

THE WRONGFUL ACTS OF INDEPENDENT STATE ENTITIES AND ATTRIBUTION TO STATES IN INTERNATIONAL ARBITRATION

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Abstract

In spite of the fact that consent is the main building block of arbitration, arbitral awards have been steady for some years that a claimant need not have a contractual relationship with a respondent state to initiate arbitral proceedings versus this state, *i.e.* states unexpectedly were made respondents in arbitrations under arbitration clauses they have never approved or even bargained.

The main reason for this arbitral attitude is the extraordinary proliferation of multilateral and bilateral investment treaties (BITs) and national investment laws promoting the settlement of investment disputes through arbitration. A host state might in its national law promoting investment offer to submit disputes arising under certain categories of investments to the jurisdiction of any international arbitral institution and the investor might give its consent thereto in writing.

Despite the international acceptance of the aforementioned arbitral attitude among most of the commentators, practitioners suffer the lack of informative and comprehensive academic writings that provide an answer for the question of whether states may incur liability for the acts of their independent entities or not. The imputability of these acts to states is a long discussed and still controversial issue.

The international law rules of attribution assume the violation of an international obligation or attribution of wrongfulness of the conduct to the state, even when it is performed by private entities or subordinate organs of the state.

The concept gives rise to questions of imputability, especially when the state entities involved are under an obligation to act independently and separately without the active involvement or approval of their state. Since, these are issues, which frequently come up in assessing the responsibility of states in respect of the violations committed by their independent entities or emanations, this article throws dark shadow on the various approaches adopted by the ILC Articles, ICSID Convention and Case Law through providing an objective analysis for these approaches dealing with all the emerging related issues such as the doctrine of privity of contracts, differentiation between treaty based claims and contract based claims, the so called umbrella clauses, and the applicability of the theory of *alter ego* in this respect.

The Problem:

Most of the independent state entities do not have the sufficient financial capabilities to meet an award, however the state coffers can do. This point is the main motive that urges claimants in most of the investment disputes to argue that the states themselves are their real counterparties trying to impute the failure of the independent state entities to fulfil their contractual obligations to any kind of default from the part of the states such as bureaucracy, intended change of applicable laws, functional or structural state control over the independent state entity or the disappearance of the independent state entity due to reorganizing policies adopted by the state.

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At the other end of the spectrum, according to article 25 of the ICSID convention, for the Centre to have jurisdiction, certain requirements need to be satisfied. The ICSID jurisdiction *ratione personae* restrict the parties eligible for dispute resolution to a contracting state and a foreign investor. Thus, as regards ICSID jurisdiction, claimants always try to involve states, as their counterparties, in order to let ICSID have jurisdiction and to let tribunals have competence to rule on their claims.

The Intended Meaning of 'Independent State Entities:

For the purpose of this article, an 'independent state entity' means any entity constituted or organized under applicable law, whether or not for profit, governmentally controlled either functionally¹, structurally² or through ownership interests³, by the state; and includes a corporation, trust, partnership, sole proprietorship, branch, joint venture, association, or other organization.

Although the aforementioned definition is written with a considerable clarity, it is important not to confuse some state organs that are required to act independently under the constitutional principle of separation of powers, which is commonly known in the democratic states. The said principle imposes that some state entities must act independently without any kind of control from the part of their governments.

Parliaments, central banks and judicial authorities are glittering examples for this kind of entities. The acts of these entities are not expected to be problematic in the course of this article since they are not expected to be involved directly in an investment due to their political or judicial nature, however the meant independent state entities are those having commercial nature.

It is undeniable that the independent state entities that are required to act independently under the constitutional principle of separation of powers are normally and legally indistinguishable parts of the state notwithstanding their independence, sine the functions carried out by these kinds of state entities are apparently governmental.

In the *Ad hoc* Arbitration, *Eureko B.V. v. Republic of Poland*, one of the issues that were in question was whether the acts of the State Treasury were attributable to the State or not, the Tribunal held that:

'In brief, whatever may be the status of the State Treasury in Polish law, in the perspective of international law, which this Tribunal is bound to apply, the Republic of Poland is responsible to Eureko for the actions of the State Treasury. These actions, if they amount to internationally wrongful act, are clearly attributable to the Respondent and the Tribunal so finds'⁴

¹ The term 'functionally' means that the functions carried out by the independent state entity are described, in accordance to the internal law of the state, to be governmental.

² The term 'structurally' means that the structure of the independent state entity includes any of the state officials as board members or executive managers ...etc.

³ The expression 'through ownership interests' means that the state owns, in particular as a shareholder, some portions in the share capital of the independent state entity.

⁴ *Ad hoc* Arbitration, *Eureko B.V. v. Republic of Poland*, Partial Award and Dissenting Opinion, 19 August 2005, para 134.

The Divergent Approaches of Arbitral Tribunals:

The criteria of structural and functional control of the state over its independent state entities were recently adopted by the ICSID Tribunal in the award rendered on January 25, 2000 in ICSID Case No. ARB/97/7, *Emilio Agustin Maffezini v. Kingdom of Spain*.

The Tribunal held that; for the determination of whether an entity was a state organ whose acts could be attributable to the state, two tests were required to be done; one of them is structural and the other is functional.

According to the Tribunal's view, if on analyzing the structure of an entity it appears to be distinct from the state due to the usage of a corporate veil, the second examination must be done to examine the functional status of this entity so that if it is entrusted with any governmental functions, it will necessarily be deemed to be a state organ whose acts are attributable to the state.

