

THE FOREIGN INVESTORS AND NATIONALITY CONCEPT UNDER INTERNATIONAL LAW

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Abstract: *Although in the last years the international community has adopted a broad approach, the definition of foreign investors and foreign investments is still very important for the development of international investment law. The nationality of the foreign investor, whether a natural person or legal entity, sometimes is decisive, especially in front of the international jurisdictions. The paper tries to follow the examples from bilateral investment agreements as well as from multilateral instrument such as the International Centre for Settlement of Investment Disputes (ICSID) Convention. An important case concerning Bulgaria in past decades is also briefly discussed. The authors pay attention to some new moments re-developing the area of investment dispute settlement within the context of EU Mixed Agreements, especially after the EU-Canada Comprehensive Economic and Trade Agreement.*

Keywords: *Investment agreements, ICSID Convention, EU mixed agreements.*

1. INTRODUCTION

In recent years, the legal problems of foreign regulation have received increasing attention. This trend is due to the objective development of economic processes, especially in the 21st century, when investment flows generally increased international trade in goods and services together. At the same time, international investment co-operation acts as a catalyst for globalization processes at almost all levels of the economic development of the world.

International investment law belongs to the broader Public International law, as far as its rules are created on the basis of a voluntary agreement of States' will, and the relations it governs have public nature. The voluntary removal of economic borders agreed upon by States on a global scale poses phenomenal legal challenges. This is most evident in the very fact of the simultaneous interaction and the opposition between the international and national legal systems. Such confrontation is characterized by escalating conflicts over the jurisdiction of States. The latter is particularly relevant to the existing international arbitration mechanism for resolving investment disputes.

2. THE FOREIGN INVESTORS AND THEIR NATIONALITY

The main figure of this kind of legal relationships is a private investor, acting in the absolute majority of cases as a private subject (physical person or legal entity). The subject of legal relationships regulated by international investment law is direct investments whether material or in the form of intellectual property, the conditions of their access at the stage of pre-investment activities, legal regimes of foreign investments, their insurance, the order of resolution of investment disputes, etc.

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The contentious issues arising in foreign investment concern two crucial aspects: the first is the obstacles to the conduct of a foreign investor's business activities, for example, in the form of the deprivation of an investor's license to take a certain kind of activity, the introduction of new taxes; the second is the adoption by the host State of measures that deprive a foreign investor of the opportunity to carry out economic activities, for example in the form of nationalization. As a result, the aggrieved party seeks to recover their rights and to be compensated for the losses suffered. Historically, the protection of foreign investment has been carried out by mechanisms under Public International law. A foreign investor who had suffered damages in connection with the actions of the State in which their property was located could only resort to the diplomatic protection of their own State. And any dispute that arose was seen solely as a dispute between states. Tsirina (2017) found that „the protection of foreign property was based on the principle of state compensation for the nationalized property” (p.107).

The use of the term 'nationality' in relation to legal entities is more than conditional, as opposed to individuals. But this concept is used in the legal literature when it comes to determining the nationality of a legal entity, i.e. the domestic entities from foreign entities. The term 'nationality' became to be used in relation to legal entities in order to establish their relationship with the state.

The nationality of a legal entity is determined by the law related to the legal entity. Under the Private International law, the legal personality of foreign entities may be recognized on the basis of bilateral international treaties which sometimes contain colliding rules.

The question of the admission of a foreign legal entity to perform an economic activity in the territory of the host state is decided by the legislation of the latter. In most countries, such activities are possible when certain rules and conditions set by national law are implemented (direct method).

However, as a result of long-term international practice, general criteria have been developed for the qualification of the subjectivity of domestic or foreign law and order. Such is the theory of incorporation, the theory of settlement, the theory of the center of exploitation, the theory of control. Under the theory of incorporation, the main criteria are that of the establishment or registration of the legal entity. The company is governed by the law and order of the country in which it is established in accordance with its legislation. The same criterion for defining 'nationality' is often applied to the non-profitable foreign entities.

For the theory of an effective residence, the most important is the state where the governing bodies of the company (the board of directors, the other executive bodies) are located, and not where the business activity of the legal entity takes place. Belgium, Spain, Luxembourg, France, Germany and most EU Member States were among the countries that support such a legal position. According to the next theory, the determining place is the place where the legal entity conducts its economic activity. This criterion is accepted by most of the developing countries. The control theory has the greatest application in the sphere of government regulation of foreign investment.

