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THE APPLICATION OF DENIAL-OF-BENEFITS CLAUSES IN THE SETTLEMENT OF INTERNATIONAL ENERGY DISPUTES

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THE APPLICATION OF DENIAL-OF-BENEFITS CLAUSES IN THE SETTLEMENT OF INTERNATIONAL ENERGY DISPUTES

A Master's Thesis

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THE APPLICATION OF DENIAL-OF-BENEFITS CLAUSES IN THE SETTLEMENT OF INTERNATIONAL ENERGY DISPUTES

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ABSTRACT

THE APPLICATION OF DENIAL-OF-BENEFITS CLAUSES IN THE SETTLEMENT OF INTERNATIONAL ENERGY DISPUTES

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This thesis aims at an analysis of the interpretation and application of denial-of-benefits clauses in international investment arbitration, with a specific emphasis on energy investment disputes.

In such elaboration, it, first, covers the definition, purpose, scope, and boundaries of the denial of benefits in conceptual terms. Second, it examines the evolution of such clauses in terms of their components and types. Thereafter, whether the relevant rights are of jurisdictional or admissibility nature, the substantive and procedural requirements included in such clauses, whether the invocation of DOB rights has a prospective or retrospective effect, and the burden of proof regarding the fulfillment of denial-of-benefits requirements are addressed. At the end, considering the allegedly problematic application of the so-called denial-of-benefits clause in the Energy Charter Treaty, Article 17, the modernization process of the Energy Charter Treaty is examined.

Key Words: Denial of Benefits, Treaty Shopping, Mailbox Companies, Energy Charter Treaty, International Energy Disputes.

ÖZET

ULUSLARARASI ENERJİ UYUŞMAZLIKLARININ ÇÖZÜMÜNDE FAYDALARIN REDDİ KLOZLARININ TATBİKİ

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Bu tez, faydaların reddi klozlarının, enerji yatırım uyuşmazlıklarına özel vurgu ile birlikte uluslararası yatırım tahkimindeki yorum ve tatbik şeklini incelemeyi hedeflemektedir.

Bu çaba çerçevesinde, öncelikle, kavramsal bağlamda faydaların reddinin tanımı, maksadı, kapsamı ve sınırları konu edilmiştir. İkinci olarak, söz konusu klozların bileşenleri ve tipleri itibari ile geçirdiği evrim incelenmiştir. Sonrasında, bu klozların yargı yetkisine mi yoksa kabul edilebilirliğe mi ilişkin olduğu bağlamında niteliği, içerdikleri maddi ve şekli şartlar, icra edilmesinin geçmişe mi yoksa geleceğe mi etki doğuracağı konusu ve son olarak faydaların reddi şartlarının sağlandığına ilişkin ispat külfeti konuları üzerinde durulmuştur. En sonunda, Enerji Şartı Anlaşması kapsamında yer alan faydaların reddi niteliğindeki Madde 17 düzenlemesinin sebep olduğu sorunlu uygulama dikkate alınarak, Enerji Şartı Anlaşması ile ilgili olarak başlatılan modernizasyon süreci incelenmiştir.

Anahtar Kelimeler: Faydaların Reddi, Anlaşma Edinimi, Posta Kutusu Şirketler, Enerji Şartı Anlaşması, Uluslararası Enerji Uyuşmazlıkları.

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ABBREVIATIONS

Art.	Article
ASEAN	Association of Southeast Asian Nations
BIT	Bilateral Investment Treaty
CAFTA	Central America-Dominican Republic-United States Free Trade Agreement
CETA	Comprehensive Economic and Trade Agreement between Canada and the European Union
CUSMA	Agreement between the United States of America, the United Mexican States, and Canada
DOB	denial-of-benefits
e.g.	for example
ECT	Energy Charter Treaty
Ed. (pl. Eds.)	editor
et seq.	and the following
EU	European Union
FCN	Treaty of Friendship, Commerce and Navigation
Final Act	Final Act of the European Energy Charter Conference, Lisbon, 16-17 December 1994
FTA	Free Trade Agreement
i.e.	that is
ICJ	International Court of Justice

ICSID	International Centre for Settlement of Investment Disputes
ICSID Convention	Convention for the Settlement of Investment Disputes between States and Nationals of Other States
Ibid.	the same
IIA	international investment agreement
ILC	International Law Commission
ISDS	investor-state dispute settlement
MIA	multilateral investment agreement
NAFTA	North American Free Trade Agreement
fn.	footnote
No.	Number
OECD	Organisation for Economic Co-operation and Development
p.	page
pp.	pages
para.	paragraph
paras.	paragraphs
PCA	Permanent Court of Arbitration
PCIJ	Permanent Court of International Justice
pl.	plural
SCC	Arbitration Institute of the Stockholm Chamber of Commerce

UNCITRAL	United Nations Commission on International Trade Law
UNCTAD	United Nations Conference on Trade and Development
US	United States of America
v.	versus
VCLT	Vienna Convention on the Law of Treaties 1969
Vol.	Volume

INTRODUCTION

The balance strived to be struck between foreign investors and host states on the ground of international investment regime at the beginning of the 1950s was relatively simpler than today: it was principally based on the protection of the former against uncompensated nationalization and expropriation on the one hand, and the latter's desire for the foreign direct investment in their territories on the other. The first IIAs in the form of BITs were devised in such climate and with such expectations.[1]

One of the most revolutionary reforms introduced by the referred BIT-transformed international investment system has been the ISDS mechanism, whereby investors—in the capacity of private legal persons—gained the right of action against host states before arbitral authorities.[2] Although such BIT mechanism had resulted in mainly-neocolonialism-related hesitations on the side of developing countries, they commonly commenced engaging in the referred system following the 1980s' debt crisis to attract more and more foreign investment.[3] As a result, the number of BITs has increased to 2584 at present, which was lesser than 400 until the 1980s.[4] Also, the mentioned process resulting in the depoliticization of international investment system has been carried out by some groups of states in the way culminating with MIAs, such as NAFTA, CAFTA, the ECT, etc.

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[1] Behlman, J.: *Out on a Rim: Pacific Rim's Venture into CAFTA's Denial of Benefits Clause*, University of Miami Inter-American Law Review, Vol. 45, No. 2, 2014, p. 397.
[2] *Ibid.*, pp. 397-398.
[3] *Ibid.*, p. 398. For further details, see, Tiryakioğlu, B.: Doğrudan Yatırımların Uluslararası Hukukta Korunması, Ankara, 2003 (Doğrudan Yatırımlar), pp. 13-27; Köşgeroğlu Şit, B.: *Model İkili Yatırım Anlaşmaları ve Türkiye'nin Model İkili Yatırım Anlaşması Taslağı*, Türkiye Barolar Birliği Dergisi, 2013 (Model Anlaşmalar), pp. 144-148.
[4] Behlman, p. 398.

Among such MIAs, the ECT, signed in 1994 and entered into force in April 1998,[5] is submitted to be of the distinct significance primarily due to the strategic, geopolitical, and economic magnitude of its subject matter, the energy sector.[6] More, while the other MIAs are of regional nature, the ECT has a global reach as the most-widely-ratified IIA with fifty-four signatory parties at present.[7] It is also praised for succeeding in forging a compromise between the parties from Eastern Europe, who are with rich energy sources but in urgent need of foreign investment to regenerate their economies, and Western Europe, who are with such capital to invest abroad but in need of energy security and diversity in sources.[8]

As an inevitable corollary of the above-mentioned process, in which the number of BITs has remarkably increased and the access to MIAs has tremendously expanded, the acts of treaty shopping has emerged to be a concern for contracting parties to such treaties.[9] In this sense, treaty shopping comes about in such circumstances where a non-party national acquires the ownership and/or control of an investor of legal entity form that has no substantial business activities in its place of incorporation (i.e., the home state) and/or its investment with the sole purpose of accessing to IIA benefits that, naturally, includes the ISDS mechanism. Further, the

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[5] The Energy Charter Treaty, adopted on 17 December 1994, https://jusmundi.com/en/document/treaty/en-the-energy-charter-treaty-the-energy-charter-treaty-1994-saturday-17th-december-1994 (accessed on 22 August 2022).

[6] Cima, E.: *Investment Arbitration in the Energy Sector: Past, present, and future,* The Oxford Handbook of International Arbitration (Eds.: Schultz T. / Ortino F.), Oxford University Press, New York 2020, p. 823; Köşgeroğlu Şit, B.: Enerji Yatırım Sözleşmeleri ve Bunların Uluslararası Yatırım Anlaşmaları ile Korunması, Istanbul, 2012 (Enerji Yatırım Sözleşmeleri), p. 1.

[7] Roe, T. / Happold, M. / Dingemans QC, J.: Settlement of Investment Disputes under the Energy Charter Treaty (Law Practitioner Series). Cambridge: Cambridge University Press, 2011, p. 8; Energy Charter Secretariat: *Energy Charter Treaty: Signatories/Contracting Parties*, 18 February 2019, https://www.energycharter.org/process/energy-charter-treaty-1994/energy-charter-treaty/signatories-contracting-parties/ (accessed on 22 August 2022).

[8] Cima, p. 814.

[9] Behlman, p. 398; also see generally, Demirkol, B.: *Yatırım Tahkiminde Paravan Şirketlerin Yol Açtığı Yetki Sorunları,* Banka ve Ticaret Hukuku Dergisi, Vol. 28, No. 3, 2012, p. 304.

cases where such non-party is a state, with which the host state does not have normal economic and/or diplomatic relations, intensify the referred concerns. DOB clauses come into play at this juncture to thwart the mentioned conducts and deny treaty benefits to such investors and/or investments within the ownership and/or control of the described non-party nationals.[10]

In this context, this thesis aims at exploring, in the most general sense, the definition, scope, formulation, and application of DOB clauses in IIAs with a specific emphasis on energy disputes and the interpretation of the ECT DOB clause.

For such purpose, in Chapter 1, the characteristics and evolution of DOB clauses are analyzed. In this context, first, the definition, scope and purpose of these clauses are explained. Thereafter, taking the relevant notions into account, the boundaries of the DOB concept is touched upon by distinguishing it from similar mechanisms. Last, based on the conclusion arrived at as to the foregoing, the historical evolution of DOB formulations is attempted to be explored in BITs, MIAs and newly emerging IIAs.

In Chapter 2, the application of DOB clauses with relevant topical issues are analyzed mainly based on the interpretation of tribunals from both the ECT and non-ECT jurisprudences. In that Chapter, the following matters are addressed: whether the application of DOB provisions are of jurisdictional or admissibility-related nature; the substantive requirements included in DOB clauses; the procedural requirements for respondents (i.e., host states) to succeed in invoking DOB clauses effectively; the

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[10] See generally, Kaya, T.: *Ticaret Şirketleri Bakımından Tâbiiyet Planlaması ve Uluslararası Yatırım Hukuku Açısından Doğurduğu Sonuçlar,* Ankara Hacı Bayram Veli Üniversitesi Hukuk Fakültesi Dergisi, Vol. 25, No. 4, 2021, p. 65.

effects of the invocation of DOB clauses—i.e., if they have retrospective or prospective effect—and then the burden of proof issue.

While dealing with the referred matters, a specific emphasis is casted on the divergence between the ECT and non-ECT jurisprudences with regard to each topic. In this sense, at the end of Chapter 2, it is concluded that the ECT-jurisprudence approach to the interpretation of DOB clauses leads to the circumstances where the invocation of DOB clauses is almost impossible and impracticable. Therefore, in that Chapter, the recent developments in the ECT modernization aiming at resolving such complications are reported.

CHAPTER 1

THE CHARACTERISTICS AND EVOLUTION

OF

DENIAL-OF-BENEFITS CLAUSES

I. Characteristics of DOB Clauses

A. Definition and Purpose of DOB Clauses

The definition of DOB clauses,[11] as a challenging endeavor, could only be possible based on the function they perform.[12] In the most general terms and considering the explanations given place in the following parts, they could functionally be defined as the provisions providing the parties to an IIA with the right to deny the benefits and advantages of such IIA to the group of legal entities that are defined, described, and included in such clauses. The referred group of legal entities could mainly be defined depending on, *inter alia*, their economic connection with their home state (i.e., the state of incorporation); and/or the diplomatic relations between the host state and the state, whose nationals own or control the entity.

The said categories of legal entities also draw the scope of DOB clauses: the benefits of an IIA are denied by states in two major categories of circumstances: (1) when the putative investor does not have any substantial business activities in the home state and is under the ownership or control of a third-state national, and/or (2) when it is owned or controlled by the nationals a third-state, with whom the denying party does

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[11] At this juncture, first of all, it must be noted that no such direct and perfectly framed definition could be found in the literature. Authors seem to provide descriptions based on DOB clauses' functions, rather than definitions on the basis of such clauses' nature, text, and context.

[12] See, e.g., Dolzer, R. / Schreuer, C.: Principles of International Investment Law, Second Edition, Oxford, 2017, p. 55; Mistelis, L.A. / Baltag, C.M.: *Denial of Benefits and Article 17 of the Energy Charter Treaty*, Penn State Law Review, Vol. 113, No. 4, 2009 (Energy Charter Treaty), p. 1302.

not have normal economic or diplomatic relations; yet, the second category emerges in practice less frequently.[13]

To comprehend the *raison d'être* of such provisions, the following historical remark would merit a mention at this point: in his article "*Provisions on Companies in United States Commercial Treaties,*" Herman Walker, Jr., indicated that the US had always been hesitated to include foreign corporations in its international commercial treaties. This was essentially because it had had the concern that such inclusion could and would be benefited from the third-party states by their nationals' utilization of corporations as an indirect way to gain treaty advantages without any reciprocal undertakings.[14] According to the author, following the inclusion of corporations in its IIAs, the US, with the above-referred concerns, started to include reservations to the piercing-the-corporate-veil effect, which addressed the circumstances where the ownership or control of the corporations were held by third-state nationals.[15]

In line with the foregoing, and considering the enormous increase in the number of IIAs in the second half of the last century[16] and ISDS proceedings in the last three decades,[17] such concerns regarding the potential exploitation of IIAs via free-

[13] Baltag (Denial of Benefits), p. 5.

[14] In Walker's words describing the referred concern: "*a fear lest such commitment could become a cloak under cover of which rights would be gained by interests of third countries-in a situation in which the party to the treaty would not wish to be obligated to accord them, whether because such third countries were not party to the reciprocal arrangements embodied in the treaty or for other reason.*" For further details, see, Walker, Jr., H.: *Provisions on Companies in United States Commercial Treaties*, The American Journal of Law, Vol. 50, No. 2, 1956, p. 388.

[15] *Ibid*.

[16] Behlman, p. 398.

[17] For example, see, Kang, P.: *The Relationship between the Investor-State Dispute Settlement and the Denial of Benefits with Specific Reference to the Energy Charter Treaty*, Asian Business Lawyer, Vol. 19, No. 15, 2017, p. 16, where the author states: *"During the first 30 years since the ratification of the Convention on the Settlement of Investment Disputes between States and Nationals of Other States…, where member states agreed to establish the ICSID, there were only 26 cases submitted for arbitration. There was a considerable increase in the number of arbitration cases over the following 20 years, with 438 cases being referred from 1996 to 2015."*

riding by third-state nationals started to be voiced by different states as well;[18] and the referred US reservations blossomed into DOB provisions in IIAs in the course of time to satisfy such concerns. Therefore, in this sense, two major and interrelated purposes are submitted in relation to the purpose of DOB clauses: the provision of reciprocity and the prevention of treaty abuses.

1. The Provision of Reciprocity

Notwithstanding the substantial number of IIAs that have been concluded up to the present, there still may be a number of states not signing BITs with each other or not entering into to the same MIAs, which could result from the tenuous relations of such states or any other practical reason. In the case the nationals of a third state, with whom the denying state has not entered into an IIA or does not have normal diplomatic relations, are permitted to benefit from the IIA entered into by the denying state with another state by the way of acquiring the nationality of the latter, such permission could cause the denying host state to lose the opportunity to negotiate the legal instruments with reciprocal privileges and obligations with such third states. Therefore, the principal purpose ascribed to DOB clauses is mainly concerning the reciprocity of the privileges and obligations provided in IIAs:[19] DOB provisions are considered to be an IIA component aiming at providing such balance of treaty rights and obligations.[20]

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[18] Walker, pp. 373, 388, as cited in, Behlman, p. 398.

[19] Kang, p. 24; Gastrell, L. / Le Cannu, P.: *Procedural Requirements of 'Denial-of-Benefits' Clauses in Investment Treaties: A Review of Arbitral Decisions*, ICSID Review, Vol. 30, No. 1, 2015, p. 81.

[20] Baltag, C.: *Denial of Benefits of Investment Treaties: A Step Further?*, Romanian Arbitration Journal / Revista Romana de Arbitraj, Vol. 9, No. 2, 2015 (Denial of Benefits), p.1; Kang, pp. 24, 26.

2. The Prevention of Treaty Abuses

In addition to the reciprocity-related objective, DOB clauses are considered to be as a type of abuse-preclusion mechanism: there is a clear consensus in the literature that one of the principal purposes of DOB clauses is the prevention of IIA abuses carried out for benefiting from IIA protections in the way not foreseen and aimed therein.[21]

In ISDS proceedings, the natural reaction of host states in the respondent position is to endeavor to preclude the abuse, if not the use,[22] of the ISDS benefits provided by relevant IIAs.[23] For such purpose, there are two potentially functioning methods adopted by host states: excluding claimants from the investor category of the relevant IIA or exercise its rights, if any, to deny the IIA benefits to putative investors.[24] At this point, DOB provisions come into play to realize the latter method,[25] by confining the benefits provided by IIAs to the *bona fide* investor.[26] In other words, by means of such clauses, it is aimed at preventing the investors owned or controlled by third-state nationals and with no substantial business activities in the home state from benefiting from the investment protection mechanisms, either substantive or

[21] *Ibid*. Also, for a detailed analysis on the conditions of such abuse, *see*, Kang, pp. 29-32.
[22] As for the ICSID ISDS mechanism, Bolivia, in 2007, Ecuador, in 2009, and Venezuela, in 2012, withdrew from the ICSID Convention for various reasons. Also, there have been numerous BIT denunciations by some other states, such as the Republic of South Africa. Such withdrawals and denunciations are considered to be reflecting the negative attitude that has been adopted states toward the ISDS mechanisms. Other ways potentially followed for such purposes may be not including the ISDS mechanisms in IIAs and implementing, in lieu of that, ISA mechanisms therein and/or limiting the subject-matter of ISDS mechanisms. For further details regarding such developments and their causes, *see,* Kang, pp. 20-23.
[23] Kang, p. 17.
[24] *Ibid*.
[25] *Ibid*., p. 23.
[26] Ramachanderan, R.: *Enabling Retrospective Application of The Denial of Benefits Clause: An Analysis of Decisions of Tribunals Under the Energy Charter Treaty*. University of Miami International and Comparative Law Review, Vol. 26, No. 1, 2018, p. 212; see also generally, Sornarajah, M.: *Good Faith, Corporate Nationality, and Denial of* Benefits, Good Faith and International Economic Law (Eds.: Mitchell, A.D. / Sornarajah, M. / Voon, T.), Oxford University Press, 2015 (Good Faith), pp. 119.

procedural, and it's function is considered to serve the "*counteract strategies*" against such investors acquiring the home state nationality with the sole purpose of benefiting from referred IIA protections.[27] In this sense, DOB clauses function to exclude the group of investors and their investments from the ambit of IIA protection in the cases where such investors' economic presence in the state of their incorporation does not meet the "*substantial business activity*" or "*real economic connection*" threshold.[28]

The concept of "treaty shopping" emerges at this point to cover the above-referred circumstances, which merits a mention to have a more comprehensive grasp of the purpose of DOB clauses. The objective of DOB clauses in this sense is understood to be the alleviation of treaty-shopping practices.[29]

In the literature and arbitral decisions, there are several terms utilized to mean or imply the concept of "treaty shopping," such as "nationality of convenience,"[30] "nationality shopping," and "protection shopping,"[31] etc. Although the cited terms are indicated not to be newly emerging in the field,[32] treaty shopping and others are destitute of any universally accepted definitions. To the investment treaties area, it is

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[27] Dolzer / Schreuer, p. 55.
[28] Dolzer / Schreuer, p. 55; Behlman, p. 398; Mistelis, L. A. / Baltag, C.: *'Denial of Benefits' Clause in Investment Treaty Arbitration*. Queen Mary School of Law Legal Studies Research Paper No. 293/2018, Available at SSRN: https://ssrn.com/abstract=3300618A2 (accessed on 22 August 2022) (Investment Treaty Arbitration), p. 12; Kang, p. 30; Salacuse, J.W.: *BIT by BIT: The Growth of Bilateral Investment Treaties and Their Impact on Foreign Investment in Developing Countries*, The International Lawyer, Vol. 24, 1990, p. 665.
[29] Mistelis / Baltag (Investment Treaty Arbitration), p. 38; Sornarajah, M.: The International Law on Foreign Investment, Third Edition, Cambridge University Press, 2010 (Foreign Investment), p. 327.
[30] See, e.g., *Limited Liability Company Amto v. Ukraine*, SCC Case No. 080/2005, Final Award, 26 March 2008, para. 69, https://jusmundi.com/en/document/decision/en-limited-liability-company-amto-v-ukraine-final-award-wednesday-26th-march-2008 (accessed on 22 August 2022) (*AMTO v. Ukraine*).
[31] See, e.g., *Waste Management v. United Mexican States (II)*, ICSID Case No. ARB(AF)/00/3, Award, 30 April 2004, para. 80, https://jusmundi.com/en/document/decision/en-waste-management-v-united-mexican-states-ii-award-friday-30th-april-2004 (accessed on 22 August 2022) (*Waste Management*).
[32] Côté, C.E.: *Piercing the Corporate Veil in International Investment Law: Problems with the Denial of Benefits Clause*, The Corporation in International Law and Governance. Perspectives on Globalized Rule of Law (Ed.: Fitzgerald, O.). Available at SSRN: https://ssrn.com/abstract=3523769 or http://dx.doi.org/10.2139/ssrn.3523769 (accessed on 22 August 2022), p. 1.

imported from the tax field, where it means the establishment of corporate entities in tax havens with the sole purpose of benefiting from more advantageous tax treaties.[33] In the field of investment treaties and investment arbitration, the concept is described as the acquaintance of a nationality of convenience to evade taxation, avoid regulative measures, and/or to benefit from more advantageous treaty provisions.[34] To be more precise, in the investment field, such concept refers to the circumstances where any non-party-state entity, i.e., a free-rider,[35] possesses the ownership or control of an enterprise (that does not have any substantial business activities in the country of its constitution or organization) with the sole purposes of benefiting from IIA protection.[36] In line of the foregoing, in his book "Treaty Shopping in International Investment Law," Jorun Baumgartner describes the concept in the following way:

> "*Treaty shopping should thus be understood to include all legal operations aimed at invoking or creating a qualifying nationality and/ or a qualifying investment, for example by structuring or restructuring an investment or by otherwise conferring an entitlement or property right to an investment, with a view to benefitting from a particular international investment agreement granting an investor direct standing (ius standi).*"[37] [Emphasis added, the underlined emphasis provided in the original text in italics].