In support to its view the tribunal cited the relevant Article of the ILC Articles on Responsibility of States for Internationally Wrongful Acts⁵ and noted that the functional test was applied⁶, in respect of the definition of a national of a Contracting State, in the decision of the ICSID Tribunal on objections to jurisdiction in the case of *Ceskoslovenska Obchodni Banka, A. S. v. the Slovak Republic*, in which the Tribunal held that the fact of State ownership of the shares of the corporate entity was not sufficient to decide whether the Claimant had standing under the Convention as a national of a Contracting State as long as the activities themselves were essentially commercial rather than governmental in nature.⁷

Indeed the Tribunal provided two objective criteria that will necessarily help the other ICSID Tribunals to decide whether an act of an independent state entity is attributable to the state or not, however it obviously failed to determine clearly the rules and basis, that these structural and functional tests must be done in their conformity, *i.e.* whether the structural and functional tests must be done in conformity to the applicable national law of the host state, relevant customary international law rules or at the discretion of the tribunal...etc.

Indeed, arbitral tribunals had taken divergent positions while dealing with the question of whether the acts of independent state entities can possibly be attributed to states or not, however unlike the ICSID Tribunal in *Emilio Agustin Maffezini v. Kingdom of Spain*, the vast majority of the tribunals applied various tests to determine the status of the involved independent state entities in accordance to the internal laws of the host states.

In *Impregilo S.p.A. v. Islamic Republic of Pakistan*, while examining the status of WAPDA, the involved independent State entity, the Tribunal, at the outset, noted that its examination would be conducted in accordance to the applicable internal law of Pakistan:

⁵ The International Law Commission (ILC) is a U.N. agency that was established in 1947. The mission of ILC is to contribute to codifying the existing customary law and to encourage the progressive development of international law.

⁶ ICSID Case No. ARB/97/7, *Emilio Agustin Maffezini v. Kingdom of Spain*, Decision on Jurisdiction, 25 January 2000, Paras 78-80.

⁷ ICSID Case No. ARB/97/4, *Ceskoslovenska Obchodni Banka, A. S. v. the Slovak Republic* Decision on Objections to Jurisdiction, May 24, 1999, *ICSID Review, Foreign Investment Law Journal*, Vol. 14, 1999, at p. 250.

'The status of WAPDA as a party to the Contracts is a matter for the law of Pakistan, being both the law by which WAPDA was established and exists, and also the law governing the Contracts.'⁸

The Tribunal then proceeded to perform some tests in accordance to the applicable domestic law of Pakistan in order to determine the status of WAPDA.

The Tribunal adopted the criteria of whether the state practiced any structural control over WAPDA *i.e.* did the Pakistani government have the power to appoint any of WAPDA's officials or not, the Tribunal found that:

'WAPDA consists of a Chairman, and not more than three Members appointed by the Government (Section 4). They "receive such salary and allowances" and are "subject to such conditions of service as may be prescribed by the Government" (Section 5). Under Section 6 of the 1958 Act, the Government may remove the Chairman and any Member of the Board for various reasons, in particular if they become, in the opinion of the Government, incapable of discharging their responsibilities under the 1958 Act or if they have been declared to be disqualified for employment in, or have been dismissed from, the service of Pakistan.'⁹

The Tribunal then examined the status of the personnel of WAPDA in order to determine whether working for WAPDA would be deemed as working for Pakistan or not, the Tribunal found that:

'Service under the Authority is considered to be service of Pakistan and every person holding a post under the Authority, not being a person who is on deputation to the authority from any Province, shall be deemed to be a civil servant for the purposes of the Service Tribunals Act, 1973" (Section 17 (1-D)) and within the meaning of Section 21 of the Pakistan Penal Code (Section 19(1)).'¹⁰

The Tribunal also adopted the criterion of functional control *i.e.* whether Pakistan practiced any functional control over WAPDA or not, the Tribunal found that:

'The power and duties of the Authority are defined in Sections 8 to 16 of the Act. Under Section 8, the Authority "shall prepare, for the approval of the Government a comprehensive plan for the development and utilization of the Water and Power resources of Pakistan ...". It also may frame schemes for a province or any part thereof, subject here again to approval by the Government.'¹¹

Finally the Tribunal examined whether Pakistan practiced any financial control over WAPDA or not:

8 ICSID Case No. ARB/03/3, *Impregilo S.p.A. v. Islamic Republic of Pakistan*, Decision on jurisdiction, 22 April 2005, para. 199.

⁹ *Ibid*, para. 202.

¹⁰ *Ibid*, para. 203.

¹¹ *Ibid*, para. 204.

'The accounts of the Authority are audited by the Auditor General of Pakistan. The Auditor Report with the comments of the Authority are sent to the Government and the Authority "shall carry out any directive issued by the Government for rectification of an audit objection". Each year, the Authority submits to the Government for approval a statement of the estimated receipts and expenditures in respect of the next financial year (Section 27).'¹²

After performing all the aforementioned tests the Tribunal then weighed the outcome of these tests as follows:

'Although the Government of Pakistan exercises a strict control on WAPDA, in light of the terms of the 1958 Act that established it, the Tribunal considers that WAPDA is properly characterised as an autonomous corporate body, legally and financially distinct from Pakistan.'¹³

In *Wena Hotels Ltd. v. Egypt*; the dispute arose out of agreements concluded between Wena Hotels Limited (a British Company), and the Egyptian Hotels Company, a State-owned Egyptian company, to develop and manage two hotels in Luxor and Cairo. Wena invoked the Agreement for the Promotion and Protection of Investments between Egypt and the United Kingdom ("Egypt-U.K. BIT"). Egypt raised four preliminary objections to the jurisdiction of the Tribunal and the admissibility of the claim, two of which it subsequently withdrew.

Egypt's second objection was that there was no legal dispute between the Claimant and the Respondent. The Tribunal first noted that the sole shareholder of EHC was Egypt and that EHC's shareholder assembly was chaired by the Minister of Tourism and would be attended by several other government officials. The Minister of Tourism also was responsible for the appointment of at least one half of the Board of Directors of EHC, and furthermore nominated EHC's Chairman. The Tribunal also noted that the Minister of Tourism was also empowered to dismiss the chairman and the members of the Board of EHC if it appears that the continued presence of these persons would affect the proper functioning of the company.

