

# Dispute Resolution Hotline

December 11, 2013

## ICSID TRIBUNAL INTERPRETS SCOPE OF 'INVESTOR' AND 'INVESTMENT': SHOULD INDIA KEEP A CLOSE WATCH?

- ICSID Tribunal interprets the scope of the words '*Investor*' and '*Investment*' for disputes under the Washington Convention.
- ICSID Tribunal has reaffirmed that the term '*Investment*' in a Bilateral Investment Treaty, under Washington Convention, should be defined in accordance with relevant factors such as contribution or allocation of resources, duration, and risk which includes the expectation of a commercial return.
- By signing the Washington Convention, India could limit claims from such entities who under established international standards don't qualify as '*Investor*' and/or '*Investment*'.

Recently in *KT Asia Investment Group B.V. v. Republic of Kazakhstan*<sup>1</sup>, the Tribunal constituted under the rules of International Centre for Settlement of Investment Disputes ["**ICSID Tribunal**"], has declined jurisdiction on the ground that there was no '*Investment*' for the purposes of the Convention on the Settlement of Investment Disputes between States and Nationals of Other States ["**Washington Convention**"] and Agreement on encouragement and reciprocal protection of Investments between the Republic of Kazakhstan and the Kingdom of the Netherlands ["**Treaty**"].

### FACTS

KT Asia Investment Group B.V. ["**Claimant**"] was a company incorporated in the Netherlands. However, the ultimate beneficial owner of the Claimant was Mr. Mukhtar Ablyazov, ["**Ablyazov**"] a private businessman and Kazakh national. The substance of the dispute concerned the Claimant's allegations of a forced nationalization by the Republic of Kazakhstan ["**Respondent**"] of the Claimant's minority interest in the BTA Bank ["**BTA**"].

In 1998 Ablyazov along with a consortium of investors purchased BTA for US\$72 million. Ablyazov controlled 75.18% of BTA, which had been acquired in stages, through a series of separate companies incorporated in different jurisdictions under the direction of trusted associates. Each of the companies, ultimately beneficially owned by Ablyazov, held less than 10% of the shares of BTA.

On August 1, 2007, the Treaty entered into force. On December 12, 2007 the Claimant was incorporated in Rotterdam as a shell company to hold Ablyazov's shares in BTA pending a private placement with third party investors. Subsequently, on December 14, 2007, it purchased 808,321 shares in BTA from two BVI companies, representing 9.96% in BTA. The Claimant's position was that during January and February of 2009, the FSA<sup>2</sup> and the Kazakh Government adopted a series of measures aimed at removing control over BTA from its shareholders, which eventually culminated in the forced nationalization of the Bank.

The Claimant filed a Request for Arbitration on April 24, 2009 pursuant to Article 36 of the Washington Convention and the Treaty.

### ISSUE

ICSID Tribunal dealt with jurisdictional objections, whether the Claimant came within the definition of an '*Investor*' and whether its minority interest in BTA qualified as '*Investment*' under the Washington Convention as well as the Treaty.

### Contention by the Claimant

The Claimant contended that ICSID Tribunal had the jurisdiction to decide the case because the Claimant qualified under the definition of '*Investor*' provided under Article 1 (b) (ii)<sup>3</sup> of the Treaty as well as Article 25 (2) (b)<sup>4</sup> of the Washington Convention.

Further, Claimant argued that although Article 25 (1)<sup>5</sup> of the Washington Convention limits the disputes which can be referred to Washington Convention to those arising directly '*out of an Investment*', it does not define '*Investment*'.

However, the Treaty defines the term '*Investment*' in Article 1(1)<sup>6</sup> and hence the criteria in *Salini Construttori S.p.A. and Italstrade S.p.A. v. Kingdom of Morocco*, ["**Salini**"]<sup>7</sup> should not be applied as rigid jurisdictional preconditions.

### Contention by the Respondent

The Respondent argued that the Claimant cannot be considered an '*Investor*' if the Treaty and the Washington Convention are interpreted in accordance with Article 31 (1) of the Vienna Convention of Law of Treaties ["**VCLT**"], which requires an ICSID Tribunal to take into account the Treaty's object and purpose, and as such Claimant is a corporation of convenience, wholly owned and controlled by Ablyazov and therefore the Claimants real and effective nationality is Kazakh. Additionally, it was submitted that the Claimant had no connection

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with the Netherlands besides its place of incorporation.

Further, on the definition of '*Investment*' it was submitted that the Claimant was unable to satisfy the requirement of the Treaty and the Washington Convention. In particular, the Claimant's alleged '*Investment*' had a) no particular duration b) no anticipated regularity of profit and return c) the gratuitous transfer of shares did not amount to contribution d) Claimant never transferred ownership or control of the shares, nor intended to do so because it never had any control over the shares.

## DECISION

On the issue of Claimant being an '*Investor*', the ICSID Tribunal held that Claimant was an '*Investor*' within the terms of the Treaty and the Washington Convention, which provided that a legal entity constituted under the laws of the Contracting State was an '*Investor*', without the need for any further requirements. Accordingly, ICSID Tribunal rejected Respondent's argument that there were additional conditions (real and effective nationality) by relying on the ordinary meaning of Article 1 (b) (ii) of the Treaty, pursuant to Article 31 (1) of the VCLT which lays down the principle that a treaty must be interpreted in good faith and in accordance with its ordinary meaning in light of its object and purpose.