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[33] Baumgartner, J.: Treaty Shopping in International Investment Law, Oxford University Press, Oxford, 2016, p. 7.
[34] Behlman, p. 399; Kang, p. 32, fn. 62.
[35] Badini, A.A.: *Denial of Benefits - Practical Lessons for States and Investors from the Pac Rim Arbitration*, Yearbook on International Arbitration Vol. 3, 2013, p. 294.
[36] *Waste Management*, Para. 80.
[37] Baumgartner, p. 12. Also, for the sake of delineation of treaty shopping, the concept of "forum shopping" must be distinguished. Although they are related practices, the latter concerns the choice of the most advantageous *forum* among the *fora* the party to a dispute may choose. Forum shopping, insofar as it does not result in multiple proceedings, is considered to be an unproblematic concept. For

As regards the foregoing explanations, for the avoidance of any doubt, it should be noted that while the acquaintance of a nationality with profit-maximization purposes is deemed legally acceptable;[38] only the treaty-shopping practice with the sole purpose of benefiting from ISDS mechanisms is considered to be jeopardizing the stability in the global investment regime aimed at by IIAs and condemned.[39]

At this point, the above-given explanations require a closer analysis of "mailbox/shell/sham companies/corporations"[40] as the facilitating mechanism for treaty-shopping purposes. Such entities, in short, are considered to be special purpose vehicles without any genuine nexus to party states to IIAs other than being incorporated in the home state.[41] The referred terms seem to be used in a way to imply the same concept in the literature and arbitral decisions; therefore, the concept of "mailbox company" is preferred in this thesis to refer to all of them.

The mailbox-company concept, just like treaty shopping, is destitute of a commonly accepted definition. This is why it is submitted that the concept could be approached based on the following elementary components: the lack of any substantial business activities in the state of incorporation and the ownership or control by third- or host-state nationals,[42] which are also the fundamental requirements of DOB clauses.

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further details on the difference between treaty shopping and forum shopping, see, Baumgartner, pp. 15-19. For further analysis on *shopping for jurisdiction* and its relevance to DOB provisions, see, Sornarajah (Foreign Investment), pp. 327-329.

[38] Pinto, D.C.: *Is the retrospective exercise of the 'denial of benefits' clause contrary to the investor's legitimate expectations under the Energy Charter Treaty?* Maastricht University Working Paper (March 2016), DOI: 10.13140/RG.2.1.1164.2481 (accessed on 22 August 2022), p. 3.

[39] Kang, p. 30, fn. 52. Also, in relation to the foregoing, it is observed that: *"If a country's people can enjoy the benefits of an investment treaty concluded by other countries, it will not need to enter into an investment treaty to protect its own people. Conversely, as a host state, if it is easy to bear the liabilities of an investment treaty for a foreign investor who is from a third party to the investment treaty, the existing investment treaty parties may end the investment treaty."*: Kang, p. 33. *See also,* Kaya, p. 64.

[40] Badini, p. 294.

[41] Ramachanderan, p. 227.

[42] Baumgartner, p. 108.

Therefore, it is patently obvious that DOB clauses' essential objective is directly related to the mailbox-company practices as well.

In this sense, in *Waste Management*, the tribunal referred to such mailbox companies as "*simply an intermediary for interests substantially foreign,*" and stated that the relevant NAFTA DOB clause (i.e., Art. 1113(2)) aimed at withdrawing the treaty protections from them.[43] Also, in *Ampal v. Egypt*, the tribunal provided the following description for the mailbox-company concept while analyzing the objectives of DOB clauses:

> "***Denial-of-benefits clauses*** *in investment treaties are* ***generally designed to exclude from Treaty protections nationals of third States*** *which claim rights through so-called* ***"mailbox"*** *or* ***"shell" companies*** *that* ***have no economic connection to the state whose nationality is invoked****.*"[44] [Emphasis added].

Last, with regard to the purposes of DOB clauses, it must be noted that such clauses do not target only third-state nationals, but also host-state nationals when the formulation to such effect is explicitly inserted in the provision. To be more precise, in a number of IIAs, the host-state nationals owning or controlling a home-state investor or investment are also included in such denied category of investors since their main objective is considered to be benefiting from IIA advantages and avoiding the domestic courts' jurisdiction. Such activities carried out by host-state nationals are

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[43] *Waste Management*, para. 80.

[44] *Ampal-American Israel Corp., EGI-Fund (08-10) Investors LLC, EGI-Series Investments LLC, BSS-EMG Investors LLC and David Fischer v. Arab Republic of Egypt*, ICSID Case No. ARB/12/11, Decision on Jurisdiction, 1 February 2016, para. 125, https://jusmundi.com/en/document/decision/en-ampal-american-israel-corp-egi-fund-08-10-investors-llc-egi-series-investments-llc-bss-emg-investors-llc-and-david-fischer-v-arab-republic-of-egypt-decision-on-jurisdiction-monday-1st-february-2016 (accessed on 5 August 2022) (*Ampal v. Egypt*).

called "round-tripping," for which establishing mailbox companies is a preferred facilitating mechanism."[45]

B. Boundaries of DOB: Distinguishing DOB Clauses from Similar Mechanisms

When it comes to the boundaries of the DOB concept, to have a comprehensive grasp, one may find it necessary to make a comparison of DOB provisions with the notions most juxtaposed to it in an alternative way, namely, the abuse-of-rights doctrine, piercing the corporate veil, and the IIA provisions defining the covered investor.

1. Abuse-of-Rights Doctrine

Regarding the abuse-of-rights doctrine, it is put forth in the literature that the DOB notion and the doctrine are based on similar motives and aim at identical results.[46] However, when it comes to the invocation of only one of them, it is submitted that DOB clauses should be preferred over the other; this is because of the former's being a part of treaty text and the explicit reflection of the parties' mutual understanding on such circumstances where the benefits provided by the IIA may be denied. As a consequence of not being included within the treaty text, the invocation of the abuse-of-rights doctrine is deemed to result in open-ended and speculative

[45] Côté, p. 3. For further details on the definition of round-tripping and mailbox-company concepts, see, Baumgartner, p. 102 *et seq.*; Demirkol, p. 312.
[46] See, e.g., Mistelis / Baltag (Investment Treaty Arbitration), p. 3. Also, for a detailed analysis on the application of the abuse-of-rights doctrine to prevent treaty shopping, see, Kaya, pp. 85-90; Demirkol, pp. 323-325.

theories developed by claimants and unforeseeable applications by arbitral tribunals, which could cause instability and uncertainty in the ISDS mechanisms of IIAs.[47]

Mark Feldman, comparing DOB rights with the abuse-of-rights doctrine, stated that the predictability concerning the measures taken against treaty shopping was a legal imperative for the sake of stability in ISDS mechanisms. In this sense, according to him, the abuse-of-rights doctrine seems not to serve this purpose, while the inclusion of DOB clauses in IIAs provides investors with a foreseeable and accessible roadmap to follow for falling within the category benefiting from IIA benefits.[48]

2. Piercing the Corporate Veil

Another concept, which is frequently referred to alongside the DOB concept, is piercing the corporate veil. It is submitted that DOB rights in IIAs aim at the facilitation of piercing the corporate veil with the purpose of excluding shell companies from the benefits of such IIAs.[49] As regards the scope of such notions, piercing the corporate veil appears to be an objective itself, for which DOB provisions, with other mechanisms and procedures, may be used as a vehicle to restrict the treaty protection.[50]

3. Investor Definitions and Nationality Requirements in IIAs

The last notion that must be addressed here is the investor definitions under IIAs. The investor definitions are designed and included to determine the natural and

[47] Feldman, M.: *Setting Limits on Corporate Nationality Planning in Investment Treaty Arbitration*, ICSID Review, Vol. 27, No. 2, 2012, pp. 283, 302.
[48] *Ibid.*, p. 302.
[49] Côté, p.1.
[50] Mudliar, A.: *Article 17: Non-application of Part III in certain circumstances*, Commentary on the Energy Charter Treaty (Ed.: Leal-Arcas, R.), Edward Elgar Publishing, Cheltenham, 2018, p. 249.

legal persons covered by IIAs,[51] which naturally entails benefiting from the protections provided therein. By some authors and tribunals, the function of DOB clauses is considered to be similar to that of the restrictions imposed investor definitions in IIAs, while others put forth that the implications of such notions are significantly different than each other.[52]

First, and most importantly, the restrictions on the investor definition would affect only the *ratione personae* jurisdiction; while DOB clauses, based on its interpretation, may affect either the jurisdiction or merits aspect of a dispute, as examined in the following Chapter. Also, in most IIAs, it is foreseen that the rights included in the DOB clause should be actively exercised by the host state as the respondent in order for it to be able to invoke such denial, and practically it cannot be considered by the tribunal *ex officio*.[53] However, on the other hand, giving place to DOB requirements in the investor definition as a factor determining the *ratione personae* jurisdiction would result in the automatic application of investor exclusion.[54]

As regards the referred concepts' differences in practice, under the IIAs without DOB clauses, arbitral tribunals are mostly reluctant to scrutinize the ownership

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[51] Feldman, p. 283.

[52] See, e.g., Mistelis / Baltag (Investment Treaty Arbitration), p.2. Also, with reference to Article 17(1) of the ECT, it is argued that the DOB provision should have been considered as an aspect of nationality requirements in the way regulating the genuineness of the nationality link, as under Article 9 of the Draft Articles on Diplomatic Protection (*see, infra* fn. 241). However, on the other hand, this view was rejected by others submitting that the referred Article was not a nationality provision, which was explicitly set forth under Article 1(7)(a)(ii) of the ECT. See, e.g., Mistelis / Baltag (Energy Charter Treaty), p. 1318.

[53] Mistelis / Baltag (Investment Treaty Arbitration), pp. 2, 38.

[54] For the views that such exceptions could have been given in investor definitions had the contracting parties wished for an automatic application, see, *Khan Resources Inc., Khan Resources B.V. and Cauc Holding Company Ltd. v. the Government of Mongolia and Monatom Co., Ltd.*, PCA Case No. 2011-09, Decision on Jurisdiction, 25 July 2012, para. 420, https://jusmundi.com/en/document/decision/en-khan-resources-inc-khan-resources-b-v-and-cauc-holding-company-ltd-v-the-government-of-mongolia-and-monatom-co-ltd-decision-on-jurisdiction-wednesday-25th-july-2012 (accessed on 22 August 2022) (*Khan Resources*).

and/or control structure and the economic activities of investors,[55] unless such requirements are explicitly included in the investor definition.[56] This is because, such tribunals, applying Article 31 of the VCLT to the treaty in question find that the plain language must primarily be taken into consideration as a basis of interpretation.[57] In addition to the employment of such literal interpretation, the referred tribunals also find that the lack of DOB clause in an IIA should be considered as a conscious preference of the party states and be evaluated in the way that the parties deliberately do not place economic activity, ownership, and/or control-related restrictions on the category of investors otherwise falling within the investor definition.[58] Tribunals avoid such practice of reading an extra provision into a treaty on the basis of the *pacta sunt*

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[55] Mistelis / Baltag (Investment Treaty Arbitration), p. 3.

[56] In some circumstances, having substantial business activities in the home state is given place as a condition under investor definition. See, e.g., Kang, p. 33. It is also submitted that in the absence of DOB provisions, investors may benefit from the advantages of an IIA via direct access (i.e., being a genuine investor from the home state) or MFN clauses. Therefore, according to the authors of such opinion, DOB provisions also aim at the restriction of the implications of MFN clauses potentially paving the way for treaty shopping. For further details on such argumentation, see, Behlman, pp. 399, 423.

[57] *Yukos Universal Limited (Isle of Man) v. The Russian Federation*, PCA Case No. 2005-04/AA227, Interim Award on Jurisdiction and Admissibility, 30 November 2009, para. 411. *https://jusmundi.com/en/document/decision/en-yukos-universal-limited-isle-of-man-v-the-russian-federation-interim-award-on-jurisdiction-and-admissibility-monday-30th-november-2009* (accessed on 15 August 2022) (*Yukos* cases). Also, for the text of the VCLT, see, Vienna Convention on the Law of Treaties, adopted on 23 May 1969, https://legal.un.org/ilc/texts/instruments/english/conventions/1_1_1969.pdf (accessed on 22 August 2022)

[58] See, e.g., "*These investment agreements confirm that state parties are capable of excluding from the scope of the agreement entities of the other party that are controlled by nationals of third countries or by nationals of the host country.* ***The Ukraine-Lithuania BIT, by contrast, includes no such "denial of benefits" provision with respect to entities controlled by third-country nationals or by nationals of the denying party. We regard the absence of such a provision as a deliberate choice*** *of the Contracting Parties. In our view,* ***it is not for tribunals to impose limits on the scope of BITs not found in the text,*** *much less limits nowhere evident from the negotiating history. An international tribunal of defined jurisdiction* ***should not reach out to exercise a jurisdiction beyond the borders of the definition****. But equally an international tribunal should exercise, and indeed is bound to exercise, the measure of jurisdiction with which it is endowed.*" [Emphasis added]. *Tokios Tokelés v. Ukraine*, ICSID Case No. ARB/02/18, Decision on Jurisdiction, 29 April 2004, para. 36, https://jusmundi.com/en/document/decision/en-tokios-tokeles-v-ukraine-decision-on-jurisdiction-thursday-29th-april-2004 (accessed on 10 August 2022) (*Tokios Tokelés*).

servanda, as an essential principle prevailing in the field of international investment law.[59]

For example, in the *Yukos* cases,[60] although the applicable treaty was the ECT that included a DOB provision under its Article 17, the tribunal needed to address if the "*claimant qualified as a protected "investor"*" under the investor definition of the ECT, Article 1(7), separately. The tribunal found that the investor definition provision did not include any requirement apart from being duly organized under the home state's applicable laws.[61] Besides, the tribunal assessed that the corporate structure of the claimant was not of irrelevance and would be taken into consideration in relation to Article 17 including the pertinent requirements.[62] Therefore, it is inferred from the tribunal's reasoning that even in the disputes the IIAs with DOB clauses are involved, tribunals would be very inclined not to read additional corporate structure- and economic activity-related requirements into the investor definitions, and they consider such notions solely within the scope of such DOB clauses. In the way affirming the foregoing inference, the tribunal pointed out that there were not any "*general principles of international law*" requiring a further inquiry into the operation of legal

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[59] Ramachanderan, p. 212.

[60] By *Yukos* cases, in this thesis, the following case is referred: *Yukos Universal Limited (Isle of Man) v. The Russian Federation*, PCA Case No. 2005-04/AA227, Interim Award on Jurisdiction and Admissibility, 30 November 2009, https://jusmundi.com/en/document/decision/en-yukos-universal-limited-isle-of-man-v-the-russian-federation-interim-award-on-jurisdiction-and-admissibility-monday-30th-november-2009 (accessed on 15 August 2022), the reasoning of which is identical to the following cases: *Hulley Enterprises Ltd. v. Russian Federation*, PCA Case No. 2005-03/AA226, Interim Award on Jurisdiction and Admissibility, 30 November 2009, https://jusmundi.com/en/document/decision/en-hulley-enterprises-ltd-v-russian-federation-interim-award-on-jurisdiction-and-admissibility-monday-30th-november-2009 (accessed on 15 August 2022); *Veteran Petroleum Limited v. The Russian Federation*, PCA Case No. 2005-05/AA228, Interim Award on Jurisdiction and Admissibility, 30 November 2009, https://jusmundi.com/en/document/decision/en-veteran-petroleum-limited-v-the-russian-federation-interim-award-on-jurisdiction-and-admissibility-monday-30th-november-2009 (accessed on 15 August 2022). The same preference takes place in other sources of literature as well, for example, see, Baltag (Denial of Benefits), p. 3, fn. 10.

[61] *Yukos* cases, para. 411

[62] *Yukos* cases, para. 412

entities when the subject-matter treaty requires only the incorporation and organization in compliance with the home state laws in its investor definition. Also, added by the tribunal, the principles prevailing in international law barred arbitral tribunals from reading such additional criteria into treaty text—regardless of to what extent those are deemed to be proper and desirable by them.[63]

In *Saluka v. Czech Republic*, under the Agreement on Encouragement and Reciprocal Protection of Investment between the Netherlands and the Czech and Slovak Federal Republic adopted on 29 April 1991,[64] the tribunal reasoned in the same vein as the foregoing. In this sense, the tribunal acknowledged that it had a sympathy for the respondent's contention that a company in the form of shell company—which is without any genuine links to the home state and controlled by a third-state company—would not be endowed with the IIA protections.[65] It also determined that such practices could result in the abuse of dispute settlement mechanisms, in addition to treaty shopping practices. However, despite such sympathy and assessment concerning the potential abuses, the tribunal held that the determining factor, on which the tribunal's functions and conducts must have been dependent, was the terms agreed

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[63] *Yukos* cases, para. 415. Also, the referred paragraph ends with a reference to an Advisory Opinion issued by PCIJ concerning the "Acquisition of Polish Nationality," which states: "*To impose an additional condition for the acquisition of Polish nationality, a condition not provided for in the Treaty of June 28th, 1919, would be equivalent; not to interpreting the Treaty, but to reconstructing it.*" *Acquisition of Polish Nationality*, PCIJ Series B. No 7, Advisory Opinion, 15 September 1923, page. 20.

[64] The complete name of the referred Treaty is Agreement on Encouragement and Reciprocal Protection of Investments Between the Kingdom of The Netherlands and the Czech and Slovak Federal Republic, signed on 29 April 1991. For the full text of the Treaty, please see. https://jusmundi.com/en/document/treaty/en-agreement-on-encouragement-and-reciprocal-protection-of-investments-between-the-kingdom-of-the-netherlands-and-the-czech-and-slovak-federal-republic-czech-and-slovak-republic-netherlands-bit-1991-monday-29th-april-1991#art_1441 (accessed on 22 August 2022).