The Tribunal then reached the following conclusion:

'In sum, the Tribunal concludes that Egypt breached its obligations under Article 2(2) of the IPPA by failing to accord Wena's investments in Egypt "fair and equitable treatment" and "full protection and security." Even if the Egyptian Government did not authorize or participate in the attacks, its failure to prevent the seizures and subsequent failure to protect Wena's investments give rise to liability. The Tribunal also finds that Egypt's actions amounted to an expropriation – transferring control of the hotels from Wena to EHC without "prompt, adequate and effective compensation" in violation of Article 5 of the IPPA.'¹⁴

In the Annulment proceedings, the *ad hoc* Committee expressly upheld the Award. The ICSID *ad hoc* Committee rejected all of Egypt's objections to the award of 8 December 2000 in *Wena v. Egypt* as unfounded. Egypt's grounds for annulment were revolving around the differentiation

¹² *Ibid*, para. 207.

¹³ *Ibid*, para. 209.

¹⁴ ICSID Case No. ARB/98/4, *Wena Hotels Ltd. v. Egypt*, Final Award, 8 December 2000, Para 131.

The Committee noted that:

‘The Committee cannot ignore of course that there is a connection between the leases and the IPPA since the former were designed to operate under the protection of the IPPA as the materialization of the investment. But this is simply a condition precedent to the operation of the IPPA. It does not involve an amalgamation of different legal instruments and dispute settlement arrangements. Just as EHC does not represent the State nor can its acts be attributed to it because of its commercial and private function, the acts or failures to act of the State cannot be considered as a question connected to the performance of the parties under the leases. The private and public functions of these various instruments are thus kept separate and distinct.

This Committee accordingly concludes that the subject matter of the lease agreements submitted to Egyptian law was different from the subject matter brought before ICSID arbitration under the IPPA. It follows that it cannot be held that the Parties to the instant case have made a choice of law under the first sentence of Article 42(l) of the ICSID Convention.¹⁵

However both of the Tribunal and the Committee in *Wena* expressly noted that Egypt is not EHC and conversely EHC is not Egypt, and thus the acts of EHC could not possibly be attributed to Egypt, they held Egypt liable for ‘expropriation’ to which Egypt had never contributed to, relying on Egypt’s control over EHC as a pretext for holding Egypt liable noting that Egypt could and should have stopped the acts of EHC.

It seems with clear implication that both the Tribunal and the Committee adopted the *alter ego* doctrine¹⁶ in their findings without providing any relevant justification for this attitude.

The ICSID Convention:

Unfortunately, article 25 of the ICSID convention, while determining the scope of ICSID jurisdiction uses the expression ‘any constituent subdivision or agency of a Contracting State’ repeatedly without providing an accurate and clear definition for this expression and whether it includes the independent state entities as defined above or not.

As regards the expression ‘constituent subdivision’, it only covers the state entities, which are normally and legally indistinguishable parts of the contracting states, but could sometimes have independent legal personalities and are entrusted with some governmental functions.

As regards the term ‘agencies’, it is probably necessary that the entity be acting on behalf of the government of the contracting state to be deemed as an ‘agency’ for the purposes of this portion of the ICSID convention. Remarkably, providing a definition for the term ‘agencies’ might give rise to a lot of difficulties, specially with respect to the question whether the independent state entity is acting as an agent on behalf of the contracting state or not.

Thus the terms ‘constituent subdivision’ and ‘agencies’ are both trite and cannot possibly cover the independent state entities as defined above.

¹⁵ ICSID Case No. ARB/98/4, *Wena Hotels Ltd. v. Egypt*, Decision on Annulment, 5 February 2002, Para 35.

¹⁶ ‘*Alter Ego*’ is the doctrine of the law disregarding the limited personal liability enjoyed when acting in a corporate capacity when no separate identity of the individual and corporation exists.

In *Emilio Agustin Maffezini v. Kingdom of Spain*, the tribunal noted that:

'The Convention contains no criteria dealing with the attribution to the State of acts or omissions undertaken by such State entities, subdivisions or agencies'¹⁷.

Moreover, article 25(3) of the ICSID convention that requires the approval of the contracting state itself for the sake of involving the 'constituent subdivision or agency' of such contracting state as a party, seems to be irrelevant because in the vast majority of the bilateral and multilateral investment treaties, the dispute-settlement provisions contain consents from the contracting states to refer the investment disputes to ICSID.

Eloïse Obadia comments on the issue as follows:

'The investment treaties generally include provisions by which each state party to the treaty undertakes to give investors from the other State or States involved fair and equitable treatment; full protection and security; prompt, adequate and effective compensation in the event of expropriation; and freedom from currency transfer restrictions. In addition, most of these treaties contain broad definitions of the investments and of the disputes covered.

Investors have used quite extensively, and sometimes creatively, these broad definitions to bring claims that the States party to the treaty had not necessarily contemplated at the time of the drafting. Not surprisingly, objections to jurisdiction have been raised by the respondent host States in all but 2 cases.

These objections reflect some of the complexity of bringing cases under investment treaties. The jurisdiction of the Centre, as well as of the competence of tribunals, must be established under either the ICSID Convention (or the ICSID Additional Facility Rules), and the bilateral or multilateral treaty concerned.'¹⁸

The ILC Articles on Responsibility of States for Internationally Wrongful Acts:

Chapter II of the ILC Articles on Responsibility of States for Internationally Wrongful Acts provides a wider scope for the attribution of conduct to a state than that provided under the ICSID Convention. Article 4(1) of the ILC Articles provides:

'The conduct of any State organ shall be considered an act of that State under international law, whether the organ exercises legislative, executive, judicial or any other functions, whatever position it holds in the organization of the State, and whatever its character as an organ of the central government or of a territorial unit of the State.'

