not only resolve disputes but also execute arbitral awards with its prestige and credibility to increase the credibility of international investment treaties [25]. These two

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theories explain arbitral tribunals' different positions and approaches to resolving disputes. The essay believes that ICSID should find a balance between these two theories, respecting the parties' intentions without violating the object and purpose of the ICSID and ensuring a neutral ruling.

7. Conclusion

In international investment practice, the determination of the nationality of juridical person investors has been controversial due to the ambiguity of investor definition in the ICSID Convention and bilateral investment treaties. Although arbitral tribunals generally adopt a comprehensive interpretation approach in the cases, the standards applied are sometimes inconsistent. The solution's heart lies in balancing the interests of host countries and foreign investors. The essay analyzes how to solve the problem by analyzing the definition of juridical investors and piercing the corporate veil in ICSID arbitration practice. For the state, it is necessary to be more cautious about the provisions on investor identification in the BIT; For the arbitral tribunal, it is necessary to avoid the personal bias and unreasonable discretion of the judges as much as possible and unify the determination and labeling of the nationality of juridical persons. Only a comprehensive approach can strike a balance between the interests of investors and host countries in the context of the expansion of ICSID jurisdiction.

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