[65] *Saluka Investments BV v. The Czech Republic*, PCA Case No. 2001-04, Partial Award, 17 March 2006, para. 240, https://jusmundi.com/en/document/decision/en-saluka-investments-bv-v-the-czech-republic-partial-award-friday-17th-march-2006 (accessed on 22 August 2022) (*Saluka v. Czech Republic*).

by the parties, which naturally included, *inter alia*, the provisions defining who may be qualified as an investor; that is, the potential claimant. It is added by the tribunal that it did not have the authority to amend such provisions agreed by the parties; therefore, the tribunal rejected to impose any additional requirement that had not been foreseen under the relevant treaty provision that solely brought about the requirement of duly constitution under home-state applicable law.[66]

The same line of reasoning was followed by the tribunal in *Garanti Koza v. Turkmenistan*, where the applicable BIT did not include a DOB clause, and the incorporation in the UK was the only requirement in its investment definition. Therefore, the tribunal rejected to read additional conditions into the nationality requirements of the BIT holding that the respondent, Turkmenistan, was conscious of dealing with a company eligible to the treaty protection.[67]

At this point, the determination of nationality, as a concept closely connected to the delineation of the investor status under IIAs, assumes utmost importance:[68] only the putative investors holding the home-state nationality in terms of the relevant IIA may benefit from the advantages provided by such IIA. In this sense, the nationality of natural persons requires a relatively straightforward analysis that is generally based on the applicable laws of the state, the nationality of which is claimed.[69] On the other hand, there is not a uniform implementation and interpretation with regard to the

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[66] *Saluka v. Czech Republic*, para. 241.
[67] *Garanti Koza LLP v. Turkmenistan*, ICSID Case No. ARB/11/20, Award, 19 December 2016, para. 222, https://jusmundi.com/en/document/decision/en-garanti-koza-llp-v-turkmenistan-award-monday-19th-december-2016 (accessed on 22 August 2022) (*Garanti Koza*).
[68] Legum, B.: *Defining Investment and Investor: Who is Entitled to Claim?*, Arbitration International, Vol. 22, No. 4, 2006, p. 524.
[69] For further information on the determination of natural persons' nationality, see, Yannaca-Small, K.: *WHO IS ENTITLED TO CLAIM?: The Definition of Nationality in Investment Arbitration*, Arbitration Under International Investment Agreements: A Guide to the Key Issues (Ed.: Yannaca-Small, K.), Second Edition, Oxford University Press, Oxford, 2018, pp. 224-230.

determination of corporate nationality. For such analysis, the state of incorporation, the state of administration, and/or the nationality of the controlling shareholders are utilized, either in an alternative or cumulative way.[70]

The first—the state of incorporation—is ascertained based on the place where the subject-matter entity is incorporated or organized in accordance with the applicable laws, and the method adopting it as the basis for corporate nationality is generally applied and preferred by common law countries.[71] Such method, although facilitating the determination of corporate nationality, is very likely to enable treaty shopping practices[72] by entitling the entities only with "*a nominal connection to their home [s]tate*" to benefit from treaty protections.[73] Therefore, DOB provisions' main objective seems to be the alleviation of the potential inconveniences resulting from this method.[74]

The second method—dependent on the place of administration—is the one usually preferred by civil law countries.[75] With reference to the same phenomenon, several terms are in use in IIAs: the place or country of head office, business, *siège social*, main headquarters, and/or effective management, etc.[76]

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[70] Kang, p. 27. Also, for a general view on the determination of nationality in international investment law, see generally, Kaya, pp. 72-78; Sinclair, A.C.,: *ICSID's Nationality Requirements*, ICSID Review – Foreign Investment Law Journal, Vol. 23, No. 1, 2008, pp. 57-118.
[71] *Ibid*.
[72] Kang, P., pp. 27-28; Kaya, p. 64.
[73] Feldman, p. 284; Kaya, p. 63.
[74] Feldman, p. 282. To obviate such complications, which emerges also in the sphere of international public law, the DOB requirements was adopted by the Draft Articles on Diplomatic Protection to ascertain the state of nationality considering the substantial business activities and control components of legal entities for the purposes of diplomatic protection. *See,* Mistelis / Baltag (Energy Charter Treaty), p. 1309. In other words, the state of incorporation is rejected to have diplomatic protection rights regarding a corporation which is controlled by third-state nationals, does not have any substantial business activity in the state on incorporation, "*and*," the corporation does not have the seat of management of financial control in the state of incorporation.
[75] Kang, p. 28.
[76] *Ibid.*; Salacuse, p. 666; Feldman, p. 283.

The last method, which centers on the nationality of controlling shareholders, focuses on the natural or legal persons actually possessing the control of the relevant investor or investment.[77] Due to the prevailing multi-layer corporate structures in international investments, reaching solid consequences via such method may require cumbersome analyses.[78] As the corollary of such structures, further, adopting this method in IIAs could result in parallel arbitral proceedings initiated by different shareholders, i.e., investors, of the same investment.[79]Also, it hereby should be noted that the rationale behind the introduction of such control test into the provisions with nationality-related items, e.g., investor or investment definitions, is argued to be extending the IIA protections to those holding the control of and/or substantial interests in the relevant legal-entity investors or investments.[80]

In brief, the IIAs employing any of the above-explained nationality-determining methods require the following, either in an alternative or cumulative way, for a legal entity to be considered as an investor benefiting from treaty protections: (1) to have the place of incorporation in the home state; (2) to have the place of administration in the home state; or (3) directly or indirectly owned or controlled by home-state nationals.[81] Among them do the second and third methods provide the host

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[77] Kang, p. 28.
[78] *Ibid.*
[79] *Ibid.*
[80] The clauses with such nationality criterion are also called "*Barcelona Traction clauses*," which "*includes all clauses that introduce, in addition or alternatively to the place of incorporation and/or seat tests, a control test in order to extend the protection of the treaty to the parent company or to the shareholders of a third country company or of a Calvo corporation.*": Protopsaltis, P.M.: *The Challenge of the Barcelona Traction Hypothesis: Barcelona Traction Clauses and Denial of Benefits Clauses in BITs and IIAs*, The Journal of World Investment & Trade: Law, Economics, Politics, Vol. 11, No. 4, 2010, p. 567. Also, for the argument that the Barcelona Traction clauses and DOB clauses are "*two sides of one and the same coin,*" which both aim at the mitigation of the Barcelona Traction decision's effects, see generally, Protopsaltis, pp. 561-599. For an analysis on the effects of the *Barcelona Traction* case over international law, see, Soyler, Y.: *Barcelona Traction Davası ve Uluslararası Hukuka Etkisi*, Gazi Üniversitesi Hukuk Fakültesi Dergisi, Vol. 19, No. 3, 2015, pp. 207-247.
[81] Feldman, pp. 283-284; Kaya, p. 63.

state with the opportunity to guard against the legal entities with ungenuine and insubstantial relations with the purported home state,[82] while the first one entails the need for DOB provisions in the IIA.[83] Therefore, in other words, when the nationality of legal entities attempting to benefit from IIA protections is not determined based on their controlling shareholders' nationality, as is often the case, the absence of restricting mechanisms in IIAs, such as DOB clauses, would and could facilitate treaty shopping.[84]

As a result, the restrictions given place in investor definitions and DOB provisions could be considered as complimentary, rather than alternatives or competing. This is because while the former draw limits on the scope of investors; the latter allow the party states to deny the IIA advantages to a legal entity if it does not have a substantial and genuine link with the home state even though it would otherwise fall within the investor definition.[85]

Based on the above-given explanations on the definition and scope of DOB clauses, in the following part will the evolution such clauses in terms of their components and types be analyzed.

[82] Feldman, p. 283.
[83] *Ibid.*, p. 284.
[84] Shill, S.: *Ordering Paradigms in International Investment Law*, The Foundations of International Investment Law: Bringing Theory into Practice (Eds.: Douglas, Z. / Pauwelyn, J / Vinuales, J.E.), Oxford University Press, 2014 (International Investment Law), p. 121.
[85] Feldman, pp. 282, 284; Gaillard, E. / McNeill, M.: *THE ENERGY CHARTER TREATY*, Arbitration Under International Investment Agreements: A Guide to the Key Issues (Ed.: Yannaca-Small, K.), Second Edition, Oxford University Press, Oxford, 2018, p. 37; Yılmaz, İ.: Uluslararası Yatırım Uyuşmazlıklarının Tahkim Yoluyla Çözümü ve ICSID, First Edition, Istanbul, 2004, p. 195.

II. Evolution of Text and Context: The Components of DOB Clauses in the Past and Present

A. First Examples of DOB Clauses

DOB clauses—although commenced to be a proliferated element of IIAs in the last two decades—had not been an essential part of or indispensable to IIAs since the outset of their modern versions.[86] Likewise, DOB clause concept is still not a common component in such agreements at present.[87]

Besides, the US, Canada, Australia, and China have given place to DOB clauses since the earliest BITs and FTAs they had concluded. In such IIAs, DOB provisions aimed at preventing legal entities from benefiting from treaty protections without the assumption of any obligations set forth by them.[88] The earliest version of the DOB clauses in such IIAs is tracked down in the FCN entered into by and between the US and China in 1948,[89] which foresaw only corporate substantive requirements in a very broad way and a rule requiring the legal persons' political activities for such denial. While the former has been included within DOB clauses in the years following the cited treaty, albeit evolving, the latter has never been common in such clauses,

[86] Mistelis / Baltag (Investment Treaty Arbitration), p.1. According to the statistics provided by UNCTAD, the percentage of BITs including DOB clauses between 1959-2010 is 5%, while it increased to 58% for those concluded between 2011-2016. UNCTAD: *UNCTAD's REFORM PACKAGE FOR THE INTERNATIONAL INVESTMENT REGIME*, 2018 (Reform Package), https://investmentpolicy.unctad.org/publications/1190/unctad-s-reform-package-for-the-international-investment-regime-2018-edition-#:~:text=UNCTAD's%20Reform%20Package%20(2018%20edition,stakeholders%20in%20the%20field%20of (accessed on 20 August 2022), p. 70.

[87] Mistelis / Baltag (Investment Treaty Arbitration), p. 4. Having carried out a search in the UNCTAD Investment Policy Hub website database, it appears that "*226 out of 2584 mapped treaties*" include DOB clauses, *see*, https://investmentpolicy.unctad.org/international-investment-agreements/iia-mapping (Accessed on 20 August 2022).

[88] Mistelis / Baltag (Energy Charter Treaty), p. 1302.

[89] For a few examples among many sources citing the referred FCN as the earliest treaty including a DOB clause, see, Mistelis / Baltag (Investment Treaty Arbitration), p. 5; Ramachanderan, p. 230.

which would rather be implied in the investor definitions of IIAs. The referred clause provided the following language:

> "*The provisions of this Treaty shall not be construed to accord any rights or privileges to corporations and associations engaged in political activities or with respect to the organization of or participation in such corporations and associations. Moreover, each High Contracting Party reserves the right to deny any of the rights and privileges accorded by this Treaty to any corporation or association created or organized under the laws and regulations of the other High Contracting Party which is directly or indirectly owned or controlled, through majority stock ownership or otherwise, by nationals, corporations or associations of any third country or countries.*"[90]

In the UNCTAD Investment Policy Hub database,[91] the oldest BIT with a DOB clause is the one between the Republic of Korea and Switzerland adopted in 1971. The Protocol signed by the parties in addition to the BIT foresaw the following DOB provision:

> "*Notwithstanding Article 7 (b), each Party may reserve the right to deny the benefit of the present Agreement to any company which is controlled by nationals or companies of a third country.*
>
> *Both Parties shall come to an understanding in each case with regard to whether the interest held by nationals of either Party is a controlling*

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[90] United Nations: *Treaty Series: Treaties and international agreements registered or filed and recorded with the Secretariat of the United Nations*, Vol. 25, 1949, https://treaties.un.org/doc/Publication/UNTS/Volume%2025/v25.pdf (accessed on 19 August 2022), p. 138.

[91] *See*, https://investmentpolicy.unctad.org/international-investment-agreements/iia-mapping (Accessed on 20 August 2022).

interest permitting to exercise decisive influence on the company. Should such a [sic] *understanding not be reached, the case shall be settled under Article 8.*"[92]

The referred clause seems to be formulated in a very broad way that any company controlled by third-country nationals may be denied the benefits under the BIT. Also, for the party states, it sets forth a consultation requirement regarding the determination of the extend of the control possessed by each parties' nationals. Last, the provision foresees that in the case of the failure of such consultations, Article 8 on SSDS would apply.

B. Components and Types of Formulations of DOB Clauses in IIAs

In this part of the thesis, the components and formulation types of DOB clauses will be examined with the examples of such clauses included in BITs and MIAs for two purposes: to demonstrate the evolution of such clauses since the very first examples and to ascertain the factors differentiating such clauses in different IIAs. In this elaboration, the historical line of IIAs will be followed, and the clauses with certain characteristics emerging for the first time will be attempted to be presented. For such endeavor, one may need to distinguish the categories of denial requirements, on which DOB clauses are based and which needs to be met for host states to be able to deny treaty benefits, wholly or in part, or for such benefits to be automatically denied.

[92] Korea, Republic of - Switzerland BIT (1971) , adopted on 7 April 1971, https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/3340/download (accessed on 5 August 2022).

First, in such clauses, substantive requirements take place, which mainly concern the corporate and diplomatic items.[93] For example, regarding the former, the ownership or control requirement (i.e., whether the putative investor or investment referred to in a DOB provision is owned or controlled by a third-state national) and substantial business activity requirements could be given. The latter[94] refers to the diplomatic and economic relations between the denying party and the third state, the nationals of which own or control the putative investor or the investment in question, and it may include the diplomatic relations between the states as a whole, e.g., whether maintaining diplomatic or economic relations or not, or may refer to any measures taken by the denying party against such third state or its nationals. For practical purposes, in this part of the thesis, the first substantive requirement category will be referred to as "corporate substantive requirements," while the second one, "diplomatic substantive requirements." Having said that, one should not overlook the fact that the items placed under the said categories may vary to certain extent.

For example, while diplomatic substantive requirements in some provisions may set forth the denying party not having diplomatic or economic relations with a third state, some others may refer to or add measures (e.g., sanctions or any other form of prohibitive measures) taken by the denying party, sometimes even specifying their purposes (e.g., the maintenance of international peace and security). Also, as it will be seen in the below-given examples and cases, the denial may be formulated by: (1)

[93] Kartal, B.: Enerji Şartı Anlaşması Çerçevesinde Uyuşmazlıkların Çözümü ve Stockholm Ticaret Odası Tahkimi, Onikilevha, İstanbul, 2020, pp. 26-27; Yılmaz, p. 193.

[94] For a view in the way that such diplomatic components in DOB provisions serve the denying states' foreign policy objectives by preventing the nationals of certain countries from benefiting from IIA protections, see, Baltag, C.: The Energy Charter Treaty: The Notion of Investor, Kluwer Law International, 2017 (Investor), p. 163, citing, Vandevelde, K.J.: Bilateral Investment Treaties: History, Policy and Interpretation, Oxford University Press, New York, 2010, p. 163.

addressing investors, as in Article 17(1) of the ECT with corporate substantive requirements and Article 1(2) of the US-Ecuador BIT, entered into force on 11 May 1997, with both corporate and diplomatic substantive requirements, or (2) investments, as in Article 17(2) of the ECT with diplomatic substantive requirements, or (3) both investors and investments, as in Article 12 of the US Model BIT (2004) with both corporate and diplomatic substantive requirements.

Second, there may be procedural requirements in DOB clauses, and they may oblige the denying party to satisfy certain procedural pre-conditions for the invocation of such clauses. Said requirements might necessitate taking actions in collaboration with the other, non-denying, party to the IIA, such as notice and/or consultation requirements; or they may deal with the procedures needed to be applied by the denying party to be able to benefit from the DOB provisions, such as the timing of invocation of the relevant DOB clause.

In light of the foregoing elements of DOB clauses, such provisions are considered to be split into four categories: (1) the “unlimited clause” type that may be activated at the discretion of the denying party and deny the benefits of an IIA to the entities under the ownership and/or control of third-state nationals; (2) the “conditional clause” type, as the most conventional one among all, including the requirements concerning substantial business activities and/or diplomatic relations between the host state and third state, in addition to the ownership- and/or control-related requirement; (3) the “consensual clause” type that requires the joint decision of the party states to the relevant IIA; and, (4) the “automatic clause” type, including various combinations of the referred requirements with a formulation automatically triggering the denial upon the fulfillment of such requirements.[95]

In the following section, samples of DOB clauses from BITs and MIAs will be analyzed to demonstrate how DOB clauses in different IIAs may be at variance in spite of the fact that they aim at the same objective.

1. DOB Provisions in BITs

In Egypt-Switzerland BIT (1973)[96], entered into force on 4 June 1974 and was terminated in 2010, the second DOB provision, mainly in line with the above-examined Republic of Korea-Switzerland BIT,[97] was included via the exchange of Letters, incorporated into the BIT as annexes and integrated parts.[98] That is, the Letter no. 1. brought about a corporate (i.e., ownership or control by third-state nationals) and a consultation requirement.[99]

In Article 1(c) of the US-Panama BIT (1982), entered into force on 30 May 1991, a DOB provision was included, which set forth that each party reserved the right to deny the advantages of the BIT to the companies of any parties if they are owned or controlled by third-party state nationals. However, according to the referred provision,

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95 Côté, pp. 3-4.

96 Convention entre la Confédération Suisse et la République Arabe d'Egypte concernant l'encouragement et la protection réciproque des investissements, adopted on 25 July 1973, https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/1114/download (accessed on 22 August 2022) (Egypt-Switzerland BIT (1973)).

97 See, *supra* fn. 124.

98 See, Art. 12 of the Egypt-Switzerland BIT 1973: "*Quatre lettres (no I–IV) échangées entre les Parties Contractantes sont annexées au présent texte. La lettre n° I se référant à l'article 1, chiffre 2, et la lettre no IV se référant à l'article 8 font partie intégrante de la présente Convention.*"

99 See, the relevant part of the Letter no.1 is as the following: "*Nonobstant l'article 1, chiffre 2, chaque partie peut se réserver le droit de refuser le bénéfice de la présente Convention à toute société dans laquelle des ressortissants ou sociétés d'un Etat tiers ont un intérêt prépondérant. Les deux Parties Contractantes s'entendront dans chaque cas sur la question de savoir si l'intérêt qui appartient aux ressortissants de l'une des Parties Contractantes constitue un intérêt prépondérant permettant de contrôler la société ou d'exercer sur elle une influence déterminante. Si une entente ne peut être trouvée, le cas sera réglé conformément à l'article 10.*": *supra* fn. 128.

in the case such denied company is of the party other than the denying party, the denying part should have consulted with the other to find "*a mutually satisfactory resolution*" regarding the issue in question.[100] Therefore, in this provision, too, the only substantive requirement is the ownership or control by third-state nationals, and it foresees a consultation mechanism.

In the BITs to which Australia has been a party, DOB clauses take part in different formulations. Article 2(3) of Australia-Papua New Guinea BIT (1990), entered into force on 20 October 1991, provides that each party thereto reserves the right to deny the treaty benefits to *"any of its own companies"* under the ownership or control of third-state nationals or companies.[101] Article 2(2) of Australia-Vietnam BIT (1991), entered into force on 11 September 1991, and Australia-Czech Republic BIT (1993), entered into force on 29 June 1994, both require that the parties make a joint decision via consultation to deny the treaty benefits to the companies of a contracting party, which are owned or controlled by third-state nationals.[102] Therefore, precisely,

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[100] The referred clause reads as the following: *"Each Party reserves the right to deny to any of its own companies or to a company of the other Party the advantages of this Treaty, except with respect to recognition of juridical status and access to courts, if nationals of any third country own or control such company; provided that whenever one Party concludes that the benefits of this Treaty should not be extended to a company of the other Party for this reason, it shall consult with the other Party to seek a mutually satisfactory resolution to this matter"*: Treaty between the United States of America and the Republic of Panama concerning the Treatment and Protection of Investments, adopted on 27 October 1982, https://jusmundi.com/en/document/treaty/en-treaty-between-the-united-states-of-america-and-the-republic-of-panama-concerning-the-treatment-and-protection-of-investments-panama-united-states-of-america-bit-1982-wednesday-27th-october-1982 (accessed on 22 August 2022) (the US-Panama BIT (1982)).

[101] The referred clause reads as the following: "*Each Contracting Party reserves the right to refuse to extend the rights and benefits of this Agreement to any of its own companies if nationals or companies of any third country own or control any such company.*": Agreement Between the Government of Australia and the Government of the Independent State of Papua New Guinea for the Promotion and Protection of Investments, adopted on 3 September 1990, https://jusmundi.com/en/document/treaty/en-australia-papua-new-guinea-bit-1990-australia-papua-new-guinea-bit-1990-monday-3rd-september-1990 (accessed on 22 August 2022) (Australia-Papua New Guinea BIT (1990)).

[102] The referred clause reads as the following: "*Where a company of a Contracting Party is owned or controlled by a citizen or a company of any third country, the Contracting Parties may decide jointly in consultation not to extend the rights and benefits of this Agreement to such company.*": Agreement Between Australia and the Czech Republic on the Reciprocal Promotion and Protection of Investments,

mainly differing from the Australia-Papua New Guinea BIT (1990), the Australia-Vietnam BIT (1991) and Australia-Czech Republic BIT (1993) provide a joint consultation requirement in case where third-state nationals hold the ownership or control over the companies in question.

In the US-Egypt BIT (1982), entered into force on 27 June 1992, and got amended in between, a DOB provision takes place as well. According to Paragraph 1 of the Protocol to the BIT, agreed on 11 March 1986 as an integral part of the BIT, the DOB clause existed with regard to "*any company of either [p]arty,*" together with the affiliates or subsidiaries thereof, which are under the control of third-state nationals. The point in such clause that turned out to be controversial as analyzed in the following chapter is that it foresees a prompt consultation requirement upon any party's decision to deny the treaty benefits to the above-referred entities.[103]

As of the 1985s, there emerged two new components in the DOB clauses included in the BITs signed by the US: substantial business activity and normal economic relations requirements.

Article 1(2) of the US-Grenada BIT (1986), entered into force on 3 March 1989, had the following DOB clause:

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adopted on 30 September 1993, https://jusmundi.com/en/document/treaty/en-australia-czech-republic-bit-1993-australia-czech-republic-bit-1993-thursday-30th-september-1993 (accessed on 22 August 2022) (Australia-Czech Republic BIT (1993)); Agreement Between Australia and the Socialist Republic of Vietnam on the Reciprocal Promotion and Protection of Investments, adopted on 5 March 1991, https://jusmundi.com/en/document/treaty/en-australia-viet-nam-bit-1991-australia-viet-nam-bit-1991-tuesday-5th-march-1991 (accessed on 22 August 2022) (Australia-Vietnam BIT (1991)).