As international economic investment expanded, the question of establishing the nationality of a legal entity was becoming more complex. Traditional ways of determining the nationality of a legal entity are not sufficient in the investment relationship between the host state and the foreign investor. For example, a legal entity established in accordance with the host State legislation cannot always be considered enough to demonstrate the domestic nature of the investor. This forced the international community to adopt a broader control criterion. The theory of

control, in general, is characterized by an individual approach to each case. Thus, in the case *Compania de Aguas del Aconquija, S.A. & Compagnie Générale des Eaux v. Argentina*, the host State challenged the jurisdiction of the ICSID arbitration because the entity (the plaintiff) did not have the status of a foreign investor. According to Farhutdinov (2013), “the ICSID determined control not on the basis of the *de jure* acquisition of shares, but on the fact of *de facto* management of the company” (p.181).

3. THE ESTABLISHMENT OF THE INTERNATIONAL CENTRE FOR THE SETTLEMENT OF INVESTMENT DISPUTES AND THE NATIONALITY CRITERION

If the dispute cannot be resolved through negotiation, the investor’s choice may be referred to the competent court of the contracting party in which the investment is made or to the *ad hoc* arbitration court or to the court established under the UNCITRAL Arbitration Regulations, or to the International Centre for the Settlement of Investment Disputes (ICSID), established under the Convention on the Settlement of Investment Disputes between States and Individuals or legal entities of other states in 1965 (Tsirina, 2017).

It should be noted that in 1965, with the signing of the Convention on the Settlement of Investment Disputes between States and individuals or entities of other states (the 1965 Washington Convention), the International Centre for the Settlement of Investment Disputes (ICSID) was established. It has become a global arbitration institution, which aims to resolve disputes between private investors and recipient states. Based on an international agreement, the 1965 Washington Convention, ICSID has a special position in the system of non-state jurisdictions. On the one hand, the legal basis for ICSID’s work is an international treaty requiring states parties to comply with ICSID decisions as if they were decisions of the highest court of the state (Article 26). On the other hand, the mechanism proposed under the Convention has all the hallmarks of an international commercial arbitration court. The court consists of one arbitrator or any odd number of arbitrators appointed in the agreement of the parties. If the parties do not agree on the number of arbitrators and the order of their appointment, the court is formed as a member of three arbitrators, one of whom appoints each of the parties, and the third, who is the president of the court, is appointed by agreement of the parties (Article 37 of 1965 Washington Convention).

As stated in the legal doctrine (Yulov, 2017), “The main idea of the Convention is, through the establishment of a special investment dispute resolution centre ICSID, to organize the resolution of such disputes between foreign private investors and states that accept these investments internationally” (p.188). According to Article 2 of the Washington Convention, “The purpose of the Center is to provide structures for reconciliation and arbitration in connection with investment disputes between contracting states and individuals or entities of other Contracting States in accordance with the provisions of this Convention”. In both statements, the mixed public-private nature of the investment disputes is underlined.

Nevertheless, it is with the jurisdiction of ICSID to resolve legal disputes that arise directly from investment-related relationships. At the same time, the 1965 Convention does not disclose the meaning of the ‘foreign investment’ term. According to a very well-founded C. Schreuer’s commentary (2000), this concept cannot yet be developed because of the variety of forms, types and methods of investing but “it is, however, feasible to find our particular features of an investment within the Convention based on the ICSID case-law:

- the project ought to have a definite time span;
- there ought to be an established regularity of gain and return;
- there is often a certain risk for the two sides;
- the obligation involved needs to be fundamental;
- the action ought to be a considerable one for the host state's growth" (pp.139-141).

The author has shed light stating that the abovementioned features ought not to be inevitably perceived as jurisdictional demands but as distinctive characteristics of an investment (Schreuer, 2000, p.140).

The decision is binding on the Parties and is not subject to an appeal or other correction, except as stipulated in Art. 52, par.1 of 1965 Washington Convention, namely in cases where:

- The court was improperly formed;
- the court has exceeded its authority;
- there was a corruption of a member of the court;
- there has been a serious deviation from any substantive rule of procedure;
- the decision did not set out the considerations on which it was based.

To this extent, ICSID is a unique non-national regulatory body that serves as a 'line of defence' for foreign investors when disagreements arise with the recipient State.

Article 25(1) of the ICSID Convention defines that: "The jurisdiction of the Centre shall extend to any legal dispute arising directly out of an investment between a Contracting State [...] and a national of another Contracting State [...]". Regarding physical persons, Article 25(2) of the Convention considers "National of another Contracting State" as: "a) 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".

The ICSID Convention demands applicants to initiate that they had the nationality of a Contracting State on two crucial dates: the date of permission to arbitration and 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. An extension of treaty rights to permanent residents cannot extend ICSID's jurisdiction beyond nationals of Contracting States to the ICSID Convention. As regards dual nationality, the ICSID Convention excludes dual nationals, if one of the nationalities is that of the host state (OECD, 2008, p.10).