It is quite clear that this Article covers the state entities, which are normally and legally indistinguishable parts of the contracting states, and expressly adopts the criterion of 'governmental functions' for attributing the conduct of any state organ to the state itself.

¹⁷ ICSID Case No. ARB/97/7, *Emilio Agustin Maffezini v. Kingdom of Spain*, Decision on Jurisdiction, 25 January 2000, Para 74.

¹⁸ *ICSID, Investment Treaties and Arbitration: Current and Emerging Issues*, Eloïse Obadia, Counsel, ICSID, a paper delivered at the Swiss Arbitration Association Conference on Investment Treaties and Arbitration, held in Zurich on January 25, 2002, published at <http://www.worldbank.org/icsid/news/n-18-2-4.htm>.

This approach is totally logic and acceptable for most of the concerned investors and states, since there is no doubt that any entity which practices one or more governmental functions is an indistinguishable part of the state and all its acts should be attributed to the state itself, however this approach gives rise to the following question: how can the status of a state organ be known? In other words: On which basis one can decide that an entity is a state organ, which practises one or more governmental functions? Article 4(2) of the ILC Articles answers this question as follows:

‘An organ includes any person or entity which has that status in accordance with the internal law of the State.’

Thus the basis for deciding that an entity is a state organ, which practises one or more governmental functions, is the provisions of the applicable domestic law of that state.

Article 5 of the ILC Articles provides a much wider approach for attributing the acts of separate state entities to states, the said article provides:

‘The conduct of a person or entity which is not an organ of the State under article 4 but which is empowered by the law of that State to exercise elements of the governmental authority shall be considered an act of the State under international law, provided the person or entity is acting in that capacity in the particular instance.’

In the above terms, Article 5 of the ILC Articles provides that the acts of independent state entity are attributable to the state, if, and only if, this state entity is empowered by the law of that state to exercise elements of governmental authority, *i.e.* to practice some of the state sovereign powers. Moreover the act of that state entity, that is to be examined for attributability must be committed by such independent entity in its capacity as an empowered entity to exercise elements of the governmental authority

In light of the aforementioned approach, the ILC Articles stake out the issue of attributability through requiring the simultaneous fulfilment of two conditions, in order to deem an act of an independent state entity attributable to the state; the first condition concerns the ‘status of the independent state entity’ and whether it is empowered to exercise some sovereign powers of the governmental authority or not, and the second one concerns the ‘nature of the act itself’ and whether it is a sovereign act that is committed by the independent state entity in its capacity as an empowered entity to exercise elements of the governmental authority or not.

Indeed the ILC Articles approach seems to be fair and acceptable, however the critical question that comes up frequently in this connexion is: what is meant exactly by the expression ‘elements of governmental authority’?

Unfortunately the ILC Articles do not provide a definition for this expression; however, some arbitral tribunals gave the answer for this question. In *Impregilo S.p.A. v. Islamic Republic of Pakistan*, the ICSID tribunal, with a clear implication adopted the approach of the ILC Articles in respect of attributing the acts of the involved independent state entity ‘WAPDA’ to Pakistan, and thus differentiated between two categories of acts; namely sovereign or governmental acts and the acts committed by the independent state entity as a contracting noting that treaty based claims must be arising out of the former category of acts.

The tribunal held that:

‘In fact, the State or its emanation, may have behaved as an ordinary contracting party having a difference of approach, in fact or in law, with the investor. In order that the alleged breach of contract may

constitute a violation of the BIT, it must be the result of behaviour going beyond that which an ordinary contracting party could adopt.¹¹⁸ Only the State in the exercise of its sovereign authority (“*puissance publique*”), and not as a contracting party, may breach the obligations assumed under the BIT. In other words, the investment protection treaty only provides a remedy to the investor where the investor proves that the alleged damages were a consequence of the behaviour of the Host State acting in breach of the obligations it had assumed under the treaty.¹¹⁹

The ICSID Tribunal in *Joy Mining Machinery v. Egypt* brought the same distinction expressly. The Tribunal held that:

‘A basic general distinction can be made between commercial aspects of a dispute and other aspects involving the existence of some forms of State interference with the operation of the contract involved.’¹²⁰

Privity of Municipal Investment Contracts:

The doctrine of ‘privity of contracts’ provides that a contract cannot confer rights or impose obligations arising under it on any person or agent except the parties to it.¹²¹

Clearly it is fair that states should not incur obligations in respect of contracts to which they are not party.

The ICSID Tribunal in *Impregilo S.p.A. v. Islamic Republic of Pakistan* implicitly adopted the doctrine of ‘privity’ of contracts, the Tribunal found that WAPDA, the involved independent state entity, is an ‘autonomous corporate body, legally and financially distinct from Pakistan’¹²², then brought a distinction between treaty based claims and contract based claims and finally reached the following conclusion:

‘Given that the Contracts at issue were concluded between the Claimant and WAPDA, and not between the Claimant and Pakistan; that under the law of Pakistan, which governs both the Contracts and the status and capacity of WAPDA for the purposes of the Contracts, WAPDA is a legal entity distinct from the State of Pakistan; and given that Article 9 of the BIT does not cover breaches of contracts concluded by such an entity, it must follow that this Tribunal has no jurisdiction under the BIT to entertain Impregilo’s claims based on alleged breaches of the Contracts.’¹²³

¹⁹ ICSID Case No. ARB/03/3, *Impregilo S.p.A. v. Islamic Republic of Pakistan*, Decision on jurisdiction, 22 April 2005, para. 260.

²⁰ ICSID Case No. ARB/03/11, *Joy Mining Machinery v. Egypt*, Decision on Jurisdiction, 30 July 2004, para 72.

²¹ Kevin's collaborative English law glossary, at: <http://law.web-tomorrow.com>.