[103] The referred clause reads as the following: "*Each Party reserves the right to deny the benefits of this Treaty to any company of either Party, or its affiliates or subsidiaries, if nationals of any third country control such company, affiliate or subsidiary; provided that, whenever one Party concludes that the benefits of this Treaty should not be extended for this reason, it shall promptly consult with the other Party to seek a mutually satisfactory resolution of this matter.*": A Treaty between the United States of America and the Arab Republic of Egypt concerning the Reciprocal Encouragement and Protection of Investments, adopted on 29 September 1982, https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/1123/download (accessed on 22 August 2022) (the US-Egypt BIT (1982)).

"***Each Party reserves the right to deny*** *to any company* ***the advantages of the Treaty*** *if* ***nationals of any third country control*** *such company and, in the case of a company of the other Party,* ***that company has no substantial business activities*** *in the territory of the other Party* ***or*** *is controlled by nationals* ***of a third country*** *with which* ***the denying Party does not maintain normal economic relations****.*"[104] [Emphasis added].

According to the referred clause, the treaty benefits could be denied to any company under the control of third-state nationals. However, as for the companies from the party other than the denying party, any of the following scenarios were required for such application: the company's lack of substantial business activities in the country of incorporation or the absence of "*normal economic relations*" between the denying party and the third state, of which the controlling actors have the nationality. In comparison with the previous US BITs, in the cited clause, it appears that the consultation requirement is removed, the requirement of the ownership and control by a third-state national has retained; and for the companies of the other party, in addition to the referred ownership and control requirement, the company's not having substantial business activity in such other party's territory or, alternatively, being controlled by the nationals of a third state with whom the denying party does not have normal economic relations is required for the party states to be able to deny the benefits of the treaty. In this sense, one may interpret such changes in the DOB clauses in the way that the corporate substantial requirements had undergone an evolution and

[104] Treaty between the United States of America and Grenada concerning the Reciprocal Encouragement and Protection of Investment, adopted on 2 May 1986, https://jusmundi.com/en/document/treaty/en-treaty-between-the-united-states-of-america-and-grenada-concerning-the-reciprocal-encouragement-and-protection-of-investment-grenada-united-states-of-america-bit-1986-friday-2nd-may-1986 (accessed on 22 August 2022) (the US-Grenada BIT (1986)).

expansion by embracing the substantial business activity requirement in their texts, and diplomatic substantial requirements in the modern form began to be inserted as a part of such clauses. Therefore, the US-Grenada BIT (1986), with this formulation, seems to contain most of the modern components, albeit with changes in terminology and their scope, included in contemporary DOB clauses.

In the same vein as the above referred DOB clause, the US has given place to the DOB provisions with referred components in its model agreements since 1994. Article 12 in the US Model BIT (1994) provided a DOB clause of modern type. According to the referred clause, the DOB rights are reserved by each party with regard to the other-party companies under the ownership or control of third-state nationals in the presence of one of the following alternative conditions: (1) the denied company's lack of substantial business activities in the state of its constitution or organization, or (2) the third state in concern and denying party do not have "*normal economic relations.*"[105] This formulation has remained unchanged in the 1998 revision made on the referred model BIT.[106]

This provision of Article 12 in the US Model BIT (1994) was inserted into the corresponding article of the US-Bolivia BIT (1998), entered into force on 6 June 2001

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[105] The referred clause reads as the following:

> "*Each Party reserves the right to deny to a company of the other Party the benefits of this Treaty if nationals of a third country own or control the company and*
> *(a) the denying Party does not maintain normal economic relations with the third country; or*
> *(b) the company has no substantial business activities in the territory of the Party under whose laws it is constituted or organized.*"

See, Treaty Between the Government of the United States of America and the Government of [...] Concerning the Encouragement and Reciprocal Protection of Investment, adopted on 1994, https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/2867/download (accessed on 22 August 2022) (the US Model BIT (1994)).

[106] Treaty Between the Government of the United States of America and the Government of [...] Concerning the Encouragement and Reciprocal Protection of Investment, adopted on 1998, https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/2868/download (accessed on 22 August 2022) (the US Model BIT (1998)).

and terminated on 10 June 2012,[107] which included the US' Letter of Submittal clarifying the components included in the referred Article. In the Letter, the case of not maintaining normal economic relations with a third country is exemplified by economic sanctions, more specifically with the countries Cuba and Libya at the time. Also, it provided, as an example, that the clause would allow the US to deny the treaty benefits to a subsidiary of a mailbox company incorporated in Bolivia if third-state nationals control such entity and clarified that the provision would not grant a general permission for the US to apply such denial to the companies, whose seat (*siège social*) took place in Bolivia or which possessed a "*real and continuous link*" with it.[108]

When it comes to the US Model BITs dated 2004[109] and 2012,[110] more in line with then-contemporary US approach with a more detailed structure,[111] Article 17(1) provision included in both texts provides each parties with the DOB rights addressing the other-party investors in the form of enterprise, as defined and described in such BIT, and their investments, both under the ownership or control of non-party nationals in the presence of the following requirements: (1) the denying party and the referred

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[107] Treaty between the Government of the United States of America and the Government of the Republic of Bolivia concerning the Encouragement and Reciprocal Protection of Investment, adopted on 17 April 1998, https://jusmundi.com/en/document/treaty/en-treaty-between-the-government-of-the-united-states-of-america-and-the-government-of-the-republic-of-bolivia-concerning-the-encouragement-and-reciprocal-protection-of-investment-bolivia-united-states-of-america-bit-1998-friday-17th-april-1998 (accessed on 22 August 2022) (the US-Bolivia BIT (1998)).

[108] Mistelis / Baltag (Investment Treaty Arbitration), p. 9. Also, for a conclusion reached to the same effect, see, the commentary and the text of the *Treaty between the Government of the United States of America and the Government of the Hashemite Kingdom of Jordan concerning the Encouragement and Reciprocal Protection of Investment*, signed on 2 July 1995, are available at http://www.state.gov/documents/organization/43565.pdf, as cited and explained in, Mistelis / Baltag (Energy Charter Treaty), p. 1305.

[109] Treaty Between the Government of the United States of America and the Government of [...] Concerning the Encouragement and Reciprocal Protection of Investment, adopted on 2004, https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/2872/download (accessed on 22 August 2022) (the US Model BIT (2004)).

[110] Treaty Between the Government of the United States of America and the Government of [...] Concerning the Encouragement and Reciprocal Protection of Investment, adopted on 2012, https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/2870/download (accessed on 22 August 2022) (the US Model BIT (2012)).

[111] Mistelis / Baltag (Energy Charter Treaty), p. 1305.

non-party state "*does not maintain diplomatic relations,*" or (2) the denying party has imposed the measures aiming at the non-party state in question or the referred persons from that state, which amounts to the prohibition of subject-matter transactions with the other-party enterprise or are of the content violated or circumvented if the treaty benefits are accorded to such enterprises. In addition to the foregoing diplomatic substantive requirements, the corporate substantive requirements are set forth under Article 17(2), which put forth that such DOB rights may be exercised to the other-party investors in the form of enterprise and their investments, both under the ownership or control of non-party nationals, if such enterprise does not hold any substantial business activities in the other party.[112]

In the cited provision—although the motives and objectives are virtually same and completely consistent with the provisions in the previous US Model BITs—the terminology and scope of DOB clauses have changed and expanded. For example, the notion that had been given place as "normal economic relations" in the previous provisions evolved into a wider concept, and it is put forth that the third state, whose nationals own or control the investor in case, should be one with whom the denying party does not "maintain diplomatic relations" or the denying party should have such measures (e.g., sanctions or any other type of prohibitive measures imposed on the

[112] The referred clause reads as the following:

> "*1. A Party **may deny** the benefits of this Treaty to an investor of the other Party that is an enterprise of such other Party and to investments of that investor **if persons of a non-Party own or control** the enterprise and the denying Party:*
> *(a) does **not maintain diplomatic relations with the non-Party**; or*
> *(b) adopts or maintains **measures with respect to the non-Party or a person of the non-Party** that **prohibit transactions** with the enterprise **or** that **would be violated or circumvented** if the benefits of this Treaty were accorded to the enterprise or to its investments.*
> *2. A Party **may deny the** benefits of this Treaty to an investor of the other Party that is an enterprise of such other Party and to investments of that investor if the enterprise has **no substantial business activities** in the territory of the other Party **and persons of a non-Party, or of the denying Party, own or control** the enterprise*." [Emphasis added].

See, *supra* fn. 142 and 143.

third state or any person from it) that could be violated if the putative investor benefits from the protection provided by the BIT. Therefore, the first sub-paragraph presents an evolution of diplomatic substantive requirements in the US Model BITs. Also, in the second sub-paragraph, it seems that the widely utilized formula of corporate substantive requirement, including the ownership or control test and substantial business activity requirement, was kept by the drafters by subsuming the denying party nationals' ownership or control under the same category as the non-parties.[113]

In the modern model BITs that have been prepared and finalized in the recent years, one could see that the DOB provisions are drawn up in the way to encapsulate the components included the above-given examples, with some characterization differences regarding the categories of requirements—i.e., the corporate and diplomatic substantive requirements.[114]

For example, in Article 11 of the Czech Republic Model BIT (2016), the diplomatic substantive requirements are formulated in the way not explicitly reciting the maintenance-of-diplomatic-relations item but including the following cumulative conditions: first, the denying party should have imposed measures against the third

[113] In Article 10.12(2) of the US-Panama Trade Promotion Agreement, entered into force on 31 October 2012, notification and consultation requirements were included, in addition to the text identical to the corresponding sub-paragraph in the US Model BIT (2012). See, Trade Promotion Agreement between the United States and Panama, adopted on 28 June 2007, https://jusmundi.com/en/document/treaty/en-free-trade-agreement-between-the-united-states-and-panama-panama-us-fta-thursday-28th-june-2007 (accessed on 22 August 2022) (the US-Panama BIT (2012)).

[114] For the DOB clauses with similar components, see, e.g., Article 10 of Slovakia Model BIT (2009) (Agreement Between the Slovak Republic and [...] for the Promotion and Reciprocal Protection of Investments, adopted in 2019, https://jusmundi.com/en/document/treaty/en-agreement-between-the-slovak-republic-and-for-the-promotion-and-reciprocal-protection-of-investments-slovakia-model-bit-2019-tuesday-1st-january-2019) (accessed on 22 August 2022) (the Slovakia Model BIT (2009)); Article 13 of BLEU Model BIT (2019) (Agreement between the Belgium-Luxembourg Economic Union, on the One Hand and [...], on the Other Hand, on the Reciprocal Promotion and Protection of Investments, adopted on 28 March 2019, https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/5854/download) (accessed on 22 August 2022) (the BLEU Model BIT (2019)); Article 34 of Italy Model BIT (2021), Italy Model BIT, adopted in 2021, https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/6390/download (accessed on 22 August 2022).

state, which are regarding "*the maintenance of international peace and security*;" and second, such measures should have prohibited the transactions in question with the putative investor or the referred measures should have been "*violated or circumvented*" if the benefits of the BIT were provided to it or its investments.[115]

Last, but not least, the position of the Republic of Turkey here merits a mention: because although it had not given place to a DOB clause in its model BITs dated 2000[116] and 2009[117], such clauses with differing formulations have taken part in the BITs it has entered into.

The first such BIT with a DOB clause is the US-Turkey BIT (1985), which included a BIT formulation in its Article 1(2) identical to those included in the most then-contemporary US BITs:

> *"Each Party reserves the right to deny to any of its own companies or to a company of the other Party company the advantages of this Treaty if nationals of any third country control such company, provided that, whenever one party concludes that the benefits of this Treaty should not*

[115] Article 11 with the referred content reads as the following:

> "*A Contracting Party may deny the benefits of this Agreement to an investor of the other Contracting Party and to investments of that investor if investors of a third State own or control the investor and the denying Contracting Party adopts or maintains measures with respect to the third State that are related to maintenance of international peace and security and prohibit transactions with the investor or would be violated or circumvented if the benefits of this Agreement were accorded to the investor or to its investments.*"

See, Agreement Between the Czech Republic and [...] for the Promotion and Reciprocal Protection of Investments, adopted on 28 December 2016, https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/5407/download (accessed on 22 August 2022).

[116] Turkey Model BIT (2000), adopted in 2000, https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/2851/download (accessed on 28 August 2022) [Turkey Model BIT (2000)].

[117] Turkey Model BIT (2009), adopted in May 2009, https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/2852/download (accessed on 28 August 2022) [Turkey Model BIT (2009)]. Although Turkey replaced Turkey Model BIT (2009) with another model BIT dated 2016, the latter could not be found in the relevant databases. *See, e.g.*, https://investmentpolicy.unctad.org/international-investment-agreements/model-agreements (accessed on 28 August 2022).

be extended to a company of the other Party for this reason, it shall promptly consult with the other Party to seek a mutually satisfactory resolution of the matter. This right shall not apply with respect to recognition of juridical status and access to courts."[118]

Also, the DOB clauses including exactly the same components, albeit in different languages, took place in the Turkey BITs signed in the following years.[119] As of the 2010s, DOB clauses seem to have flourished and taken place in the Turkey BITs more commonly than before. With the Turkey-Azerbaijan BIT (2011), entered into force on 2 May 2013, the first diplomatic substantive requirements commenced to appear in DOB provisions. More interestingly, in the referred BIT, the DOB provision is given place in the definition of investor, and it foresees an automatic application of the DOB rights in the case an investor is under the ownership or control of a national of a third state, with whom the host state does not have diplomatic relations:

"If the investor is owned or controlled by persons having the nationality of a third state that has no diplomatic relations with the Contracting Party in whose territory the investment is made, this investor will not benefit from this Agreement."[120]

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[118] Treaty Between the United States of America and the Republic of Turkey Concerning The Reciprocal Encouragement and Protection of Investments, adopted on 3 December 1985, https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/2356/download (accessed on 28 August 2022) [the US-Turkey BIT (1985)].

[119] See, e.g., Article 1(2) of the Agreement Between the Republic of Turkey and The People's Republic of Bangladesh Concerning the Reciprocal Encouragement and Protection of Investments, adopted on 12 November 1987, https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/275/download ((accessed on 28 August 2022).

[120] Agreement Between the Government of the Republic of Turkey and the Government of the Republic of Azerbaijan on the Reciprocal Protection and Promotion of Investments, adopted on 25 October 2011, https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/3144/download (accessed on 28 August 2022) (the Turkey-Azerbaijan BIT (2011)).

In the Turkey-Pakistan BIT (2012)—not in force, though—a DOB clause with the traditional corporate substantial requirements is given place: such clause provides each party with the right to deny the BIT benefits to the investors of company form from the other party—and their investments—if such company does not have substantial business activities in the country of incorporation or organization (i.e., the home state) and owned or controlled by third-state investors. Also, as an interstate procedural requirement, the provision requires a notification by the denying party addressing the other party. The referred provision in Article 11 of the Turkey-Pakistan BIT (2012) provides the following:

> *"1. A Contracting Party may deny the benefits of this Agreement to an investor of the other Contracting Party that is a company of such other Contracting Party and to investments of such investor if the company has no substantial business activities in the territory of the Contracting Party under whose law it is constituted or organized, and investors of a non-Contracting Party or investors of the denying Contracting Party, own or control the company.*
>
> *2. The denying Contracting Party shall, to the extent practicable, notify the other Contracting Party before denying the benefits."*[121]

[121] Agreement Between the Government of the Republic of Turkey and the Government of the Islamic Republic of Pakistan Concerning the Reciprocal Promotion and Protection of Investments, adopted on 22 May 2012, https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/2134/download (accessed on 25 August 2022) (the Turkey-Pakistan BIT (2012)). For the same formulation, albeit with minor terminological changes, taking place under the corresponding articles in other Turkey BITs, see, Agreement Between the Government of the Republic of Turkey and the Government of the Gabonese Republic Concerning the Reciprocal Promotion and Protection of Investments, adopted on 18 July 2012, https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/1307/download (accessed on 25 August 2022); Agreement Between the Government of the Republic of Turkey and the Government of the Republic of the Gambia Concerning the Reciprocal Promotion and Protection of Investments, adopted on 12 March 2013, https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/3345/download

In the Turkey-Ghana BIT (2016), in addition to the corporate substantive requirements included in the foregoing Turkey BITs, a diplomatic substantive requirement is also given place: each party may invoke the DOB rights thereunder in the case an investor, and its investments, are owned or controlled by an investor from a third-state, targeting which the denying party holds measures to the prohibitive or restrictive effect on the relevant transactions.[122]

When it comes to the DOB provisions in MIAs, they seem to include more or less similar, if not the same, components as those included in BITs, which are addressed in the following part.

2. DOB Provisions on MIAs

NAFTA, entered into force on 1 January 1994, sets forth the DOB provision under Article 1113 in two sub-paragraphs as following:

(accessed on 25 August 2022); Agreement Between the Government of the Republic of Turkey and the Government of the Republic of the Guinea Concerning the Reciprocal Promotion and Protection of Investments, adopted on 18 June 2013, https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/6092/download (accessed on 25 August 2022); Agreement Between the Government of the Republic of Rwanda and the Government of the Republic of Turkey Concerning the Reciprocal Promotion and Protection of Investments, adopted on 3 March 2016, https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/5415/download (accessed on 25 August 2022); Agreement Between the Government of the Republic of Turkey and the Government of Burkina Faso Concerning the Reciprocal Promotion and Protection of Investments, adopted on 11 April 2019, https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/6087/download (accessed on 25 August 2022). For the DOB clause with the same corporate substantive requirements as above but without the notification requirement, see, Article 13 in Agreement Between the Government of the Republic of Colombia and the Government of the Republic of Turkey Concerning the Reciprocal Promotion and Protection of Investments, adopted on 28 July 2014, https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/3249/download (accessed on 25 August 2022). For the DOB clause with the same corporate substantive requirements as above in different language and with an additional consultation requirement dependent on the request of the home state, see, Article 13 in Agreement on Investment Under the Framework Agreement Establishing a Free Trade Area Between the Republic of Korea and the Republic of Turkey, adopted on 26 February 2015, https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/4729/download (accessed on 25 August 2022).

[122] Agreement Between the Government of the Republic of Turkey and the Government of the Republic of Ghana for the Reciprocal Promotion and Protection of Investments, adopted on 1 March 2016, https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/5844/download (accessed on 25 August 2022) (the Turkey-Ghana BIT (2016)).

"1. A Party may deny the benefits of this Chapter to an investor of another Party that is an enterprise of such Party and to investments of such investor if investors of a non-Party own or control the enterprise and the denying Party:

a. does not maintain diplomatic relations with the non-Party; or

b. adopts or maintains ***measures*** *with respect to* ***the non-Party that prohibit transactions with the enterprise or that would be violated or circumvented*** *if the benefits of this Chapter were accorded to the enterprise or to its investments.*

2. Subject to ***prior notification and consultation*** *in accordance with Articles 1803 (Notification and Provision of Information) and 2006 (Consultations),* ***a Party may deny the benefits of this Chapter*** *to an investor of another Party that is an enterprise of such Party and to investments of such investors* ***if investors of a non-Party own or control the enterprise and the enterprise has no substantial business activities in the territory of the Party*** *under whose law it is constituted or organized."*[123] [Emphasis added]

The first sub-paragraph includes the diplomatic substantive requirements and states that the parties may deny the benefits given place under the chapter, where the referred Article locates, to the other-party investors of enterprise form and their investments if they are owned or controlled by the investors from third states in cases where the denying party does not have diplomatic relations with such third states or

[123] North American Free Trade Agreement, adopted on 17 December 1992, Article 1113: Denial of Benefits, https://jusmundi.com/en/document/treaty/en-north-american-free-trade-agreement-nafta-thursday-17th-december-1992 (accessed on 22 August 2022).

has taken measures regarding them "*that prohibit transactions with the enterprise or that would be violated or circumvented*" by the provision of treaty protection to the referred enterprise. Therefore, this sub-paragraph appears to be in line with the modern conventional formulation of diplomatic substantive requirements in BITs and other MIAs. As for the second sub-paragraph, which deals with the corporate substantive requirements, the provision brings about two distinctive procedural pre-conditions for the invocation of DOB mechanism in addition to the common requirements: Prior notification and consultation.[124]

CUSMA, drafted with the purpose to replace NAFTA[125] and entered into force on 1 July 2020,[126] includes a DOB provision in its Article 14.14, which sets forth substantially similar formulation and almost identical components as NAFTA.[127] The

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[124] For the view in the literature that the implication of the notification requirement is "*unclear,*" see, Mistelis / Baltag (Energy Charter Treaty), p. 1308, fn. 29.

[125] For the Protocol Replacing the NAFTA with the USMCA (2018), see, Protocol Replacing the North American Free Trade Agreement with the Agreement Between Canada, the United States of America and the United Mexican States (2018), adopted on 30 November 2018, https://jusmundi.com/en/document/treaty/en-protocol-replacing-the-north-american-free-trade-agreement-with-the-agreement-between-canada-the-united-states-of-america-and-the-united-mexican-states-2018-protocol-replacing-the-nafta-with-the-usmca-2018-friday-30th-november-2018 (accessed on 22 August 2022).