The problems connected to the nationality of legal entities may even be more complex than for physical persons. Companies nowadays act in manners that could make it quite hard to define nationality. Variety of shareholders, both physical and legal entities themselves from different countries, established under the third state legislation and performing its major business in a fourth state nowadays is a common situation. That is why some bilateral investment treaties also include the test of control explained above. For example, the Netherlands-Bulgaria bilateral investment treaty entered into force on 1 March 2001 covers: "Legal persons not constituted under the law of that Contracting Party but controlled directly, or indirectly by natural persons

as defined in a) or by legal persons as defined in b)", (OECD, 2008, p. 26). However, courts have normally abstained from occupying in substantive investigations of a company's control and they have generally adopted the test of incorporation or location rather than control when defining the nationality of a legal entity.

With the development of international investment law, nonetheless, the nationality criterion has been deprived of some of its significance. As A. Broches (1965), one of the main drafters of the ICSID Convention observed: "... The significance of nationality in traditional instances of an espousal of a national's claim should be distinguished from its relatively unimportant role within the framework of the Convention. In the former case, the issue of nationality is of substantive importance as being crucial in determining the right of State to bring an international claim, while under the Convention it is only relevant as regards the capacity of the investor to bring a dispute before the Centre" (pp. 557, 579-582).

4. *PLAMA V. BULGARIA* CASE AND THE 'DENIAL OF BENEFITS' CLAUSE

Hence, it is the common practice in investment agreements to particularly define the unbiased criteria that make a legal entity a national, or investor, for aims of the treaties, rather than to just count on the term 'nationality' and international law. As investors try to build their legal structure in their favour, states can also search beforehand to avoid claims from particular entities to whom a host state might not want to extend the treaty protection. Therefore, a few treaties themselves comprise 'denial of benefit clauses' permitting exclusion of investors in particular categories. The provision allows the host state the authority efficiently to obtain from the meaning of 'investor' shell companies owned by nationals of a third-country or the host state and companies owned by definite third-country aliens (OECD, 2008, p.28).

This question was raised in *Plama v. Bulgaria* (2005) decision of ICSID concerning the Energy Charter Treaty provisions for the interpretation of the definition of the 'denial of benefits' clauses. Considering the certain language of the ECT, the ICSID ruled against Bulgaria. As pointed by Gaillard (2005), who represented the claimant in this arbitration, contrasting most investment treaties, the Energy Charter Treaty's denial of benefits clause does not operate as a denial of all benefits to the investor. However, it is expressly restricted to a denial of some specific pros covered by Treaty. The question at stake was if the denial of benefits under Article 17(1) of the ECT operates automatically and demands no further action from the host state as argued by the respondent, or if it demands the right to deny to be exercised via positive action taken by the host state as argued by the claimant. In this case, Bulgaria, after it had received the request for arbitration, sent to ICSID a letter by which, under Article 17(1) of the ECT, it denied ECT protection to the claimant. This was done on the reasons that the claimant was "a 'mailbox' company with no substantial business activities in the Republic of Cyprus" (par.31) where it was incorporated and it was not owned or controlled by a national of an ECT state. In fact, the company was owned indirectly by a French individual. As regards Bulgaria's arguments, the tribunal concluded that Plama was ultimately owned by a French individual. France is a party to the ECT and, therefore, Bulgaria could not deny protection to Plama. Bulgaria also argued that the ECT's drafters meant to confer on a host state a direct and unlimited right of denial that might be exercised on any occasion and in any way. On the contrary, the tribunal made it clear "the existence of a 'right' is distinct from the exercise of that right..." (par.155). It additionally held that: "The exercise would necessarily be associated with publicity or other notice so as to become reasonably available to investors and their advisers. To this end, a general declaration

in a Contracting State's official gazette could suffice; or a statutory provision in a Contracting State's investment or other laws; or even an exchange of letters with a particular investor or class of investors" (paras.157-158). The Tribunal further considered that the exercise of this right should have no retrospective effect.

5. A NEW DISPUTE SETTLEMENT FRAMEWORK IN THE EU BILATERAL INVESTMENT AGREEMENTS

After the Lisbon Treaty entered into force, the European Union (EU) has started negotiating EU-wide bilateral investment agreements with the inclusion of investment provisions in its free trade agreements. The Comprehensive Economic and Trade Agreement with Canada (CETA) is the first and foremost EU agreement that was signed by the EU comprising investment protection provisions. Investment provisions contain investment liberalisation measures as well as an investment protection framework with the addition of a dispute settlement mechanism. It is applied for disputes which arise between investors from the partner state and the host state. In the majority of the investment agreements, this investor-state dispute settlement implements an international arbitration framework. Puccio and Harte (2017) observed that "a few concerns raised by civil society regarding the international arbitration framework led the EU to commence a process in order to reform the arbitration provisions". As an outcome of a consultation on the Transatlantic Trade and Investment Partnership with the United States of America, the European Parliament sought their placement of international arbitration with a new system within the framework of EU trade and investment negotiations.