²² ICSID Case No. ARB/03/3, *Impregilo S.p.A. v. Islamic Republic of Pakistan*, Decision on jurisdiction, 22 April 2005, para. 209.

²³ *Ibid*, para. 216.

The same approach was adopted by the ICSID Tribunal in *Salini Costruttori S.p.A and Italsrade S.p.A. v the Hashemite Kingdom of Jordan*, where Jordan disputed the Tribunal's jurisdiction to hear a claim commenced by Salini pursuant to the bilateral investment treaty between Italy and Jordan.

Having analysed the relevant provisions of the BIT and the contract in question, the Tribunal accepted jurisdiction over Salini's alleged treaty claims (*i.e.* claims based on Jordan's alleged breach of the BIT), but declined jurisdiction over Salini's breach of contract claims.

The Tribunal found that JVA, the involved independent state entity, is 'an autonomous corporate body, distinct legally and financially from the State of Jordan' and thus held that the contractual claims would only fall within its jurisdiction if the alleged breach of contract also represented a breach of the BIT.²⁴

On the other hand the Tribunal noted that:

'Lastly, the Tribunal will note that the dispute settlement procedures provided for in the Contract could only cover claims based on breaches of the Contract. Those procedures cannot cover claims based on breaches of the BIT (including breaches of those provisions of the BIT guaranteeing fulfillment of contracts signed with foreign investors). Therefore Article 9(2) does not deprive the Tribunal of such jurisdiction, as it may have, to entertain treaty claims of this nature under other provisions of the BIT.'²⁵

Thus it is quite apparent that arbitral tribunals that are constituted in accordance to a dispute resolution regime included in a BIT do not have jurisdiction to rule on contract based claims, because of the privity of municipal contracts, since states can not possibly incur liability in respect of contracts to which they are not parties.

In the above sense, a dispute resolution regime included in a BIT can not possibly override a forum selection clause included in a municipal contract in respect of contract based claims.

Conversely, a forum selection clause in a municipal contract can not possibly override a dispute resolution regime included in a BIT in respect of treaty based claims.

The ICSID Tribunal in *Joy Mining Machinery v. Egypt* expressly reached the conclusion set above. The tribunal found that there was no treaty based claims, and thus held that:

'Having concluded that there is no investment in this case and that, moreover, all the claims involved are in any event contract-based claims, it is necessary also to conclude that in the absence of any ICSID jurisdiction only the forum selection clause stands.'²⁶

Insufficiency of Circumstantial Evidence For State Involvement In Municipal Contracts:

State practices may allow claimants in international investment disputes to rely on some circumstantial evidences in order to prove the involvement of states in municipal contracts. For example a state official may attend a ceremony for signing a municipal investment

²⁴ ICSID Case No. ARB/02/13, *Salini Costruttori S.p.A and Italsrade S.p.A. v the Hashemite Kingdom of Jordan*, Decision on Jurisdiction, 15 November 2004, paras 84-96.

²⁵ *Ibid*, para 96.

²⁶ ICSID Case No. ARB/03/11, *Joy Mining Machinery v. Egypt*, Decision on Jurisdiction, 30 July 2004, para 89.

agreement that is concluded between an independent state entity and a foreign investor. The critical questions are: does this mean that the state approves the conduct of the independent state entity and thus this conduct can possibly be attributable to that state? Can the attitude of the state be deemed as 'equitable estoppel'²⁷, which prevents it from taking a different position while conducting the arbitration proceedings?

In the Final Arbitral Award Rendered in SCC Case No. 49/2002, the Claimant contended that it was inconceivable that the independent state entity could have entered the municipal agreement with him without reaching the approval of the government. In support of his contention, the Claimant referred to various meetings with ministers and high officials who had encouraged his contacts with the independent state entity and been informed of how these contacts developed. Those officials had also been aware of and had been satisfied with the agreement, which was the result of these contacts.²⁸

The Tribunal declined the claimant's contention and held that:

'However, the Arbitral Tribunal does not find it necessary, for the purposes of this case, to go into details in this regard but finds it sufficient to note that, in any event, there is no convincing evidence of such concrete Government involvement in connection with the conclusion of the Cooperation Agreement as would make [the Republic responsible for the implementation of the Agreement].²⁹

Moreover in the famous Pyramids Case, ICC Case No. 3493 *SPP (Middle East) Ltd. (Hong Kong) and Southern Pacific Properties Ltd. (Hong Kong) v. Arab Republic of Egypt*, where "Heads of Agreement" were executed concerning a tourist village on the Pyramids Plateau (the "Pyramid Oasis" Project) and a similar tourist resort at Ras-El-Hekma on the Mediterranean coast in Egypt. Parties to this Agreement were SPP, the Minister of Tourism and EGOH (Egyptian General Organisation for Tourism and Hotels). This Agreement was followed by a second agreement on December 12, 1974, between SPP and EGOH. However, beneath the signatures of their representatives, the words appeared "approved, agreed and ratified by the Minister of Tourism" and signature of the Minister. The Heads of Agreement did not contain an arbitration clause whereas the December Agreement did, providing for ICC arbitration.

In the early part of 1978, the Pyramids Oasis project was domestically attacked on both legal and environmental grounds. In response to this criticism, both the Minister of Tourism and the Minister of Economy defended the project in the People's Assembly. Yet, at the end of May 1978, the project was stopped by various measures of the Egyptian Government.

When an amicable settlement proved to be impossible, SPP initiated ICC arbitration against both the Egyptian State and EGOH, claiming approximately US\$ 42,500,000 as damages. Egypt objected to the competence of the arbitrators, arguing that it was not a party to the December Agreement in which the arbitration clause was included.

²⁷ The term 'estoppel' means a bar, which precludes someone from denying the truth of a fact, which has been determined in an official proceeding or by an authoritative body. There are two kinds of estoppel; (1) Collateral estoppel prevents a party to a lawsuit from raising a fact or issue, which was already decided against him in another lawsuit. (2) Equitable estoppel prevents one party from taking a different position at trial than it did at an earlier time if the other party would be harmed by the change.