[126] Under Article 14.2 of CUSMA, the ISDS mechanism is limited to those circumstances referred to in the provision, as provided in the following: "*For greater certainty, an investor may only submit a claim to arbitration under this Chapter as provided under Annex 14-C (Legacy Investment Claims and Pending Claims), Annex 14-D (Mexico-United States Investment Disputes), or Annex 14-E (Mexico-United States Investment Disputes Related to Covered Government Contracts).*" Therefore, the ISDS mechanism was kept out between Canada and the US. However, on the other hand, under Annex 14-D to CUSMA, the ISDS mechanism to apply between Mexico and the US is formulated, with a DOB provision additionally, which set forth the automatic application regarding the "*claims by shell corporations owned or controlled by a person of a non-Annex Party considered to be a nonmarket economy.*" For further details, see, Côté, p. 13.

[127] The referred clause reads as the following:

> "*1. A Party may deny the benefits of this Chapter to an investor of another Party that is an enterprise of that other Party and to investments of that investor if the enterprise:*
> *a. is owned or controlled by a person of a non-Party or of the denying Party; and*
> *b. has no substantial business activities in the territory of any Party other than the denying Party.*
> *2. A Party may deny the benefits of this Chapter to an investor of another Party that is an enterprise of that other Party and to investments of that investor if persons of a non-Party own or control the enterprise and the denying Party adopts or maintains measures with respect to the non-Party or a person of the non-Party that prohibit transactions with the enterprise or*

referred provision's most evident difference than that set forth under NAFTA is the change in the order of sub-paragraphs, which would not be expected to have any essential implications. Also, in the first sub-paragraph, the prior notice and consultation procedure required by NAFTA provision is not given place. Last, and more importantly, in the sub-paragraph 1(a), denying party is included besides the third state, of which the person owning or controlling the denied enterprise is. This addition seems to be aiming at preventing the round-tripping cases where the other-party enterprises and their investments are controlled or owned by the investors of the denying party and they have no substantial business activities in such other party.

Including mostly the same components as the above-recited provision, CAFTA, entered into force on 1 January 2009, has a DOB provision in its Article 10.12. In the referred clause, the main distinguishing element seems to be the inclusion of the denying party nationals' ownership or control alongside the non-party nationals for the prevention of the round-tripping. Also, as for the corporate substantive requirements, an interstate notification and consultation requirements are also foreseen in the provision.[128]

> *that would be violated or circumvented if the benefits of this Chapter were accorded to the enterprise or to its investments*."

See, Agreement between the United States of America, the United Mexican States, and Canada, adopted on 30 November 2018, https://jusmundi.com/en/document/treaty/en-agreement-between-the-united-states-of-america-the-united-mexican-states-and-canada-usmca-2018-friday-30th-november-2018 (accessed on 22 August 2022).

[128] The referred clause reads as the following:

> "*1. A Party* ***may deny the benefits of this Chapter*** *to an investor of another Party that is an enterprise of such other Party and to investments of that investor* ***if persons of a non-Party own or control the enterprise and the denying Party****:*
> *a. does* ***not maintain diplomatic relations*** *with the non-Party;* ***or***
> *b. adopts or maintains* ***measures*** *with respect to the non-Party or a person of the non- Party that* ***prohibit transactions*** *with the enterprise* ***or that would be violated or circumvented*** *if the benefits of this Chapter were accorded to the enterprise or to its investments.*
> *2.* ***Subject to*** *Articles 18.3 (****Notification and Provision of Information****)* ***and*** *20.4 (****Consultations****), a Party may deny the benefits of this Chapter to an investor of another Party that is an enterprise of such other Party and to investments of that investor* ***if*** *the enterprise*

Another MIA with the DOB clause is the CETA, adopted on 30 October 2016. Although CETA has not entered into force yet, its Article 30.7 permits the provisional application of the treaty provisions, within the scope of which the DOB provision included in Article 8.16 takes part.[129] The referred provision provides only diplomatic substantive requirements in the modern form.[130]

The above-cited MIA DOB clauses provide the parties with the right to deny the benefits of the "chapter" where the DOB clause takes place in lieu of making a general reference to the benefits foreseen by the treaty. Such formulation is identical to that of the ECT DOB clause, in which the language provides the right to deny the advantages

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> *has **no substantial business activities** in the territory of any Party, other than the denying Party, **and persons of a non-Party, or of the denying Party, own or control the enterprise**.*"

See, Central America-Dominican Republic-United States Free Trade Agreement (DR-CAFTA), adopted on 5 August 2004, https://jusmundi.com/en/document/treaty/en-central-america-dominican-republic-united-states-free-trade-agreement-dr-cafta-cafta-dr-usa-2004-thursday-5th-august-2004#pa_27380 (accessed on 22 August 2022).

[129]For such and further information on CETA, see, https://investmentpolicy.unctad.org/international-investment-agreements/treaties/otheriia/3546/canada---eu-ceta-2016- (accessed on 22 August 2022). For the notice released in Official Journal of the European Union with regard to the provisional application of certain CETA provisions, please see: https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:22017X0916(02)&from=LV (accessed on 22 August 2022).

[130] The referred clause reads as the following:

> "*A Party **may deny the benefits of this Chapter** to an **investor of the other Party** that is an enterprise of that Party and to investments of that investor **if**:*
> *(a) an investor of a third country owns or controls the enterprise; and*
> *(b) the denying Party **adopts or maintains a measure** with respect to the third country that:*
> *(i) relates to the maintenance of international peace and security; and*
> *(ii) **prohibits transactions** with the enterprise **or would be violated or circumvented** if the benefits of this Chapter were accorded to the enterprise or to its investments.*" [Emphasis added]

Also, the investor definition of the CETA under its Article 8.1 should also be taken into account in relation to its approach toward shell corporations:

> "***[I]nvestor** means a Party, a natural person or an enterprise of a Party, other than a branch or a representative office, that seeks to make, is making or has made an investment in the territory of the other Party;*
> *For the purposes of this definition, an **enterprise of a Party** is:*
> *(a) an enterprise that is constituted or organised under the laws of that Party and has substantial business activities in the territory of that Party; or*
> *(b) an enterprise that is constituted or organised under the laws of that Party and is directly or indirectly owned or controlled by a natural person of that Party or by an enterprise mentioned under paragraph (a)…*" [Bold emphasis provided in the original text; underlined emphasis added]

See, Comprehensive Economic and Trade Agreement between Canada and the European Union, adopted on 30 October 2016, https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/3593/download (accessed on 22 August 2022).

of the “part” where the clause is. However, the chapter-wise restriction in the non-ECT MIAs seems not to result in the complications stemming from below-analyzed ECT formulation: because, unlike the ECT, in all other MIAs all the ISDS provisions take place in the same chapter as the DOB clause.

At this point, the ECT, as the MIA most relevant to this thesis and including an oft-invoked DOB provision, should be touched upon. The ECT, entered into force in April 1998, has the DOB provision in Article 17,[131] titled “*Non-Application of Part III in Certain Circumstances*.” The said clause provides that the right to deny the benefits of the part (i.e., Part III of the ECT where the DOB clause locates) is reserved by contracting parties on the condition that there-included corporate and diplomatic substantive requirements are fulfilled. Article 17(1), dealing with the corporate substantive requirements, simply include the legal entities within the scope of denied category of investors upon the fulfillment of the following cumulative pre-conditions: (1) If they are under the ownership or control of third-state nationals, and (2) they do not have any substantial business activities in the country of organization. Article 17(2), concerning the diplomatic substantive requirements, sets forth that the investments proven by the denying party to be of a national from a third state, with which the denying party does not hold any diplomatic relations or has adopted the measures to the prohibitive effect, may be denied from the Part III benefits.[132] The referred ECT DOB clause is formulated as follows:

> “*Each Contracting Party reserves the right to deny the advantages of this Part to:*

[131] The ECT is referred to be “*the most often-invoked investment agreement worldwide.*”: Verburg, C.: *Modernising the Energy Charter Treaty: An Opportunity to Enhance Legal Certainty in Investor-State Dispute Settlement*, Journal of World Investment & Trade, Vol. 20, 2019, p. 425.
[132] See, *supra* fn. 5.

1. ***a legal entity*** *if citizens or nationals of a third state own or control such entity and if that entity has no substantial business activities in the Area of the Contracting Party in which it is organized; or*

2. ***an Investment****, if the denying Contracting Party establishes that such Investment is* ***an Investment of an Investor of a third state*** *with or as to which the denying Contracting Party:*

a. does not maintain a diplomatic relationship; or

b. adopts or maintains measures that:

i. ***prohibit transactions*** *with Investors of that state; or*

ii. ***would be violated or circumvented*** *if the benefits of this Part were accorded to Investors of that state or to their Investments.*" [133] [Emphasis added].

In the light of the above-cited DOB provisions included in BITs and other MIAs, the ECT seems not to bring about any completely exceptional or unprecedented requirements as for the DOB concept in its formulation.[134] However, for some certain reason, it is the most frequently discussed DOB provision. This is submitted to be so because, first, it is the most repeatedly invoked DOB clause among those in IIAs,[135] which could make it exposed to over-argumentation on its text by disputing parties, i.e., the claimants and respondents. Also, it locates in Part III (Investment Promotion and Protection) of the ECT,[136] while the ISDS provisions takes part in Part V (Dispute

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[133] *Ibid.*
[134] In this context, one must note that the first draft of the ECT investment chapter was designed based on the 1991 Model BIT of the UK. See, Verburg, p. 439. In other words, the MIA characteristics of the ECT, naturally, did not bring about an isolation from then present BITs and IIA practices.
[135] *Supra* fn. 164.
[136] The ECT Part III, including the substantive standards for the protection and promotion of energy investments, aims at the provision of predictable investment environment by minimizing "*non-commercial risks related to foreign investments.*": Kang, p. 19.

Settlement) of the treaty. This turned out to be a controversial issue since it had only referred to the denial of the advantages in Part III, which includes the substantive standards of investment protection and promotion—that is, leaving the ISDS provisions off, resulted in differences on whether the DOB clause applies to the ECT ISDS provisions or not.[137]

Furthermore, its not setting forth the definition of certain notions, e.g., third state, etc., and any procedural requirements regarding the application of DOB mechanism has already been resulting in contentious claims and arguments that will be touched upon with more vivid details in Chapter II. Calling other ECT provisions, such as those included in Article 2 and the Preamble, into play as an inevitable corollary of such contentions and the employment of the object-and-purpose interpretation[138] have intensified such difficulties. Therefore, the application of the ECT clause becomes more and more a complication because of what it does not provide rather, than what it does.

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[137] At this juncture, it should be noted that while the BIT provisions, examined in the previous part, refer to the benefits of the treaty in question, MIAs and FTAs make such reference to the chapter or part where such DOB provisions locate. The reason of such difference is explained to be that MIAs and FTAs, including the ECT, encompass different facets of the relevant activities, e.g., transit, trade, dispute resolution etc., while the BITs only concern with investment. Therefore, such reference specific to the MIA and/or FTA part or chapter where the investment-related clauses, along with the DOB provision, takes place seems to be conceivable. *See,* Mistelis / Baltag (Energy Charter Treaty), p. 1306. However, its being problematic in the ECT formulation and jurisprudence stems from the fact that the ISDS mechanism takes part in a different part of the ECT than where the DOB provision is, and such difference was not resolved via a direct or indirect reference between the chapters. For an example of such cross-reference in the United States-Australia Free Trade Agreement, entered into force on 1 January 2005, see, Mistelis / Baltag (Energy Charter Treaty), p. 1306, fn. 20.

[138] Such method of interpretation is given place under Article 31(1) of the VCLT, the codification of customary rules of treaty interpretation, which states the following: "*A treaty shall be interpreted* ***in good faith*** *in accordance with* ***the ordinary meaning*** *to be given to the terms of the treaty* ***in their context and in the light of its object and purpose****.*" See, *supra* fn. 69. For further information on the application and interpretation of the VCLT Article 31, see, Weeramantry, J.R.: Treaty Interpretation in Investment Arbitration, Oxford University Press, Oxford, 2012, pp. 41-76.

3. Current Trends in DOB Clauses

As briefly touched upon in the previous section with regard to the application of the ECT DOB clause and will be critically analyzed in the following chapter in relation to several IIAs, the traditional formulations of DOB clauses are naturally likely to result in differences of application and interpretation. Therefore, having taken such differences into account, the IIAs concluded in the recent years has commenced including various new requirements, specifically procedural ones. The aim of such inclusions seems to be avoiding the potential repercussions of referred differences and the provision of foreseeability and consistency in practice.

Also, apart from the mentioned category of procedural requirements, to achieve an alignment with the humanitarian concerns of international community, it appears that certain substantive requirements have been proliferating in IIAs. For example, the measures regarding international peace and security became a part of diplomatic substantive requirements in a number of IIAs. Even further, the denied investor category has extended to those committing human right violations, without any conditions regarding the ownership or control by or over such investors.

In this sense, first, the provisions of Article 17 in Canada Model BIT (2021)[139] brings about a timing-related procedural requirement for the denying-party state to be able to deny the treaty benefits to putative investors. That is, in an arbitral process, the denying party must exercise its rights under the referred Article within a reasonable

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[139] "*A Party may, within a reasonable time and no later than its principal submission on the merits, such as the counter-memorial, in an arbitration under this Agreement, deny the benefits of this Agreement to an investor.*" See, Model Agreement Between Canada and [...] for the Promotion and Protection of Investments (2021), adopted on 12 May 2021, https://jusmundi.com/en/document/treaty/en-model-agreement-between-canada-and-for-the-promotion-and-protection-of-investments-2021-canada-model-bit-2021-wednesday-12th-may-2021 (accessed on 22 August 2022) (the Canada Model BIT (2021)).

period of time, which is described to be "*no later than its principal submission on the merits, such as the counter-memorial.*" In other words, such provision enables the denying party to exercise its DOB rights after the commencement of arbitration proceedings. Also, it requires the denying party's adoption and maintenance of measures regarding the non-party or the investors of it that "*relates to the maintenance of international peace and security,*" as the first limb of cumulative diplomatic substantive requirements.

Article 19.5 of the Hong Kong, China SAR – ASEAN Investment Agreement also provides a timing provision for the exercise of denial rights by party states; however, in a permissive way rather than restrictive: it authorizes the invocation of DOB rights at any time, even after the commencement of arbitration.[140]

In a similar vein, Article 25 of Morocco Model BIT 2019 provides a procedural component stating that the treaty benefits shall be denied at any time, even after the commencement of arbitral proceedings in accordance with the treaty's relevant provisions.[141] However, the difference of this provision from the foregoing one is implied in the expression "*[l]es avantages du présent accord sont refusés,*" which

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[140] The referred clause reads as the following:

> "***A Party's right to deny*** *the benefits of this Agreement as provided for in this Article* ***may be*** *exercised at any time,* ***including after the institution of arbitration proceedings*** *in accordance with Article 20 (Settlement of Investment Disputes between a Party and an Investor).*" [Emphasis added].

See, Agreement on Investment among the Governments of the Hong Kong Special Administrative Region of the People's Republic of China and the Member States of the Association of Southeast Asian Nations, adopted on 12 November 2017, https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/5655/download (accessed on 22 August 2022) (the Hong Kong, China SAR – ASEAN Investment Agreement).

[141] Both sub-paragraphs of Article 25 of Morocco Model BIT (2019) begins with the following: "*Les avantages du présent accord sont refusés, à tout moment, y compris après l'introduction d'une procédure arbitrale en vertu de la section VI…*" See, Agreement between the Kingdom of Morocco and […] for the Reciprocal Promotion and Protection of Investments, adopted on 1 June 2019, https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/5895/download (accessed on 22 August 2022) (the Morocco Model BIT (2019)).

requires that the denial of benefits under the treaty come about automatically; that is, without the need to exercise of such right by the denying party.

The same automatic denial mechanism takes part in Article 8 of Iran-Slovakia BIT (2016), entered into force on 30 August 2017.[142] Sub-paragraph 1 of the referred Article provides that the treaty benefits *"shall be denied"* to investors in the form of enterprise from a contracting party or such investors' investments if they are wholly or partly owned or controlled by the nationals of a third state, with whom the denying party does not have diplomatic relations or against whom the denying party adopts or maintains measures as described in the provision. Sub-paragraph 2 of the BIT, interestingly, denies the benefits to the investors, described in the same form as the foregoing paragraph, and their investments if they are owned or controlled by, not third state's nationals, but only the denying party's nationals. That is to say, the sub-paragraph-2 provision differs from other corresponding formulations in most IIAs that foresees such ownership or control is held by the nationals of a third state, or, more rarely, the nationals of either a third state or denying party. Last, but not least, sub-paragraph 3 of the referred BIT provides "*for the avoidance of doubt*" that "*[t]he benefits of this Agreement shall be denied…*" if the substantive requirements given place in sub-paragraphs (1) have been fulfilled by the submission of claims to arbitration.[143]

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[142] Agreement between the Slovak Republic and the Islamic Republic of Iran for the Promotion and Reciprocal Protection of Investments, adopted on 19 January 2016, https://jusmundi.com/en/document/treaty/en-agreement-between-the-slovak-republic-and-the-islamic-republic-of-iran-for-the-promotion-and-reciprocal-protection-of-investments-iran-islamic-republic-of-slovakia-bit-2016-tuesday-19th-january-2016 (accessed on 22 August 2022) (Iran-Slovakia BIT (2016)), as cited and examined in, Mistelis / Baltag (Investment Treaty Arbitration), p. 9.

[143] Article 8 of the Iran-Slovakia BIT (2016) reads as the following:

> *"1. The benefits of this Agreement shall be denied to an investor of the Home State that is an enterprise of the Home State and to investments of that investor if natural persons or*

Article 13(2) of the BLEU Model BIT (2019),[144] provides the same provision as that included in above-analyzed Article 8(3) of Iran-Slovakia BIT (2016), while Article 13(1) in the BIT spells out the DOB requirements in line with the traditional and established wording.[145]

In certain BITs concluded in the last decade, the attempt to clarify, qualify, and/or define the terms used in traditional formulation has been observed.

The last DOB clause to be addressed here is that of the Colombia Model BIT (2017),[146] which exemplifies the evolutionary change of such provisions. The referred clause seems to be the widest and most inclusive one among the modern DOB clauses in terms of substantive requirements. The clause—including the customary

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> *enterprises of a non-Contracting Party own or control such enterprise or any part of it and the Host State:*
> *a) does not maintain* ***diplomatic relations*** *with the non-Contracting Party;* ***or***
> *b) adopts or maintains* ***measures*** *with respect to the non-Contracting Party or a natural person or enterprise of the non-Contracting Party that prohibit transactions with such natural person or enterprise or that would be violated or circumvented if the benefits of this Agreement were accorded to such investor or to its investments.*
> *2. The benefits of this Agreement shall be denied to an investor of the Home State that is an enterprise of the Home State and to investments of that investor if natural persons or enterprises of the Host State own or control the enterprise or any part of it.*
> *3. For avoidance of any doubt the benefits of this Agreement shall be denied if the preconditions set down in paragraph 1 are fulfilled at time when the claim is submitted pursuant to Article 17."* [Emphasis added]. See, *Ibid.*

[144] Article 13(2) of the BLEU Model BIT (2019) reads as the following: "*For avoidance of any doubt, the benefits of this Agreement shall be denied if the preconditions set down in paragraph 1 are fulfilled at time when the claim is submitted pursuant to Article 19 (D).*" See, *supra* fn. 147.

[145] Article 13(1) of the BLEU Model BIT (2019) reads as the following:

> *"1. A Contracting Party* ***may deny*** *the benefits of this Agreement to* ***an investor of the other Contracting Party*** *that is* ***an enterprise*** *of that Contracting Party* ***and to investments of that investor if****:*
> *(a) the investors of a non- Contracting Party own or controls the enterprise; and*
> *(b) the denying Contracting Party* ***adopts or maintains a measure*** *with respect to the non-Contracting Party, or a natural person, or an enterprise of the non-Contracting Party that:*
> *a. are related to the maintenance of* ***international peace and security****;*
> *b.* ***prohibit transactions*** *with such natural person or enterprise* ***or would be violated or circumvented*** *if the benefits of this Chapter were accorded to the investor or to its investments."* [Emphasis added]

See, *supra* fn. 147.

[146] Bilateral Investment Treaty Between the Republic of Colombia and […], adopted in 2017, https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/6082/download (accessed on 22 August 2022) (the Colombia Model BIT (2017)).

requirements in sub-paragraphs 1(a) and 1(c), though—adds many new and rarely witnessed circumstances where the treaty benefits may be denied to putative investors and their investments.