To this date, the new investment court system (ICS) has been already included in most recent free trade agreements entered into by the EU, while suggested in others currently in negotiation. Accordingly, in September 2015, the European Commission's draft text of the Transatlantic Trade and Investment Partnership, which was complemented in November 2015, constituted the first international investment agreement to include the ICS as the mechanism of dispute settlement. Subsequently, in January 2016, the ICS was implemented in the EU-Vietnam free trade agreement, followed by the EU-Canada Comprehensive Economic and Trade Agreement in February 2016. More recently, in April 2018, the ICS has been incorporated in both the EU-Singapore Investment Protection Agreement and the EU-Mexico Trade Agreement.

According to Marin and Paskaleva (2020), thus the EU and Canada renegotiated CETA and established "a new investment court system". Whilst procedurally the framework stays similar to the revised arbitration procedure of the first CETA draft, the ICS itself departs substantially from the arbitration model. The ICS is made up of a tribunal and appellate body. Contrary to the arbitration framework, parties to the dispute shall not be capable of selecting their tribunal members. They would instead be chosen on a rotational basis by a group of judges, appointed for a definite period of time by the CETA Joint Committee.

Due to the low number of cases and to comprise the cost of establishing an ICS, CETA uses the International Centre for Settlement of Investment Disputes as an administrative secretariat, charged with providing organisational and logistical assistance for the ICS proceedings. The alteration to an ICS has been welcomed by a few parties formerly critical of arbitration, but which were open to reform. Nevertheless, a few of the acclaimed system innovations shall be decided exactly after the establishment of the court (such as the code of conduct), and developments shall thus be observed.

For those supporting arbitration, the switch to an ICS is a compromise, that keeps the international investment law dispute settlement framework (though the investor has no say in choosing the tribunal members, as it did under arbitration). The major opposition to the ICS comes from the ones who mainly were in favour of a domestic approach to such disputes. According to Puccio and Harte (2017), “The ICS is an international court and provides an international route for the protection of foreign investment that is different from the human rights route which is open to domestic investors”. Criticisms would perhaps go on in the discussions on a proposed multilateral investment court. Supporters of the domestic approach have also expressed doubts concerning the compatibility of the ICS with the principle of autonomy of the EU legal order. However, the ICS may be differentiated, for different reasons, from past CJEU opinions related to the autonomy of the EU legal order.

The CJEU is not so much concerned with an actual conflict between EU law and international investment law. It is more concerned that a dispute which may potentially include issues of EU law is removed from EU courts (Ankersmit, 2018). To this extend, *Achmea* judgment raises some tension within the EU concerning the autonomous EU legal order as it means the enforcement of decisions coming from investment tribunals before courts of EU member states might become legally impossible.

It should be noted that the European Commission has taken some measures in the last negotiated agreements such as the CETA. This was done because already in Opinion 2/15, the CJEU found that an international dispute settlement mechanism in the EU–Singapore free trade agreement removed disputes from the jurisdiction of EU Member States.

Finally, as Vidal Puig (2019) has concluded *Achmea* and Opinion 1/17 have provided much-needed clarity. Contrary, Ankersmit (2018) considers it as the beginning of the end for the international dispute settlement in and with Europe. What can be summarized is that *Achmea* has confirmed that an intra-EU investor-state dispute settlement is inherently incompatible with the Treaties. In turn, Opinion 1/17 has confirmed that an extra-EU Investor-state dispute settlement is, subject to particular conditions, in harmony with the Treaties. These agreements may be distinguished from intra-EU bilateral investment treaties and are compatible in principle with EU law (Vidal Puig, 2019, p.25).

According to Opinion 1/17, the CJEU decided that the investment court system is compatible in principle with the European Union law. The ruling examined the envisaged in CETA procedure. However, the Court’s reasoning is uniformly relevant to different investment protection agreements with Singapore and Vietnam. The consequences were beyond clarity, bearing in mind the fact that in the past the accession to international dispute settlement bodies had to comply with the autonomy of the European Union legal order.

6. CONCLUSION

The current study reveals the notion of the foreign investors and the concept of their nationality in theory and the existing ICSID case-law. The establishment of the ICSID under the 1965 Washington Convention was a successful step towards the international framework for investment disputes resolution. An important contribution to the formation of the global institutional system in the sphere of foreign investments could be the evolution of the EU bilateral investment agreements such as CETA, and the establishment of the new investment court system.

The legal regulation of foreign investment on a fair and equitable basis is impossible without the harmonious interaction between national and international mechanisms, as well as the development of the EU law.

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