²⁸ SCC Case No. 49/2002, STOCKHOLM ARBITRATION REPORT 2004:1, Juris Publishing, Inc., p. 162.

²⁹ SCC Case No. 49/2002, STOCKHOLM ARBITRATION REPORT 2004:1, Juris Publishing, Inc., p. 163.

By an award dated February 16, 1983, made in Paris, the arbitrators held that Egypt was a party to the December Agreement and ordered Egypt to pay SPP US\$ 12,500,000 as damages plus interest and costs.³⁰

By writ of March 28, 1983, Egypt requested the Court of Appeal of Paris to set aside the award on the basis of Art. 1504 jo. 1502 nos. 1 and 5 of the French New "113" Code of Civil Procedure, alleging that it had never waived its immunity from jurisdiction, Egypt asserted that the arbitral tribunal had decided without any arbitration agreement and that the award had been rendered in violation of international cultural public policy and in violation of the sovereignty of States. SPP requested the Court to dismiss Egypt's action for the reasons indicated below in the Court of Appeal's judgment.

On July 12, 1984, the Court of Appeal in Paris set aside the award for lack of an arbitration agreement binding Egypt, noting that the tribunal had wrongly decided that the actions of the state had made it a party to the contract between the Claimant and EGOTH. This decision was later upheld in the court of cassation in Paris. The court of cassation in Paris reached this conclusion after reviewing post-contract correspondence between the Claimant and EGOTH, noted clear references to distinct to the distinction between EGOTH and Egypt.³¹

Qualification As Treaty Based Claims:

A BIT gives an investor an opportunity to assert specific types of claims that are usually specified in the invoked BIT. A common claim is that the host State failed to guarantee "fair and equitable treatment." Fair and equitable treatment is a standard set by international law, according to which each state is required to offer fair and equitable treatment with regard to the investments of foreign nationals.

Under international law rules, "fair and equitable treatment" is a recognized legal standard that is fully distinct from the host state's domestic laws. Clarifying the requirements of this standard, the ICSID Tribunal in *Genin, Eastern Credit Limited, Inc. and A.S. Baltoil v. Estonia*³² held that a violation of this kind could be established by "acts showing willful neglect of duty, an insufficiency of action falling far below international standards, or even subjective bad faith." and thus It went on to reject the claimant's claim on the grounds that the treatment complained of did not "rise to the level of violations of the international law standards of 'fair and equal treatment' and 'non-discriminatory and non-arbitrary treatment' of investment," as those standards were reflected in Articles II(3)(a) and (b) of the United States-Estonia BIT. I

Another common claim that can be asserted under a BIT is "expropriation" of an investment by the host state. Almost all BIT claims filed with the ICSID have alleged "host-state responsibility for some form of expropriation without compensation". Indeed, BITs do not prohibit all forms of expropriation, since it is permitted for public purposes; however it must be conducted in a non-discriminatory manner and should be accompanied by "prompt, adequate and effective compensation."

For example, the BIT between Egypt and the United Kingdom provides that "investments are not to be nationalized or expropriated except for a public purpose 'related to the internal needs' of the host state and the state must pay 'prompt, adequate and effective' compensation."³³

³⁰ ICC Yearbook, *Commercial Arbitration*, P. Sanders (ed.), Vol. IX (1984), pp. 111 —123.

³¹ *State as Party to Arbitration*, George Rosenberg, *Arbitration International*, Vol. 20 No. 4, pp. 387 – 409.

³² ICSID Case No. ARB/99/2, *Genin, Eastern Credit Limited, Inc. and A.S. Baltoil v. Estonia*, Award, 25 June 2001.

³³ The Agreement for the Promotion and Protection of Investments, June 11, 1975, U.K.-Egypt, art. 5.

If an expropriation is conducted, the issue of compensation must come up. In *Middle East Cement v. Egypt*, the tribunal found that the Claimant's chartered ship had been expropriated within the meaning of the Egypt-Greece BIT and awarded the claimant compensation and compound interest.³⁴

Differentiation Between Contract Based Claims and Treaty Based Claims:

One of the most important issues that always come to the fore during conducting arbitration proceedings is the differentiation between contract based claims and treaty based claims, which play an important role to weigh the state liability pertaining to a dispute arising out of a contract that was concluded between any of the state independent entities and an investor.

Obviously, the various approaches of the arbitral tribunals lack uniformity while dealing with the issue of differentiating between contract based claims and treaty based claims, and this attitude can be attributed to the differences between the applicable BITs and forum selection clauses invoked by the parties to the concluded cases, however the principle of distinguishing treaty based claims from contract based claims seems to be applied uniformly by various arbitral tribunals in the course of reasoning their jurisdictional findings, particularly in ICSID arbitrations.

The decision rendered in the annulment proceedings in ICSID Case No. ARB/97/3, *Compania de Aguas del Aconquija S.A. and Vivendi Universal v. Argentine Republic*, approached the issue of differentiation between contract based claims and treaty based claims. The dispute originally arose out of certain alleged acts of the Argentine Republic and its constituent Province of Tucumán that, according to Claimants, caused the termination of a thirty-year concession contract.

During the flow of the arbitration proceedings, Claimants asserted that all of these acts were attributable to the Argentine Republic under international law and, as such, violated Argentina's obligations under the Agreement between the Government of the Argentine Republic and the Government of the Republic of France for Reciprocal Protection and Promotion of Investments of 3 July 1991. On the other hand the Argentine Republic argued that the tribunal did not have jurisdiction to rule on the dispute since the dispute arose out of the concession contract, which included an exclusive Jurisdiction clause in favour of the domestic courts of the Argentine Republic.