First, sub-paragraph 1(b) subsumes the following under the denied investor category: the investors in the form of enterprise (as defined in the BIT) of the other party and its investments (as defined in the BIT), if the referred enterprise is owned or controlled by third-state investors and are without the authorization required under the referred Article dealing with "*[c]laims presented by shareholders to an [e]nterprise.*" For the sake of clarity, the referred Article on the shareholders' claims sets forth the conditions for the shareholders to be of the capacity to present their claims—i.e., written consent of the enterprise including the acknowledgement of power of attorney, and several forms. Second, under sub-paragraphs 1(d) and 1(e), which seem to be interrelated and complementary in terms of their motive, the involvement in the there-listed crimes, violations, and conducts that had been proven or decided by judicial authorities is considered as a requirement for the denial of the treaty benefits.[147]

[147] The referred provisions read as follows:

> *"d. an investor of the other Contracting Party, in case that an international court or a judicial or administrative authority of any State with which the Contracting Parties have diplomatic relations has proven that such investor has directly or indirectly:*
> *i. committed serious human rights violations;*
> *ii. sponsored persons or organisations sentenced because of serious human rights violations or violations against International Humanitarian Law or sponsors internationally-listed terrorist organisations;*
> *iii. caused serious environmental damage in the Territory of the Host Party;*
> *iv. committed serious fraudulent actions against the tax and fiscal laws and regulations of the Host Party;*
> *v. committed acts of corruption against the laws of the Host Party; vi. caused grave violations of the Host Party's labour laws; vii. engaged in money laundering activities; or*
> *e. an investor of the other Contracting Party, in case that a court of law in the Host Party has found such investor, or the directives or high executives of an investor who is an Enterprise, or the directives or high executives of the Investment which is an Enterprise, responsible for the violation of the Host Party's criminal laws, in connection with its functions as directives or high executives of such Enterprises"* See, *Ibid.*

The evolutionary line followed by the above-analyzed examples demonstrates that such evolution is in alignment with the transformation of countries' approach toward the international investment: the progression from protectionist approaches to a more liberal attitudes toward foreign investors.[148] In other words, while the first DOB provisions were formulated in a very broad way aiming at restricting treaty protections' availability to subject-matter investors[149]; the modern formulations usually have the type of wording with more detailed and expanded requirements including more qualified terms, which seem to be aiming at the interpretation and application of such provisions to be more accessible and predictable.[150]

However, as it will be analyzed in the following Chapter, in spite of the established wording and components included in such clauses, investment arbitration practice regarding their interpretation and implementation is far from being harmonious.[151]

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[148] Mistelis / Baltag (Investment Treaty Arbitration), p.11.
[149] *Ibid*.
[150] *Ibid*., p. 38.
[151] *Ibid*., p. 13; Côté, p. 5.

CHAPTER 2

QUESTIONS AS TO THE APPLICATION OF DOB CLAUSES IN PRACTICE

Notwithstanding the fact that DOB provisions in IIAs have been evolving into a more and more harmonized form, both in terms of their wordings and requirements, their interpretation and application by different tribunals may remarkably diverge on numerous grounds.[152] In the words of the *Ampal v. Egypt* tribunal:

> "*The Tribunal's review reveals that different tribunals have reached diverging decisions as to when, how and with what effect such clauses can be invoked.*"

This specifically reveals itself in the distinction of the ECT and non-ECT jurisprudences.[153] Besides, such divergence would arguably undermine one of the very purposes of IIAs: the provision of predictability to foreign investors.[154]

Some certain factors could be considered to be causing the foregoing. First, and most importantly, *stare decisis* doctrine is not prevalent in the international investment arbitration system: investment arbitral tribunals are not bound to follow the precedents created by previous tribunals.[155] Nevertheless, precedents are taken into account by tribunals with the purpose of providing a more consistent practice on same or similar issues and rules, which arguably provide a predictability to investors.[156] At

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[152] *Ampal v. Egypt*, para. 127.
[153] In the same line, see, *Ampal v. Egypt*, para. 128.
[154] Verburg, p. 427.
[155] It is argued in the literature that, although a certain degree of predictability in the interpretation and application of IIAs is desirable, the pursuit of "absolute consistency" could jeopardize the evolving characteristics of law and result in unfair consequences, specifically with respect of the substantive standards of investment protection. Hence, the implementation of *stare decisis* doctrine seems not to be a notion entirely supported in the literature. In the same line, for example, see, Verburg, p. 427.
[156] In the same direction, see, *Khan Resources*, para. 417.

this juncture, in the following parts, the grounds, on which the divergences emerge, will be addressed.

I. Implications of DOB Clauses: Jurisdiction v. Admissibility

In numerous arbitral decisions, specifically those applying the ECT, whether DOB clauses cover only substantive benefits or its invocation may also concern the procedural remedies provided by such treaties has been a contentious point.[157] The implications of such difference manifest themselves in the discussion on the basis the invocation of DOB provisions should be considered: as a jurisdictional or admissibility-related issue.

Whether a matter relates to jurisdiction or admissibility[158] may result in practical consequences of considerable importance.[159] The arbitral decisions on jurisdiction may be challenged and invalidated via the mechanisms provided by

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[157] Baltag (Denial of Benefits), p. 4; Kang, p. 38.

[158] Although this subject is examined both in terms of public and private international law, in this thesis, only investment arbitration-related facets are attempted to be analyzed. For a further analysis from the international public law perspective. *See*, Crawford, J.: Brownlie's Principles of Public International Law, Ninth Edition, Oxford University Press, Oxford, 2019. Also, another notion that has blurred borders with the terms jurisdiction and admissibility is the "*competence*." Since this is not particularly addressed by the relevant literature and most arbitral decisions, it is also excluded from the scope of this part of the thesis. For a meticulous analysis on the subject, see, Heiskanen, V.: *Ménage à trois?: Jurisdiction, Admissibility and Competence in Investment Treaty Arbitration*, ICSID Review, Vol. 29, No. 1, 2014, pp. 231-246. As a decision exemplifying the evaluation of such notion in terms of DOB provisions, see, *Bridgestone v. Panama*, in which the tribunal stated: *"Two initial issues arise in relation to this Objection. The first is whether or not it is an objection that goes to competence. Panama submits that it is; the Claimants submit that it is not. The Tribunal is satisfied that it is. This is because one of the benefits of Chapter 10 is the right to arbitrate. That right is subject to the condition subsequent that it is not removed by a valid denial of benefits."*: *Bridgestone Americas, Inc. and Bridgestone Licensing Services, Inc. v. Republic of Panama*, ICSID Case No. ARB/16/34, Decision on Expedited Objections, 13 December 2017, para. 288, https://jusmundi.com/en/document/decision/en-bridgestone-americas-inc-and-bridgestone-licensing-services-inc-v-republic-of-panama-decision-on-expedited-objections-wednesday-13th-december-2017 (accessed on 22 August 2022) (*Bridgestone v. Panama*).

[159] Paulsson, J.: *Jurisdiction and Admissibility*, Global reflections on international law, commerce and dispute resolution: liber amicorum in honour of Robert Briner (Eds.: Aksen, G. / Briner, R./*et al.*), ICC Publisging, Paris, 2005, p. 601. Also, for further analysis on the referred matter, see, Tiryakioğlu, B.: *Yatırım Tahkiminde (Uyuşmazlık Çözüm Kayıtları Kapsamında) Yetki ve Kabul Edilebilirlik*, Tahkim Anlaşması (Eds.: Balkar, S. / Özdemir Kocasakal, H.), 2020 (Yetki ve Kabul Edilebilirlik).

relevant arbitration rules or national legislations, e.g., the annulment mechanism provided by the ICSID Convention or the setting-aside procedures applied by *lex loci arbitri*;[160] while the decisions with regard to admissibility, so long as the subject-matter dispute falls within the tribunal's jurisdiction, are final as considered within the merits of claims.[161] Therefore, the misclassification of matters brought before tribunals by subsuming the admissibility-related issues under jurisdictional category could lead the decisions on such matters challenged, and thereby jeopardize the party expectations in the way that their disputes to be finally settled by arbitration.[162]

Admissibility, as an issue of merits resembling jurisdiction the most, has been widely compared and contrasted with jurisdiction in the literature and arbitral decisions. Brownlie, examining the issue in the context of interstate claims, human rights litigation, and investor-state arbitration, begins its analysis by indicating that in each and all the foregoing contexts, the party filing a claim—the claimant—needs to "*establish its entitlement to do so, and the continuing viability of the claim itself, before the merits of the claim can be decided.*"[163] In this regard, such claims may face the preliminary objections regarding jurisdiction and/or admissibility.[164] The former aims at ceasing the process entirely by stripping the tribunal of the authority to adjudicate on admissibility and other merits-related questions.[165] On the other hand, admissibility objections, assuming the jurisdiction of the tribunal, set out to get the claims dismissed, which may be justified by the impropriety of rendering a decision on the dispute at any

[160] *Ibid.*, p. 601; Mistelis / Baltag (Investment Treaty Arbitration), p. 18; Côté, p. 11.
[161] Paulsson, p. 601. Also, it should be noted that the finality of decisions on merits is not an absolute notion without exceptions. In some cases, the violation of due process and public policy rules could result in such decisions' being set aside or impede their recognition and enforcement. *See*, Paulsson, J., p. 603. However, for the sake of consistency, such scenarios are not dealt with in detailed in this thesis.
[162] Paulsson, p. 601.
[163] Crawford, p. 667.
[164] Mistelis / Baltag (Energy Charter Treaty), p. 1311.
[165] Crawford, p. 667.

given time.[166] Therefore, it is submitted that the admissibility-related objections may be decided on only upon the affirmation of the tribunal's jurisdiction, and since they have an intimate connection with the merits, they are evaluated as a part of the latter.[167]

For distinguishing them in terms of the reviewability, Jan Paulsson provided the following guideline: if the relevant challenge aims at determining that the claims should and could not have been brought before the present forum, then it is jurisdictional. On the other hand, if such challenge puts forward that such claims "*should not be heard at all (or at least not yet), then it concerns admissibility.*"[168] In this context, the tribunal in *HOCHTIEF v. Argentina*[169] determined that jurisdiction concerned the tribunal itself, while admissibility pertained to claims. Therefore, according to the tribunal, it is possible for a tribunal to decide that a claim within its jurisdiction is inadmissible due to the reasons requiring such effect (e.g., *lis alibi pendens*), or even not to receive such claims within its jurisdiction due to a principal defect in the way such claims are filed before it.[170] Also, the referred tribunal determined that any party's omission of raising objections regarding admissibility would result in its acquiescing in any contradiction with the admissibility requirements.[171]

In a nutshell, while jurisdiction refers to the authority of the tribunal in a case and it essentially depends on the party consents, admissibility deals with if a specific claim is of the characteristics requiring the settlement by the tribunal with jurisdiction

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[166] Paulsson, p. 667.
[167] *Ibid.*
[168] *Ibid.*
[169] *HOCHTIEF Aktiengesellschaft v. Argentine Republic*, ICSID Case No. ARB/07/31, Decision on Jurisdiction, 24 October 2011, https://jusmundi.com/en/document/decision/en-hochtief-aktiengesellschaft-v-argentine-republic-decision-on-jurisdiction-monday-24th-october-2011 (accessed on 22 August 2022) (*HOCHTIEF v. Argentina*).
[170] *Ibid.*, para. 90.
[171] *Ibid.*, para. 94.

at the time of submission.[172] As a result of the foregoing distinction, whether the application of DOB provisions pertains to jurisdiction or admissibility in a case is of serious implications.[173] Such analysis, as indicated in the below-referred decisions, is carried out based on the wording of such clauses and their location in the relevant treaty, which are interpreted in accordance with the customary rules of treaty interpretation codified in the VCLT.[174]

Therefore, and naturally, the relevant jurisprudence has bifurcated depending on specific treaties, specifically as the ECT and non-ECT jurisprudences: while the former qualifies the issue as an admissibility-related matter, the latter—specifically when it comes to the IIAs entered into by the US—considers it to be a jurisdictional issue.[175]

A. ECT Jurisprudence

Plama case[176] of 2005 is the first case addressing the ECT DOB provision in such detail. Although it has resulted in widespread and severe discussions,[177] it has widely been regarded as representing the ECT jurisprudence on the application of Article 17(1), including the jurisdiction v. admissibility question.

The tribunal in the case examined if the respondent's arguments regarding Article 17(1) of the ECT could deprive it of jurisdiction, which was a controversial

[172] Heiskanen, p. 237.
[173] Mistelis / Baltag (Investment Treaty Arbitration), p. 19.
[174] *Ibid.*, p. 2.
[175] Côté, p. 11.
[176] *Plama Consortium Limited v. Republic of Bulgaria*, ICSID Case No. ARB/03/24, Decision on Jurisdiction, 8 February 2005, https://jusmundi.com/en/document/decision/en-plama-consortium-limited-v-republic-of-bulgaria-decision-on-jurisdiction-tuesday-8th-february-2005 (accessed on 22 August 2022) (*Plama*).
[177] Baltag (Denial of Benefits), p. 1; Ramachanderan, p. 214, n 8.

topic between the disputing parties.[178] The respondent based its argument, first, on the contention that "*there could be no dispute over*" its ECT Part III obligations in the case where the claimant is destitute of the advantages corresponding to them. Also, in the respondent's view, the denial rights provided by Article 17 would cover all the advantages in relation to Part III: it would encompass those benefits provided by Part III directly and other Parts when they have a liaison with Part-III advantages. Therefore, according to the respondent, the ISDS mechanism set forth under Article 26 in Part V should have been considered within such scope since it enabled the invocation of the Part III advantages through arbitration.[179]

At this juncture, one may need to recall the relevant formulations in the ECT: Article 17(1), taking part in the ECT Part III and titled "*Investment Promotion and Protection,*" begins with the wording "*[e]ach Contracting Party reserves the right to deny* ***the advantages of this Part****...*" [Emphasis added]; while Article 26, included in the ECT Part V and titled "*Dispute Settlement,*" states that it concerns the disputes arising between a contracting party and an other-party investor with regard to its investment in the territory of the former in relation to "*an alleged breach*" of obligations included in Part III.

The tribunal observed that the language of Article 17(1) unambiguously referred to the advantages provided by the ECT Part III, which, in the tribunal's view, was supported by its title—*Non-Application of Part III in Certain Circumstances*—as well.[180] Therefore, interpreting the foregoing "*in good faith in accordance with their ordinary contextual meaning,*" that is, in accordance with Article 31(1) of the VCLT,

[178] *Plama*, para. 146.
[179] *Ibid.*, para. 146.
[180] *Ibid.*, para. 147.

the tribunal found that the DOB rights would only cover the Part III advantages, and reading a reference to Article 26 in Part V into the provision would be "*a gross manipulation of the language.*"[181]

The tribunal, considering if the object and purpose of the ECT would authorize such manipulation, arrived at the conclusion that the ISDS clause (i.e., Article 26) was consciously not given place in Part III. Therefore, in its view, the ECT's approach toward the DOB mechanism should have been considered in the way not excluding the relevant category of investors from the whole advantages of the treaty but a part of such advantages (i.e., those in Part III).[182] In other words, it was observed that such language and structure of the ECT would allow an ISDS process resolving if the DOB rights could have been exercised in any particular case. Therefore, given that the language could easily be constructed otherwise, the tribunal determined that the ECT's object and purpose was in the direction where the ISDS mechanism would not be affected by the exercise of the DOB rights.[183]

Reasoning the foregoing, the tribunal referred to the potentially "*wide-ranging, complex and highly controversial*" disputes that may arise with regard to the effective exercise of the DOB rights in any case, specifically in relation to the fulfillment of the substantive and procedural requirements foreseen under Article 17 of the ECT.[184] Such disputes would and could not be resolved by any adjudicative authorities if Article 26 is deemed to take part within the scope of Article 17, assessed by the tribunal. In such cases, putative investors even would be deprived of the opportunity to get their requests for arbitration registered by arbitral institutions, which would result in the

[181] *Ibid.*
[182] *Ibid.*, para. 148.
[183] *Ibid.*
[184] *Ibid.*, para. 149.

circumstances where the denying party could play the role of "*the judge of its own cause,*"[185] based on which the tribunal found "*[t]hat is a license for injustice; and it treats a covered investor as if it were not covered under the ECT at all.*"[186] As a result of the foregoing reasoning, the *Plama* case tribunal established that, under the ECT, the DOB rights is an issue of admissibility, rather than jurisdiction.

In line with and by referring to the *Plama* tribunal, the tribunal in the *Yukos* cases also addressed the jurisdiction v. admissibility question before proceeding to its detailed analysis on the requirements of the ECT DOB clause. The tribunal, with a shorter analysis, set forth that Article 17(1) and its title explicitly referred to the advantages provided by Part III, and the ISDS provision took part in Part V that is outside the scope of the DOB provision. Since the claimant's entitlement to the Part-III advantages is a matter of merits, rather than jurisdiction, and Article 17 "*exclusively*" covers the benefits brought about by Part III, rather than the whole ECT or Part V, the tribunal adopted the view of the *Plama* case tribunal.[187]

The tribunal in *Ascom v. Kazakhstan* centered its jurisdiction-related scrutiny on the investor definition in Article 1(7) of the ECT and kept the evaluation on the subject

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[185] Mistelis / Baltag (Investment Treaty Arbitration), p. 20.

[186] *Plama*, para. 149. Also, the tribunal supports this view via an argumentation based on the interpretation and application of Article 27 of the ECT—the "*Settlement of Disputes Between Contracting Parties*"—which provides in its first paragraph that "*Contracting Parties shall endeavour to settle disputes concerning the application or interpretation of this Treaty through diplomatic channels,*" and in the second paragraph, if they cannot settle in such way, then they may apply to an ad hoc arbitral tribunal. According to the tribunal, a contracting state's right to apply its rights under Article 27 is independent from the DOB rights of the ECT, and even if Article 26 is admitted being covered by Article 17(1), the home state's right to invoke an arbitration against the denying party and claim for its misapplication of DOB rights is untouched, which was followed by the following determination:

> "***It seems an unnecessarily complicated result to resolve that dispute when, on the ordinary meaning of Article 17(1), the covered investor could invoke Article 26 directly against the host state without the assistance of its home state.*** *The Tribunal notes again that for a covered investor, Article 26 is a very important feature of the ECT; and as a remedy exercisable by an investor by itself and in its own right against the host state, it cannot be equated with Article 27.* ***Under the ECT, the covered investor is more than an object of international law****...*" [Emphasis added]: *Plama*, para. 150.

[187] *Yukos* cases, paras. 441, 443.

limited to whether the claimant fell within such definition or not.[188] In a manner more result-oriented than the previous ones, the tribunal directly excluded Article 17 from its evaluation by emphasizing its irrelevance to such elaboration.[189]

In the same direction, the tribunal in *Khan Resources v. Mongolia* set forth the same line of reasoning. According to the tribunal, the "*ordinary meaning*" of Article 17 would function in the way denying the substantive protections of the ECT Part III to the claimant who would actually be entitled to benefit from them in the absence of such provision. However, in the tribunal's view, such denial would not cover the benefit of arbitration, which is because the application of Article 17 is of merits-related nature, rather than a jurisdictional one.[190]

Explaining the unacceptability of the denying party's being its own judge on claims, the tribunal in *Luxtona v. Russia* provided that it was not the ECT's objective to elevate the respondent to the level where it could be "*its own judge*" of the disputed issues. The tribunal added that the respondent's consent to arbitration, embodied in Article 26(3) of the ECT, unavoidably encompassed the jurisdiction to adjudicate over whether the pre-conditions of such consent existed in a case. Therefore, it concluded that it was within the tribunal's, rather than the respondent's, authority to ascertain and determine whether such conditions given place in the ECT DOB clause are fulfilled or not, in addition to the legal implications following such. As a result, also making a reference to the *Khan Resources v. Mongolia* case, the tribunal ruled that the

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[188] *Ascom Group S.A., Anatolie Stati, Gabriel Stati and Terra Raf Trans Traiding Ltd. v. Republic of Kazakhstan (I),* SCC Case No. 116/2010, Award, 19 December 2013, para. 740, https://jusmundi.com/en/document/decision/en-ascom-group-s-a-anatolie-stati-gabriel-stati-and-terra-raf-trans-traiding-ltd-v-republic-of-kazakhstan-award-thursday-19th-december-2013#decision_245 (accessed on 10 August 2022) (*Ascom v. Kazakhstan*).

[189] The tribunal stated that, "*Article 17 ECT, as clearly indicated by its introductory words "of this part", only applies to Part III of the ECT, leaving unaffected the dispute resolution provision in Part V with Art. 26 ECT.*": *Ascom v. Kazakhstan*, para. 745.

[190] *Khan Resources*, para. 411.

application of the ECT DOB clause would be of not jurisdictional nature, but merits-related characteristics.[191]

Thus, Article 17(1) of the ECT, as a provision limiting its application to the ECT Part III where only the substantive protections take part, has been regarded to be excluding the ISDS mechanism of the ECT, which is foreseen under Article 26 in Part V. Therefore, the invocation of DOB rights is considered as an admissibility issue, rather than a jurisdictional one. However, one must recall that such conclusion is drawn from the above-included language of Article 17(1), which may vary in other treaties.

B. Non-ECT Jurisprudence

The tribunal in *Generation Ukraine v. Ukraine*, a US-Ukraine BIT case under ICSID Arbitration Rules 1984, determined that the invocation of DOB rights under the BIT's DOB clause did not result in "*a jurisdictional hurdle*" for the prudent investor to deal with, but it simply provided "*a potential filter*" to the respondent party for the admissibility of claims raised by the claimant.[192] In the foregoing case, the tribunal seems to reach a conclusion different than the following ones although the applicable IIA included the same formulation of DOB provision.[193]

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[191] *Luxtona Limited v. The Russian Federation*, PCA Case No. 2014-09, Interim Award on Respondent's Objections to the Jurisdiction of the Tribunal, 22 March 2017, para. 239, https://jusmundi.com/en/document/decision/en-luxtona-limited-v-the-russian-federation-decision-on-jurisdiction (accessed on 10 August 2022) (*Luxtona v. Russia*).

[192] *Generation Ukraine Inc. v. Ukraine*, ICSID Case No. ARB/00/9, Award, 16 September 2003, para. 15.7, https://jusmundi.com/en/document/decision/en-generation-ukraine-inc-v-ukraine-award-tuesday-16th-september-2003 (accessed on 10 August 2022) (*Generation Ukraine v. Ukraine*).