On the requirement of '*Investment*', the ICSID Tribunal found that there was no '*Investment*'. The ICSID Tribunal, after considering existing decisions, held that the objective definition of '*Investment*' under the Washington Convention and the Treaty comprised of three elements: **a)** a contribution or allocation of resources, **b)** duration, and **c)** risk which includes the expectation of a commercial return.

The ICSID Tribunal held that the transaction did not satisfy the criteria of an '*Investment*', in light of the fact that **1)** the Claimant made no contribution with respect to its alleged '*Investment*', nor was there any evidence on record that it had the intention or the ability to do so in the future because the shares were purchased on credit and financed through loans in respect of which no interest was paid, finally the loans were never repaid and eventually were written off; **2)** the Claimant itself never had funds of any significance, other than a small amount to pay administrative expenses; and the only purpose for the incorporation of the Claimant was to hold some of the shares in BTA; **3)** the duration<sup>8</sup> of the '*Investment*' was expected to be very short, as the business plan indicated that the shares would be held with the Claimant pending private placement with third party investors.

However, in line with recent ICSID cases,<sup>9</sup> the ICSID Tribunal rejected one element of an '*Investment*' set out in '*Salini*' that a contribution to the host State's development or prosperity was a requirement for an '*Investment*'. The ICSID Tribunal noted that while such a contribution may well be the consequence of a successful '*Investment*', if the '*Investment*' fails, and thus makes no contribution at all to the host State's economy, that cannot mean that there has been no '*Investment*'.

## ANALYSIS

The definition of '*Investment*' is significant to the protection that a foreign party can claim under a Bilateral Investment Treaty ['**BIT**']. This is a welcome decision by the ICSID Tribunal and provides clarity on the definition of '*Investor*' and '*Investment*' in investment arbitrations conducted under the Washington Convention. The ICSID Tribunal has clarified '*Salini*', appreciated the facts in proper perspective and reached a reasoned conclusion.

However, the tests discussed in this case would not be applicable to an investment arbitration involving India. India is not a party to Washington Convention and as such investment arbitrations arising out of India related BITs are conducted on an ad-hoc basis under UNCITRAL Rules or in accordance with any other institutional rules. In *White Industries*<sup>10</sup>, the Tribunal clarified that the dispute was not subject to Washington Convention and as such the disputes resolved under Washington Convention would not be applicable to investment arbitration involving India. Hence, the Tribunal in *White Industries* held that '*Salini*' test, which imposes a higher standard for defining '*Investment*' under the Washington Convention would not be applicable. In light of the above, only the plain and ordinary meaning of the definition of '*Investor*' and '*Investment*' in the relevant India related BIT will be construed in the event of a dispute concerning the jurisdiction of the Tribunal under India related BITs.

As India has signed several BITs with varying standards to qualify as an '*Investor*' and/or '*Investment*', signing the Washington Convention and becoming a member of ICSID could limit claims from such entities who under established international standards don't qualify as '*Investor*' and/or '*Investment*'.<sup>11</sup> This would help India secure sanctity of the investment arbitration regime and avoid misuse and burdensome claims.

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<sup>1</sup> ICSID Case No ARB/09/8

<sup>2</sup> Agency of the Republic of Kazakhstan on Regulation and Supervision of Financial Market and Financial Institutions

<sup>3</sup> "Article 1 (b) the term '*nationals*' shall comprise with regard to either Contracting Party: (ii) legal person constituted under the law of that Contracting Party;

<sup>4</sup> Article 25 (2) (b) "*Any juridical person which had the nationality of a Contracting State other than the State party to the dispute on the date on which the parties consented to submit such dispute to conciliation or arbitration and any juridical person which had the nationality of the Contracting State party to the dispute on that date and which, because of foreign control, the parties have agreed should be treated as a national of another Contracting State for the purposes of this Convention.*"

<sup>5</sup> Article 25 (1) "*The jurisdiction of the Centre shall extend to any legal dispute arising directly out of an investment, between a Contracting State (or any constituent subdivision or agency of a Contracting State designated to the Centre by that State) and a national of another Contracting State, which the parties to the dispute consent in writing to submit to the Centre. When the parties have given their consent, no party may withdraw its consent unilaterally.*"

<sup>6</sup> Article 1(1) of the Treaty defines '*Investment*' as follows:

"For the purposes of this Agreement:

(a) The term '*investment*' means every kind of assets and more particularly, though not exclusively

... (ii) rights derived from shares, bonds and other kinds of interests in companies and joint ventures; (iii) claims to money, to other assets or to any performance having an economic value; ..."

<sup>7</sup> ICSID Case No. ARB/00/4 (Decision on Jurisdiction, July 23, 2001)

<sup>8</sup> Neither the Washington Convention nor the Treaty specified the duration required for an allocation of resources to qualify as an '*Investment*'. During the elaboration of the Washington Convention, a period of five years was suggested and the matter was eventually left to the decision of the ICSID Tribunals. However, cases have held that projects with a minimum duration between two and five years satisfied the duration element.

<sup>9</sup> *Saba Fakes v. Republic of Turkey*, ICSID Case No. ARB/07/20, *Phoenix Action Ltd v. Czech Republic*, ICSID Case No. ARB/06/5

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