The tribunal held that it had jurisdiction to rule on the dispute and provided as reasoning in support of its jurisdictional finding that the claims of the Claimant concerning the actions of the federal government of Argentina as well as those of the provincial authorities of Tucumán were properly characterized as treaty based claims arising under the BIT, and not as contract based claims arising out of the concession agreement.

The Tribunal added that; under international law, the acts of organs of both the central government and provincial authorities are attributable to the state and thus the Argentina Republic could not rely on its federal structure in order to exclude its treaty obligations from the jurisdiction of the Tribunal.

The Tribunal also noted that Article 25 (3) of the ICSID Convention which, in the Tribunal's view, intended to allow the constituent subdivisions or agencies of a contracting state to be parties in an investment dispute before an ICSID Tribunal in their own capacity, where they have so consented and the concerned contracting state has approved.

³⁴ ICSID Case No. ARB/99/6, *Middle East Cement v. Egypt*, Award, 12 April 2002.

The Tribunal further clarified that Article 25 (3) neither limits the scope of the state's international responsibilities in accordance to the normal rules of attribution nor qualifies the jurisdiction of an ICSID tribunal over that state. Similarly, in the Tribunal's view, Article 16 (4) of the Concession Contract, which provides a forum selection clause in favour of the domestic courts of Argentine, did not exclude the jurisdiction of the Tribunal under the BIT. The Tribunal added that the claims of the Claimants would not be subject to the jurisdiction of the contentious administrative tribunals of Tucumán in accordance to the forum selection clause, if those claims were not based on the concession contract but alleged a cause of action under the BIT.³⁵

The committee, in its Decision on Annulment, agreed with the tribunal's view and held that:

'In particular, the Committee agrees with the Tribunal in characterising the present dispute as one "relating to investments made under this Agreement" within the meaning of Article 8 of the BIT. Even if it were necessary in order to attract the Tribunal's jurisdiction that the dispute be characterised not merely as one relating to an investment but as one concerning the treatment of an investment in accordance with the standards laid down under the BIT, it is the case (as the Tribunal noted) that Claimants invoke substantive provisions of the BIT.

The Committee likewise agrees that the fact that the investment concerns a Concession Contract made with Tucumán, a province of Argentina which has not been separately designated to ICSID under Article 25 (1), does not mean that the dispute falls outside the scope of the BIT, or that the investment ceases to be one "between one Contracting Party and an investor of the other Contracting Party" within the meaning of Article 8 (1) of the BIT.

This being so, the fact that the Concession Contract referred contractual disputes to the contentious administrative courts of Tucumán did not affect the jurisdiction of the Tribunal with respect to a claim based on the provisions of the BIT. Article 16 (4) of the Concession Contract did not in terms purport to exclude the jurisdiction of an international tribunal arising under Article 8 (2) of the BIT; at the very least, a clear indication of an intention to exclude that jurisdiction would be required.'

The International Law Rules of Attribution Do Not Apply to Contract Based Claims:

Moreover, the committee in the annulment proceedings in *Compania de Aguas del Aconquija S.A. and Vivendi Universal v. Argentine Republic* reached a very important conclusion pertaining to the impact of distinguishing treaty based claims from contract based claims on the issue of attributing the acts of independent state entities to states, the committee expressly held that examining BIT breaches must take place in accordance to the applicable rules of international law, however, examining contract breaches must take place in accordance to the proper applicable law of the contract, in other words; contract based claims do not give rise to the application of the international law rules of attribution since the state can not possibly be deemed internationally responsible for the performance of contracts entered into by an independent state entity, as defined above, which possesses a separate legal personality under its own law and is solely responsible for the performance of its own contracts, on the other hand, the international law rules of attribution must apply to treaty breaches because the state is internationally liable , under the invoked treaty, to perform all of

³⁵ ICSID Case No. ARB/97/3, *Compania de Aguas del Aconquija S.A. and Vivendi Universal v. Argentine Republic*, Decision on Annulment, 21 November 2000, Para 14.

the obligations concerning the protection of investments made in its territories by a means of a national of the other contracting state or states.³⁶

The ICSID Tribunal in *Impregilo S.p.A. v. Islamic Republic of Pakistan*, where an independent state entity called WAPDA was involved, explicitly reached the same conclusion, the Tribunal held that:

‘This approach to the issue of overlapping Treaty and Contract Claims – i.e. to recognise that even if the two coincide, they remain analytically distinct - is all the more apposite because of the different rules of attribution that govern responsibility for the performance of BIT obligations, as opposed to responsibility for breaches of municipal law contracts. In this respect, the Tribunal has noted in Section IV.A above that the legal personality of WAPDA is distinct from that of the State of Pakistan, and that the Contracts were concluded by that authority rather than the State itself. As a consequence, the Tribunal has declined to exercise jurisdiction over the Contract Claims presented by Impregilo. In contrast, under public international law (i.e. as will apply to an alleged breach of treaty), a State may be held responsible for the acts of local public authorities or public institutions under its authority. The different rules evidence the fact that the overlap or coincidence of treaty and contract claims does not mean that the exercise of determining each will also be the same.’³⁷

The Impact of Umbrella Clauses:

Most of the ICSID Tribunals uniformly brought distinctions between treaty based claims and contract based claims in the same manner³⁸ citing the annulment decision rendered in ICSID Case No. ARB/97/3, *Compania de Aguas del Aconquija S.A. and Vivendi Universal v. Argentine Republic*, however in the cases where the effectiveness of the so called ‘Umbrella Clause’ is in question, the considerable importance of distinguishing treaty based claims from contract based claims is obviously diminished because both kinds of claims coincide, overlap and appear to be an amalgam of breaches and infractions

Umbrella clauses create a reciprocal international obligation owed by the states to each other that requires them, as host states in accordance with the provisions of the ICSID Convention, to observe obligations they have entered into with investors who are nationals of another contracting state under both of the applicable BIT and the provisions of a municipal contract that is entered between one of the state entities and the investor regardless of the status of that state entity.