[193] The referred DOB provision under Article 1(2) of the US-Ukraine BIT reads as the following:

> *"Each party reserves the right to deny to any company the advantages of this Treaty if nationals of any third country control such company and, in the case of a company of the other Party, that company has no substantial business activities in the territory of the other Party or*

The tribunal in *Ulysseas v. Ecuador*, evaluating the DOB provision under Article 1(2) of the US-Ecuador BIT,[194] entered into force on 11 May 1997, assessed that the advantages subjected to the denial rights under the provision was covering all BIT benefits, one of which was arbitration. Therefore, it came to the conclusion that the effective exercise of such rights would deprive the tribunal of jurisdiction.[195]

In *Guaracachi v. Bolivia*, Article 12 of the US-Bolivia BIT (1998), applied. The provision, beginning with the wording "*[e]ach Party reserves the right to deny to a company of the other Party the benefits of this Treaty if…*", was interpreted by the tribunal in the way that the exercise of the DOB rights would result in its lack of jurisdiction, as a part of the benefits denied by the respondent—that is, benefit to arbitrate.[196] Going a step further, the tribunal addressed and resolved a logical question in such cases: the submission of such jurisdictional objections would itself constitute the reason the tribunal is deprived of its jurisdiction. Referring to this matter, the

> *is controlled by nationals of a third country with which the denying Party does not maintain normal economic relations."*

See, Treaty Between Ukraine and the United States of America Concerning the Encouragement and Reciprocal Protection of Investments, adopted on 4 March 1994, https://jusmundi.com/en/document/treaty/en-treaty-between-the-united-states-of-america-and-ukraine-concerning-the-encouragement-and-reciprocal-protection-of-investments-ukraine-united-states-of-america-bit-1994-friday-4th-march-1994 (accessed on 10 August 2022) (the US-Ukraine BIT).

[194] The referred Article 1(2) reads as the following:

> "***Each Party reserves the right to deny to any company the advantages of this Treaty*** *if nationals of any third country control such company and, in the case of a company of the other Party, that company has no substantial business activities in the territory of the other Party or is controlled by nationals of a third country with which the denying Party does not maintain normal economic relations.*" [Emphasis added].

See, Treaty between the United States of America and the Republic of Ecuador concerning the Encouragement and Reciprocal Protection of Investments, adopted on 27 August 1993, https://jusmundi.com/en/document/treaty/en-treaty-between-the-united-states-of-america-and-the-republic-of-ecuador-concerning-the-encouragement-and-reciprocal-protection-of-investments-ecuador-united-states-of-america-bit-1993-friday-27th-august-1993 (accessed on 10 August 2022) (the US-Ecuador BIT).

[195] *Ulysseas, Inc. v. The Republic of Ecuador*, PCA Case No. 2009-19, Interim Award, 28 September 2010, para. 172, https://jusmundi.com/en/document/decision/en-ulysseas-inc-v-the-republic-of-ecuador-interim-award-tuesday-28th-september-2010 (accessed on 10 August 2022) (*Ulysseas v. Ecuador*).

[196] Baltag (Denial of Benefits), p. 4.

tribunal found that "*nothing prevents both (the act that forms the basis of the plea and the plea itself) from coinciding as they do here.*"[197]

Therefore, in the non-ECT jurisprudence, where the applicable DOB provisions make a reference to the whole treaty or a part of it—both including the ISDS mechanism provisions inside—tribunals seem to be more likely to regard the benefit to arbitration as a treaty advantage that is covered by such DOB clauses.

At this point, regardless of the adopted approach—i.e., subsuming the exercise of DOB rights under either jurisdiction or admissibility—it is submitted in the literature that the ISDS mechanism would be accessible to putative investors by tribunals' implementation of the separability of arbitration agreements. Therefore, in such way, the tribunals could have the opportunity to scrutinize if such rights were exercised in accordance with the corresponding provisions in relevant IIAs or not.[198]

Also, it is argued that in either way of interpretation, tribunals are in charge of evaluating the invocation of such provisions: they will only differ in carrying out such evaluation and render the relevant decision in the merits stage or beforehand as a part of jurisdiction-related scrutiny on the basis of *kompetenz-kompetenz* principle.[199]

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[197] *Guaracachi America, Inc. and Rurelec PLC v. The Plurinational State of Bolivia*, PCA Case No. 2011-17, Award, 31 January 2014, para. 381, https://jusmundi.com/en/document/decision/en-guaracachi-america-inc-and-rurelec-plc-v-the-plurinational-state-of-bolivia-award-friday-31st-january-2014 (accessed on 10 August 2022) (*Guaracachi v. Bolivia*).

[198] Mistelis / Baltag (Investment Treaty Arbitration), p. 22, fn. 45.

[199] Baltag (Denial of Benefits), p. 5; Mistelis / Baltag (Energy Charter Treaty), p. 1318. Although tangential to the referred discussion, the tribunal in *AMTO v. Ukraine* carried out a discussion over the relationship between the exercise of DOB rights and the application of the *kompetenz-kompetenz* principle, setting forth a hybrid approach toward the provision and providing the following: The respondent set forth that the application of Article 17(1) rights are within the scope of the host state rights under the ECT, and Article 26 only concerns the violation of the host state's obligations taking part in Part III; therefore, the host state's denial of benefits under the ECT is not within the scope of arbitration foreseen under Article 26, and the tribunal did not have jurisdiction *rationae materiae* in the case. However, based on the *kompetenz-kompetenz* principle, the tribunal ruled that the host state's qualification of such exercise does not "*detach it from the [c]laimant's assertion of the existence and breach of an obligation,*" and it is within the jurisdiction of the tribunal as a facet of the dispute. See, *AMTO v. Ukraine*, para. 60. Such approach of the referred tribunal was, on one hand, submitted to be

However, on the other hand, one should not overlook the fact that such difference is argued to have the consequences that are more extensive than the timing of the relevant examination, which were described at the beginning of this part in relation to the reviewability of decisions.[200]

Regardless of the adopted approach in terms of jurisdiction v. admissibility question, a tribunal would, in either case, need to determine if the claimant is within the scope of DOB provision or not: whether the substantive DOB requirements are met in a case or not.

II. Substantive Requirements of DOB Clauses: The Investors Subject to DOB

Depending on the treaty language applicable to the case in concern, most IIAs include two substantive DOB requirements regarding putative investors, which are the ownership or control by a third-state national and the lack of substantial business activities in the home state where such investor is constituted or incorporated. Also, in some DOB provisions, the second limb is replaced or alternatively substituted by the diplomatic and/or economic relation requirements, which refers to the cases where the denied investors or investments are under the ownership or control of the nationals of a third state, with whom the denying party does not hold normal diplomatic and/or economic relations.[201] For the sake of practicality, these requirements will hereinafter be referred to as "corporate substantive requirements" and "diplomatic substantive requirements" respectively in this part.

"...a well-balanced approach of the respective rights of the host state and the foreign investor..."; while, on the other hand, its getting adopted within the text and context of other IIAs was found to be questionable. See, Côté, p. 11.

[200] In the same line, see, Roe / Happold / Dingemans, pp. 82-83.

[201] Mistelis / Baltag (Investment Treaty Arbitration), p. 31.

In terms of the interpretation and application of such requirements, the ECT and non-ECT jurisprudences seem not to have any structural and essential divergences, as opposed to the jurisdiction v. admissibility matter and the procedural requirements analyzed under the following parts of this thesis.

As regards each of the corporate and diplomatic substantive requirements, their established formulation in IIAs seems to bring about a cumulative application of their components.[202]

According to the tribunal in the *Plama* case, being owned or controlled by the citizens or nationals of a third state—which was qualified as "*limb i*" by the tribunal—and the lack of "*substantial business activities in the Area of the Contracting Party in which it is organized*"—which was qualified as *"limb ii"*—were both required to be fulfilled due to the conjunction *"and"* linking the referred limbs. The tribunal continued with the same analysis regarding Article 17(2) of the ECT, which sets forth the diplomatic substantive requirements for investments.[203]

The tribunal in *Ulysseas v. Ecuador*, reached the same conclusion applying another treaty in the case, the US-Ecuador BIT (1993).[204] Applying the interpretation rules taking part in Article 31(1) of the VCLT, the tribunal found that both corporate

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[202] *Ibid.*, p. 32.

[203] *Plama*, para. 143. Also, the same line of reasoning and conclusion was followed by the tribunals of the following cases: *Yukos* cases, para. 460; *AMTO v. Ukraine*, para. 62; *Luxtona v.* Russia, para. 238; *Masdar Solar & Wind Cooperatief U.A. v. Kingdom of Spain,* ICSID Case No. ARB/14/1, Award, 16 May 2018, para. 251, https://jusmundi.com/en/document/decision/en-masdar-solar-wind-cooperatief-u-a-v-kingdom-of-spain-award-wednesday-16th-may-2018 (accessed on 10 August 2022) (*Masdar v. Spain*).

[204] Article 1(2) of the US-Ecuador BIT (1993) reads as the following:

> "***Each Party reserves the right to deny*** *to* ***any company*** *the advantages of this Treaty* ***if nationals of any third country control such company*** ***and****, in the case of a company of the other Party,* ***that company has no substantial business activities*** *in the territory of the other Party* ***or*** *is* ***controlled by*** *nationals of* ***a third country*** *with which the* ***denying Party*** *does* ***not maintain normal economic relations****.*" [Emphasis added]. See, *supra* fn. 227.

and diplomatic substantive requirements' components should have been present in the case for the respondent to be able to exercise its DOB rights.[205]

Therefore, as a result, the IIAs with identical conjunctions as above, i.e., "*and*," are likely to be interpreted in the way providing cumulative elements within the referred substantive requirements.

At this juncture, the main components of the referred requirements need to be addressed in more detail. However, before it, one must note that such components seldomly find a place for their definitions in IIAs, and tribunals are not inclined to provide universally adoptable definitions therefor.[206]

A. Ownership and Control by Third-State Nationals

Ownership and control concepts take part in both corporate and diplomatic substantive requirements of DOB clauses, which require the covered investor to be owned or controlled by a third-state, and/or sometimes denying-party, nationals, in addition to the substantive business activity or diplomatic relation-related pre-conditions.

Normally, the prevailing rule in international public law requires that the corporate entity itself and controlling shareholders are considered detached, as established by the seminal decision on the *Barcelona Traction* case before the ICJ.[207] Within the context of the *Barcelona Traction*, the state of incorporation is the decisive

[205] *Ulysseas v. Ecuador*, para. 167.
[206] Mistelis / Baltag (Investment Treaty Arbitration), pp. 32-33.
[207] *Barcelona Traction, Light and Power Company, Limited (Belgium v. Spain) (New Application: 1962),* Judgment - Second Phase, 5 February 1970, https://jusmundi.com/en/document/decision/en-barcelona-traction-light-and-power-company-limited-belgium-v-spain-new-application-1962-judgment-second-phase-thursday-5th-february-1970 (accessed on 22 August 2022) (*Barcelona Traction*).

factor in the ascertainment of corporate nationality, and the nationality of the shareholders of a corporation is not considered in such determination. This has also been adopted by the vast majority of IIAs in the provisions defining covered investors—with numerous exceptions, though. At this point, the DOB clauses are considered to be the sole exception to such principle in the way functioning in favor of states.[208] Therefore, the ownership and control requirement elaborated on in this section serves such purpose.

In some IIAs, a specific definition is assigned to the notions of ownership and control. Going through the IIAs, whose DOB provisions are examined under the previous Chapter, several of such definitions are as the following:

In Article 1(e) of the US-Panama BIT (1982), the term *"own and control"* was defined as the "*ownership or control exercised through subsidiaries or affiliates, wherever located.*"[209] In this definition, it seems that the mechanism of such ownership

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[208] Côté, p. 1. Other exceptions emerge, firstly, in the definition of investors covered by IIAs when they take such control, in the way of indirect ownership of investments, into account in the relevant determination. Also, second, for such control mechanism to be considered within the diplomatic protection context, the corporate entity is required to cease its existence in the country of incorporation for the reasons other than the subject-matter of such diplomatic protection. Third, the ILC has proposed that the "*real state of management and financial control of a corporation*" should have the right to carry out diplomatic protection if the relevant corporate entity is destitute of any substantial business activity in the state of incorporation. See, ILC (International Law Commission) Draft articles on Diplomatic Protection with Commentaries, adopted on 9 August 2006, Article 9, https://jusmundi.com/en/document/rule/en-ilc-international-law-commission-draft-articles-on-diplomatic-protection-with-commentaries-ilc-draft-articles-on-diplomatic-protection-with-commentaries-wednesday-9th-august-2006 (accessed on 22 August 2022) (Draft Articles on Diplomatic Protection). Fourth, the case of "*Calvo corporations,*" required to be established in the country of incorporation for the conduct of relevant businesses, is another exception to such rule in terms of the diplomatic protection provided by the state of shareholders' nationality. See, Draft Articles on Diplomatic Protection, Article 11(b). Such circumstances referred to in the third exception were also recognized by ICSID Convention by the way of enabling party states to agree on the piercing the corporate veil for providing foreign shareholders with the access to the ISDS mechanism, under its Article 25(2)(b). As specifically determined by the tribunal in *Tokios Tokelès* (see, *Tokios Tokelès*, para. 46) the referred ICSID Convention provision results in the extension of jurisdiction in such corporations' favor. This finding could be extended to the other circumstances referred to here, in other words, such exceptions to the *Barcelona Traction* rule are all in favor of the corporate entity side. See, also, Côté, pp. 1-2.

[209] See, *supra* fn. 132.

or control is highlighted, instead of providing its substantive context. The US-Egypt BIT (1982) also adopted the same approach and stated that "*ownership or control*" would include the direct or indirect "*ownership or control exercised through subsidiaries or affiliates*."[210]

Article 1(3) of Australia-Czech Republic BIT (1993), entered into force on 29 June 1994, while not providing a definition, included a rule of factual interpretation on the circumstances where such control exists. It stated that having "*a substantial interest in the other company or the investment*" would be considered as control over a company or investment.[211]

Some IIAs, although not providing a precise definition on the ownership and control notions, set forth numerous factors within other concepts, which could be benefited from for establishing an inference about the components of ownership and control notions under such treaties.

For example, CUSMA includes a definition for the term "*state-owned enterprise*" in Article 22.1 under Chapter 22, and provides a non-exhaustive list of criteria to determine whether an enterprise is a state-owned enterprise or not.[212] The referred provision deals with the state-owned enterprises, which are, by definition, the

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[210] See, *supra* fn. 135.

[211] The referred clause reads as the following: "*For the purposes of this Agreement**, a natural person or company shall be regarded as controlling** a company or an investment **if** the person or company **has a substantial interest in the other company or the investment**.*" [Emphasis added]. See, *supra* fn. 134.

[212] The referred clause reads as the following:

> ***"[S]tate-owned enterprise means*** *an enterprise that is principally engaged in commercial activities, and* ***in which a Party****:*
> *(a)* ***directly or indirectly*** *owns* ***more than 50 percent of the share capital****;*
> *(b)* ***controls, through direct or indirect ownership interests****, the exercise of* ***more than 50 percent of the voting rights****;*
> *(c)* ***holds the power to control*** *the enterprise* ***through any other ownership interest, including indirect or minority ownership****; or*
> *(d) holds* ***the power to appoint a majority of members of the board of directors*** *or any other* ***equivalent management body****."* [Emphasis added]

See, *supra* fn. 158.

enterprises under the party states' ownership and/or control. Therefore, it would not be unreasonable to generalize such factors in the way to apply to determine such ownership and control by third-state nationals over investments and investors as well. In this sense, this definition seems to take, *inter alia*, direct or indirect ownership of shares, voting rights, and the power to determine the management of such enterprises into account while determining the existence of ownership and/or control over the referred enterprises.

In the ECT, the notion of control is not defined in terms of its implications under Article 17. However, Understanding[213] no. 3 to Article 1(6), the definition of the term *"investment,"* brings about a guideline on the concept, and provides a non-exhaustive list of criteria to determine the control in terms of the ECT definition for investment.[214]

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[213] At this point, the definition of such "Understandings" may be necessary. The European Energy Charter Conference, held in Lisbon on 16-17 December 1994, opened "Final Act of the European Energy Charter Conference" for signature on 17 December 1994 (hereinafter referred to as the "Final Act"), in which the ECT itself took place as Annex A. For the complete text of the Final Act, see, https://www.energychartertreaty.org/provisions/final-act-of-the-european-energy-charter-conference/#:~:text=I.,on%2016%2D17%20December%201994 (accessed on 22 August 2022). The Final Act also included numerous Understandings, under its Section IV, with regard to the ECT as a whole or certain clauses, which were adopted by all the signatory parties to the Final Act. Therefore, such Understandings are considered to be agreements "*relating to the treaty which was made between all the parties in connection with the conclusion*" thereof, which is accepted to be within the "*context*" of a treaty "*for the purpose of the interpretation of*" such treaty under Article 31(2)(a) of the VCLT. See, Roe / Happold / Dingemans, p. 20. To be more precise, such context is taken as a basis for the general rule of interpretation under Article 31(1) of the VCLT, which sets forth: "***A treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context*** *and in the light of its object and purpose.*" [Emphasis added]. See, *supra* fn. 69.

[214] The referred Understanding No. 3 reads as the following:

> "*For greater clarity as to whether an Investment made in the Area of one Contracting Party is controlled, **directly or indirectly**, by an Investor of any other Contracting Party, **control of an Investment means control in fact, determined after an examination of the actual circumstances in each situation**. In any such examination, **all relevant factors should be considered, including the Investor's***
> *(a) **financial interest**, including equity interest, in the Investment;*
> *(b) ability **to exercise substantial influence over the management and operation** of the Investment; and*
> *(c) ability to exercise **substantial influence over the selection of members of the board of directors or any other managing body**.*
> ***Where there is doubt** as to whether an Investor controls, directly or indirectly, an Investment, **an Investor claiming such control has the burden of proof** that such control exists.*"[214] [Emphasis added].

The referred Understanding, defining the direct or indirect control over an investment, refers to the notion of "*control in fact,*" and reasonably requires a case-by-case determination based on the non-exhaustively listed factors; such as, in a very briefly manner, financial interests and the degree of influence over the management of the investment. At the end, the burden of proving that such control exists rests with the claimant. Although the purpose of such Understanding is limited to the interpretation of Article 1(6) of the ECT, defining the covered investments, it is submitted that it would operate as a "*guidance to understand the drafter's notion of 'control'.*"[215]

As a result, in addition to the fact that a considerable number of IIAs do not provide a specific definition assigned to the terms of ownership and/or control, the ones with such definitions include a reference to the case-by-case analysis for such determination. Therefore, it becomes for tribunals to ascertain the ownership and/or control requirements in terms of form and essence. In such context, even the determination of real controllers may, itself, be challenging due to the complexity of corporate structures and the globally prevailing legal environment with permissive attitude toward the change of such structures very easily and frequently.[216]

In the ECT cases surveyed in this thesis, tribunals seem to be inclined to follow the reasoning adopted by the tribunal in the *Plama* case. In the referred case, the tribunal attached importance to the conjunction *"or,"* between the terms *"own"* and *"control,"* in Article 17(1) of the ECT, and it interpreted that in the way signifying such legal statuses were alternatives. At that point, the tribunal highlighted that such ownership was encompassing the "*indirect and beneficial ownership,*" and referred

See, https://www.energychartertreaty.org/provisions/part-i-definitions-and-purpose/article-1-definitions/ (accessed on 22 August 2022).
[215] Mudliar, p. 255.
[216] Mistelis / Baltag (Investment Treaty Arbitration), p. 34

control was meaning "*control in fact*" implying a "*substantial influence*" over the management, operations, and the appointment of managers.[217]

The tribunal in *Ulysseas v. Ecuador* concentrated on the notion of control under the DOB provision of Article 1(2) of the US-Ecuador BIT. After indicating that there had not been any controversies between the parties that such notion referred to the "*legal capacity to control,*" it observed that the difference between them was in relation to whether it covered indirect control together with the direct one or not.[218] Therefore, the tribunal found it necessary to interpret the provision in the light of Article 31(1) of the VCLT: reading "*in their context and in the light of the object and purpose of the treaty.*"[219] Based on such interpretation, the tribunal ruled that the ultimate controller of the claimant and its nationality was the determining factor in the control scrutiny to be carried out under the relevant DOB provision.[220]

B. Substantial Business Activity Requirement

Although the substantive business activity requirement is one of the two main pillars of corporate substantive requirements of DOB clauses, its definition is not given in most traditional IIAs.[221] Potentially due to the foregoing, this is considered to be the most controversial substantive requirement in DOB provisions.[222]

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[217] *Plama*, para. 170.
[218] *Ulysseas v. Ecuador*, para. 168.
[219] *Ibid.*, para. 169.
[220] *Ibid.*, para. 170.
[221] Kang, p. 34. Even the recent BITs providing a specific emphasis on such notion may require a case-by-case analysis. For example, the Canada Model BIT (2021) defining the "*investor of a party*" term under its Article 1 (Definitions) requires the relevant enterprise to have substantial business activities in the home state and provides: *"…A determination of whether an enterprise has substantial business activities in the territory of a Party requires a case-by-case, fact-based inquiry…"* See, *supra* fn. 172.
[222] Côté, p. 14.