Recently, two contrasting decisions on jurisdiction were rendered in two ICSID Cases involving extensive contentions about umbrella clauses; the August 2003 decision in *SGS Société Générale de Surveillance SA v. Islamic Republic of Pakistan*, and the contrasting decision of January 2004 in *SGS Société Générale de Surveillance SA v. Republic of the Philippines*.

³⁶ *Ibid*, para 96.

³⁷ ICSID Case No. ARB/03/3, *Impregilo S.p.A. v. Islamic Republic of Pakistan*, Decision on jurisdiction, 22 April 2005, para. 262.

³⁸ See also ICSID Case No. ARB/00/4, *Salini V. Morocco*, Decision on Jurisdiction.

In the ICSID Case No. ARB/01/13, *SGS Société Générale de Surveillance SA v. Islamic Republic of Pakistan*, SGS relied on the umbrella clause in order to claim that a contract breach was equal to a treaty breach. Article 11 of the applicable BIT states:

‘Either Contracting Party shall constantly guarantee the observance of the commitments it has entered into with respect to the investments of the investors of the other Contracting Party.’

The tribunal, after showing a narrow interpretative attitude while interpreting the aforementioned article, held that such article did not automatically elevate breaches of contract to a breach of the BIT and consequently did not give rise to the application of international law rules. In so deciding, the tribunal illustrated the influence of adopting the claimant’s view would enable investors to override the forum selection clauses negotiated in the investment agreements and this will normally lead to an unintended situation, *i.e.* that the host state would not be able to benefit from the forum selection clause that was originally bargained and agreed.³⁹

In a contrasting approach to the issue, the Tribunal, in ICSID Case No. ARB/02/6, *SGS Société Générale de Surveillance SA v. Republic of the Philippines*, where the claimant relied on the BIT umbrella clause in order to let the Tribunal have jurisdiction over the contract based claims. Article X (2) of the applicable BIT reads:

‘Each Contracting Party shall observe any obligation it has assumed with regard to specific investments in its territory by investors of the other Contracting Party’

The Tribunal while interpreting the aforementioned umbrella clause recognised that its approach contradicted with the Tribunal’s approach in the ICSID Case No. ARB/01/13, *SGS Société Générale de Surveillance SA v. Islamic Republic of Pakistan*, SGS and justified this apparent contrast as follows:

‘This provisional conclusion—that Article X(2) means what it says—is however contradicted by the decision of the Tribunal in *SGS v. Pakistan*, the only ICSID case which has so far directly ruled on the question. It should be noted that the “umbrella clause” in the Swiss-Pakistan BIT was formulated in different and rather vaguer terms than Article X(2) of the Swiss-Philippines BIT.’⁴⁰

Thus it seems that the wording of umbrella clauses was of considerable importance for the two ICSID Tribunals to the extent that urged them to adopt two divergent approaches, ascribing such disparity to the clarity of the umbrella clause that was in question in the two cases.

The *Alter Ego* Doctrine (Corporate Veil Piercing):

Literally, an *alter ego* is a second self. Under the *alter ego* doctrine, a court may look past a corporate status in order to get to the individual stockholders themselves, where the

³⁹ ICSID Case No. ARB/01/13, *SGS Société Générale de Surveillance SA v. Islamic Republic of Pakistan*, SGS, Decision on Jurisdiction, 6 August 2003, Paras 163-177.

⁴⁰ *Ibid*, para 119.

stockholders have wholly disregarded the corporate form and corporate formalities. This exposes the stockholders to personal liability beyond the amount of their investment.^{41 42}

When a corporation is formed, a “corporate veil” is created between the personal assets of the founders and the business. When properly managed, corporate veils provide significant personal liability protection against lawsuits, creditors, and other disputes. However, to prevent Piercing the Corporate Veil the founders must do more than merely form a business entity and register it with the state. There are a host of ongoing governance requirements and formalities for business owners under most of the applicable laws. If challenged in a lawsuit, the founders must be able to prove that they have a bona fide business entity. They will be challenged to show that they have a real business, not just a sham created to dodge their personal liability.

Under Piercing the Corporate Veil, the corporate form is used to perpetuate a fraud, circumvent a statute, or accomplish some other wrongful or inequitable purpose, the courts may decide not observe the separation of the corporate entity from its stockholders, and it may deem the corporation’s acts to be those of the persons or organizations actually controlling the corporation.

As shown above the doctrine of ‘*alter ego*’ was originally created by the jurisprudence to test whether the acts of a company can possibly be attributed to the founders of that company personally or not, and thus it can not fit the question of attribution in respect of the acts of the independent state entities.

Moreover the application of this doctrine requires the absence of corporate formalities to be established in addition to evident intermingling of the finances and directorship of both the independent state entity and state itself. This position can not be proved easily in light of the fact that the state is an external party that does not, by definition, have a contractual relationship with either the independent state entity or the foreign investor.

Conclusion:

Although applying all the possible tests by arbitral tribunals to find whether the acts of an independent state entity can possibly be attributed to states or not is an acceptable attitude, tribunals should avoid the questions of intention in this respect. Adopting the approaches pertaining to the intention of the parties in respect of attribution may mislead to the application of irrelevant doctrines or notions like that of ‘*alter ego*’, ‘estoppels’ and ‘circumstantial evidence’ which are not expected to suit the question of attribution since their requirements are not present *ab initio* where the independent state entity is explicitly established as an independent entity under the applicable domestic law of the host state and unequivocally has right to enter contracts on its own behalf , sue and be sued in its own capacity.

⁴¹ LEGAL – TERM . COM, at <http://www.legal-term.com/alteego-definition.htm>.

⁴² The Abridged Law Dictionary, English-Arabic, Asser M. Harb, 2008, p. 22.