One of the model BITs given as an exceptional example in the literature[223] is the Netherlands Model BIT (2019), which provides a definition under its Article 1 (Definitions) on "*substantive business activities.*"[224] The said provision foresees that it is for the tribunals to establish such definition or requirements on a case-by-case basis to determine if the putative investor carries out such business activities in the home state. As will be addressed below, the principal factors considered in such inquiry includes, without limitation, if the entity in question has an office, employees, and bank accounts, etc. in the home state.[225]

Because even the IIAs with substantial business activity definition leave the relevant determination to tribunals, at this point, tribunals' interpretation and application of the subject-matter requirement acquires special significance.

In this sense, the *AMTO v. Ukraine* case provided a widely adopted analysis on the matter.[226] The tribunal, firstly, determined that the application of the ECT DOB

[223] Mistelis / Baltag (Investment Treaty Arbitration), p. 36.

[224] The referred clause reads as the following:

> *"**Indications** of having 'substantive business activities' in a Contracting Party **may include**:*
> *(i) the undertaking's **registered office and/or administration** is established in that Contracting Party;*
> *(ii) the undertaking's **headquarters and/or management** is established in that Contracting Party;*
> *(iii) **the number of employees and their qualifications** based in that Contracting Party;*
> *(iv) **the turnover** generated **in that Contracting Party**; **and***
> *(v) **an office, production facility and/or research laboratory** is established in that Contracting Party;*
> *These indications **should be assessed in each specific case**, taking into account the total number of employees and turnover of the undertaking concerned, and take account of the nature and maturity of the activities carried out by the undertaking in the Contracting Party in which it is established."* [Emphasis added]

Agreement on reciprocal promotion and protection of investments between [...] and the Kingdom of the Netherlands, adopted on 22 March 2019, https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/5832/download (accessed on 22 August 2022) (the Netherlands Model BIT (2019)).

[225] Côté, p. 15.

[226] For the literature and arbitral decisions examining the referred decision, please see, Mistelis / Baltag (Investment Treaty Arbitration), p. 34; *Luxtona v. Russia*, para. 274; *Big Sky Energy Corporation v. Republic of Kazakhstan,* ICSID Case No. ARB/17/22, Award, 24 November 2021, para. 279, https://jusmundi.com/en/document/decision/en-big-sky-energy-corporation-v-republic-of-kazakhstan-

clause would be dependent on whether the claimant had substantial business activities in the country of its organization or not. Within this context, the claimant provided the tribunal with a law firm report concerning its field of activity and conducts, a tax certificate including its paid taxes within the relevant period, its landlord's confirmation of its office rental, and a bank statement confirming the volume and types of transactions carried out by the claimant.[227] The tribunal, evaluating the listed items, observed that there had not been a definition or description of substantial business activity under the ECT and the relevant documents, i.e., the Final Act of the European Charter Conference. At this juncture, it assessed that such characteristics of business activities is to be determined based on the quality, rather than the volume or quantity, of the business in concern: The term "*substantial*" referred to the "*substance*," rather than "*form*," it did not mean "*large*," and the decisive factor would be the "*materiality*," not the "*magnitude*" of the activities in question.[228]

As a result, the tribunal ruled that the claimant in the case had substantial business activity in the home state because such activities were carried out from the premises located in that state by permanent staff, albeit in a limited number.[229] In the referred case, the procedural requirements had not been addressed as the presence of

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final-award-wednesday-24th-november-2021 (accessed on 22 August 2022) (*Big Sky Energy*); *Littop Enterprises Limited, Bridgemont Ventures Limited and Bordo Management Limited v. Ukraine,* SCC Case No. V 2015/092, Final Award, 4 February 2021, para. 616, https://jusmundi.com/en/document/decision/en-littop-enterprises-limited-bridgemont-ventures-limited-and-bordo-management-limited-v-ukraine-none-currently-available-thursday-1st-january-2015#pa_1023251 (accessed on 22 August 2022) (*Littop v. Ukraine*).

[227] *AMTO v. Ukraine*, para. 68.

[228] *Ibid.*, para. 69.

[229] *Ibid.* Similarly, in *Tokios Tokéles*, the tribunal found the "…*financial statements, employment information, and a catalogue of materials produced*…" sufficient for the ascertainment of substantial business activity—it found such ascertainment was irrelevant in the case, though. See, *Tokios Tokéles*, para. 37.

such substantial business activities disenabled the respondent state to exercise its DOB rights under the treaty.[230]

In *Masdar v. Spain*, the respondent put forward that the claimant was a shell company without any "*permanently employed people*" and offices in the home state.[231] The tribunal, observing that the requirement of being owned or controlled by third-state nationals is fulfilled in the case, decided that the critical issue remained at that point was if the claimant had had substantial business activities or not for the fulfillment of the DOB requirements.[232] Referring to the *AMTO v. Ukraine* decision, the tribunal considered the evidence establishing, *inter alia*, that the claimant was "*a holding company with substantial international assets under its control.*" The tribunal found the other facts in the case, for which the claimant submitted, unchallenged: the considerable amount of growth in the business, an office in the home state, home-state national directors participating in board meetings, regular board meetings, the claimant's independence in its financial management and assumption of its own financial risks, and bank accounts set in the home state.[233] Based on the foregoing, in

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[230] *AMTO v. Ukraine*, para. 70; *Luxtona v. Russia*, para. 274.
[231] *Masdar v. Spain*, para. 206.
[232] *Masdar v. Spain*, para. 252.
[233] The full scope of such evidence was well recited and summarized by the tribunal in *Littop v. Ukraine* as the following:

> *"This "unchallenged evidence" provided by the claimant included:*
> *1) the fact that it was "a holding company, which own[ed] major investments" not only in Spain but in other countries too, i.e. "the London Array offshore wind farm and Dudgeon projects, both UK renewable energy projects, and the Tafila wind project in Jordan, all of which [were] high value capital-intensive projects";*
> *2) the fact that it was "demonstrably a business that ha[d] grown in the period of 2008-2014";*
> *3) it had an office in Amsterdam;*
> *4) it had no employees but had two Dutch Directors who were "active participants in Board meetings";*
> *5) the Masdar Board "met at least four times a year in the Netherlands"; its functions included overseeing "the investments and the assets owned by Masdar" for the purpose of ensuring that they were "well funded, well managed" and sometimes would make decisions concerning capital contributions;*
> *6) Claimant enjoyed "autonomy in the financial management of its investments", and assumed "its own financial risks" and issued "guarantees"; and*

the case, it was held that there had been no basis for DOB under the ECT due to the claimant's substantial business activities in the home state.[234]

In the *Littop v. Ukraine*, an ECT case under SCC Arbitration Rules, the claimants, who were the shareholders of a Ukraine-incorporated company Ukrnafta, argued that they had substantial business activity in the home state by meeting the requirements recited in the *AMTO v. Ukraine* and *Masdar v. Spain* cases. In this context, they set forward that they had procured a "*legal and corporate service provider*," in addition to a "*professional services agency*," and they carried out the employment of personnel needed to keep their shareholding in the company on their behalf. Also, the claimants referred to the growth in their business, stemming from their acquiring the shares in the company. More, according to the claimants, they had financial risks due to the contracts they concluded directly, they had bank accounts, and held regular board meetings, each and all of which was proving the substantial business activities in the home country.[235] The tribunal, at that point, needed to distinguish the factual backgrounds of the present case and those in the referred cases.

> *7) Claimant held two bank accounts in the Netherlands with two different banks."* [The underlined emphasis provided by the tribunal].

See, *Littop v. Ukraine*, para. 620.

[234] *Masdar v. Spain*, para. 254.

[235] In the tribunal's wording:

> "*1) their business activities were structured through the engagement of Andreas M Sofocleous & Co (a legal and corporate service provider) and Primecap Cyprus Limited (a professional services agency),329 which employed "the necessary people to ensure that the Claimants hired the necessary legal and other advisors to maintain their shareholding in Ukrnafta";*
> *2) they are "shareholders in a business that grew" following their acquisition of the Ukrnafta shareholding;*
> *3) they assumed financial risk by entering into contracts in their own name (e.g. the 2010 Shareholders Agreement and 2010 Cooperation Agreement);*
> *4) they hold bank accounts in their own name; and*
> *5) their Boards met regularly, passed resolutions which concerned not only "minor administrative points, but also substantive points" such as "in respect of the transfer of shares an (sic) conclusion of trust deeds*". [The underlined emphasis provided by the tribunal].

See, *Littop v. Ukraine*, para. 621.

First, it determined that, unlike *Masdar v. Spain*, where the investor was a holding company with major investments, in the present case the claimants had solely one investment and business activity, which was the shares in the Ukrainian company. Therefore, as opposed to the former, in the latter, what was growing was not the business activity of the investors itself, but the value of the company shares they had acquired. More, the tribunal observed that the shares of the claimants in the company had not increased over time.[236] Also, distinguishing the *AMTO v. Ukraine* case from the present one, the tribunal followed the same argumentation as the foregoing, and it determined that the claimants in the present case could not provide sufficient evidence regarding the facts, based on which the *AMTO v. Ukraine* tribunal would find for substantial business activity in its own case.[237]

As for the assumption of financial risk argument, the tribunal observed that the contracts signed by the claimants in their own name were concluded in Ukraine, rather than the home state. Therefore, unlike *Masdar v. Spain* where such risks were assumed in the home state, such contracts would not be an indicator for such substantial business activities in the home state.[238]

As regards the services claimed to be received by the claimants in the home state—i.e., the services of the "*legal and corporate service provider*" and "*professional services agency*" referred to above—the tribunal stated that there had not been sufficient evidence establishing the performance of the relevant agreements in the home state.[239] Additionally, in the tribunal's view, the financial reports provided by the claimants side, did "*not show any real working staff or employees of the*

[236] *Littop v. Ukraine*, paras. 623-626.
[237] *Ibid.*, para. 627.
[238] *Ibid.*, paras. 636-637.
[239] *Ibid.*, para. 630.

company, no office premises, no salaries and no rent paid" in the state of incorporation.[240]

As a result, the tribunal, distinguishing the present facts from those in the *AMTO v. Ukraine* and *Masdar v. Spain* cases, ruled that the claimants' possession of over 40% shares in Uksnafta, even as a valuable asset, did not amount to a substantial business activity foreseen under the ECT Article 17(1).[241]

Another controversial question that may need to be answered by tribunals from time to time is about the business activities of group company members: Whether the activities of each member separately or the group collectively should be considered.

The tribunal in *Pac Rim v. El Salvador* addressed the foregoing question and responded in the following way: although the group itself had substantial business activities in the home state,[242] the purpose of the CAFTA DOB provision required that the member, i.e., the claimant in the present case, should have such substantial business activities.[243] To this end, in other words, the tribunal provided that the activities of the other members of the claimant's group would not be considered as the enterprise's own activities in the sense of Article 10.12.2 in CAFTA, and their activities could not be utilized to elevate the claimant's activities to the threshold required for the substantial business activities in the case.[244]

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240 *Ibid.*, para. 631.
241 *Ibid.*, para. 638.
242 *Pac Rim Cayman LLC v. The Republic of El Salvador,* ICSID Case No. ARB/09/12, Decision on the Respondent's Jurisdictional Objections, 1 June 2012, para. 4.65, https://jusmundi.com/en/document/decision/en-pac-rim-cayman-llc-v-republic-of-el-salvador-decision-on-the-respondents-jurisdictional-objections-friday-1st-june-2012 (accessed on 5 August 2022) (*Pac Rim v. El Salvador*).
243 Mistelis / Baltag (Investment Treaty Arbitration), p. 35.
244 *Pac Rim v. El Salvador*, para. 4.66.

Thereafter, the tribunal addressed the question if the business activities carried out by the claimant in the home state was substantial or not.[245] While elaborating on this issue, the tribunal noted that the claimant had changed its country of organization from the Cayman Islands to the US, a party state to CAFTA. In the case, it was observed by the tribunal that the principal business activities carried out by the group companies in the home state, i.e., the US, had not belonged to the claimant itself, but to another member of the group.[246] Also, in the tribunal's view, it was possible for traditional holding companies to conduct substantial business activities by realizing such activities within and as required by their *raison d'être* and traditional course of business.[247] However, since the claimant was merely a subsidiary, it was not required in the case to inquire if such business activities were executed by it or not.[248]

The tribunal, based on two final determinations, found that the claimant lacked substantial business activities in the home state: First, even after its country of incorporation had changed to the US, as a party to CAFTA, the scope and volume of its business activities did not change, which were insubstantial against the backdrop of

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[245] See, *Ibid.*, para. 4.66 *et seq.*
[246] *Pac Rim v. El Salvador*, para. 4.71.
[247] The functions and purposes of such holding companies are explained by the tribunal as the following: "*Generally, such holding companies are passive, owing all or substantially all of the shares in one or more subsidiary companies which will employ personnel and produce goods or services to third parties. The commercial purpose of a holding company is to own shares in its group of companies, with attendant benefits as to control, taxation and risk-management for the holding company's group of companies. It will usually have a board of directors, board minutes, a continuous physical presence and a bank account.*" See, *Pac Rim v. El Salvador*, para. 4.72. Also, such finding of the tribunal was submitted to have implications on future arbitrations. See, Badini, p. 300. For example, the referred determination was also recited affirmatively a case under the ECT, and the tribunal in *9Ren Holdings v. Spain* decided that the substantial business activities should have been analyzed based on the characteristics of the business carried out by the putative investor. In this sense such business in relation to holding companies was listed as "*paperwork, board meetings, bank accounts and cheque books.*" See, *9REN Holding S.a.r.l v. Kingdom of Spain*, ICSID Case No. ARB/15/15, Award, 31 May 2019, para. 182, https://jusmundi.com/en/document/decision/en-9ren-holding-s-a-r-l-v-kingdom-of-spain-none-currently-available-tuesday-21st-april-2015 (accessed on 5 August 2022) (*9Ren Holdings v. Spain*). Also, for the criticisms that such approach could result in a two-tier substantial business activity test, which may cause unjust consequences, see, Côté, p. 15.
[248] *Pac Rim v. El Salvador*, para. 4.73.

the CAFTA requirements. Second, the claimant's business activities had not gone beyond having the shares of its subsidiaries in El Salvador. In the tribunal's view, such possession of shares could have been deemed to be a substantial business activity had the claimant been a holding company possessing the shares in the home-state subsidiaries, which was not the case: Even were it considered to be a holding company, its activities solely related to its subsidiaries' activities in El Salvador, not the US as the home state.[249] In other words, according to the tribunal, the crux of the inquiry as to the substantial business activity matter laid in the determination of the claimant's own activities' quality, apart from the question regarding whether such investment results in substantial business activity or not.[250]

Another matter with regard to such inquiry is of temporal nature: when the claimant needs to carry out substantive business activities to avoid the application of DOB provisions. Although it has been a matter of difference between parties, no tribunal up to the present determinatively and conclusively addressed this issue. Besides, it is submitted that such activities at the moment when the arbitration notice is served should have been taken into account since it is the time the consents to the arbitration is completed.[251]

To sum up, considering the above-referred provisions and decisions, the substantial business activity requirement appears to mean that the putative investor is not a mailbox or shell company.[252] In other words, such notion requires a degree of

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[249] *Ibid.*, para. 4.74.
[250] *Ibid.*, para. 4.67.
[251] Côté, p. 16. And, as cited in the foregoing, for the party argumentation concerning such temporal aspect of the issue, see, *EuroGas Inc. and Belmont Resources Inc. v. Slovak Republic*, ICSID Case No. ARB/14/14, Award of the Tribunal, 18 August 2017, para. 281 https://jusmundi.com/en/document/decision/en-eurogas-inc-and-belmont-resources-inc-v-slovak-republic-award-of-the-tribunal-friday-18th-august-2017 (accessed on 5 August 2022) (*EuroGas v. Slovakia*).
[252] Mistelis / Baltag (Investment Treaty Arbitration), p. 35.

activity going beyond the mere corporate existence and exceeding "*substantiality*" threshold of "*any business activity,*" such as concluding and performing transactions, carrying out an employment process, maintaining a management with directors in the home state, the volume of turnover, registered office, facilities and headquarters in the territory of the home state, etc.[253] Besides, the critical aspect of such determination is its being conducted based on "*a factual inquiry*" and on a case-by-case basis.[254] In such elaboration, tribunals' analysis is expected to focus on the genuineness and legitimacy of the activities, rather than their volume and magnitude, which is evaluated to be in alignment with the purpose of DOB provisions; that is, the maintenance of reciprocity.[255]

C. "Third State/Party" Definition

Third state/party concept is given place in both corporate and diplomatic substantive requirements in the way that the denied investor and/or investment is to be under the ownership or control of such third-party/-state nationals. While it has been defined by some of IIAs –or used in a way not resulting in any contentions by and between the parties; in other IIAs, its lack of definition has resulted in controversies, specifically in the interpretation of the ECT DOB clause.

At this point, one may need to distinguish BITs and MIAs in terms of the referred controversies. As for the former, the legal entities under the ownership or control of third state, and sometimes the host state, nationals are included within the scope of DOB provisions, regarding which the meaning of third state is manifest; that is, the

[253] *Ibid.*, pp. 35, 36.
[254] *Ibid.*, p. 36.
[255] *Ibid.*, p. 37; Pang, p. 35.

non-party states.[256] However, the latter is destitute of such clarity on whether such "third state" term only refers to the non-party states or it also covers the party states excepting the host state and the state of incorporation.[257]

Among the MIAs surveyed in this thesis, NAFTA, CAFTA and CUSMA seem not to result in such controversies because they make a reference to the nationals of a "non-Party" in the way excluding the nationals of other parties to such MIAs. Additionally, under CUSMA, the host state was given place alongside such "non-Party," in the way excluding the shell corporations under the ownership and/or control of the host-state nationals, as well. As for CETA—although it only refers to the "third country" in the DOB provision, which might have resulted in the above-referred differences in interpretation like the ECT—its exclusion of shell corporations from the covered investor definition is likely to be interpreted in the way considering such corporations as under the ownership and/or control of non-parties to the treaty.

At this point, the ECT wording and its interpretation present certain intricacies in terms of the question addressed above: whether the term "third-state" also covers the contracting parties other than the home state and host state, in addition to the non-party states.[258]

As for the definition of "third state," the tribunal in *AMTO v. Ukraine* observed that it had not been defined in the ECT. However, it determined that such concept was used as the "*contradistinction to "Contracting Party'*"" under Article 1(7), defining "Investor."[259] That is, while formulating a definition for the concept of "Investor," Article 1(7)(a) refers to the natural and legal persons subsumed under such category

[256] Côté, p. 12.
[257] *Ibid*.
[258] *Ibid.*, p. 13.
[259] *AMTO v. Ukraine*, para. 62.

with respect to a "*Contracting Party*"; and, Article 1(7)(b) states that the preceding definition shall apply to "*third states*" *mutatis mutandis*.

Another arbitral decision, in which the definition and scope of "third state" was discussed in detail, is *Libananco v. Turkey*.[260] In the said case, while elaborating on the meaning and implications of the term, the witness statement of Mr. Craig Bamberger, who is the then chief legal counsel to the IEA and took place in the ECT negotiations, was benefited from.[261] The respondent, the Republic of Turkey, contended that the claimant, Libananco, as a company incorporated in Cyprus, not legally recognized by the Republic of Turkey, was in the category of investors included in Article 17(2) of the ECT; that is, "*an Investor of a third state with or as to which the denying Contracting Party… does not maintain a diplomatic relationship…*". The fundamental difference between the parties was whether or not the third-state term was to be construed within the meaning assigned under Article 7 of the ECT.[262]

Referring to the witness statement referred to above, the tribunal confirmed the following points: The term "third state" was included in various ECT Articles—*Articles l(7)(b), 7(10)(a)(i), 9(1), 10(3), 10(7), 12(1), and 17*. Apart from Article 7, the other provisions had included the wording "*states that is not a Contracting Party,*" which was replaced by the term "third state" at the final phase of negotiations for the

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[260] *Libananco Holdings Co. Limited v. Republic of Turkey*, ICSID Case No. ARB/06/8, Award, 2 September 2011, paras. 551-556, https://jusmundi.com/en/document/decision/en-libananco-holdings-co-limited-v-republic-of-turkey-award-friday-2nd-september-2011 (accessed on 22 August 2022) (*Libananco v. Turkey*).

[261] *Ibid.*, para. 551.

[262] *Ibid.*, para. 551. Also, the referred Article 7 provision reads as follows:

> "*10. **For the purposes of this Article**:*
> *a. **"Transit" means***
> *i. the carriage through the Area of a Contracting Party, or to or from port facilities in its Area for loading or unloading, of Energy Materials and Products originating in the Area of another state and destined for the Area of a third state, **so long as either the other state or the third state is a Contracting Party**; or…*" [Emphasis added]

See, *supra* fn. 5.

sole purposes of drafting concerns—not aiming at any change in meaning. Further, the negotiations of Article 7 and Article 17 were carried out separately.[263] Based on such observations, the tribunal applied the rules of interpretations codified in the VCLT, and it observed that the term "third state" was well recognized and defined in treaty law. Inferring from the use of the term in Section 4 of the VCLT (Treaties and Third States), the tribunal determined that it obviously was used in the meaning "*state not party to the treaty in question*", and such use was in alignment with the developments in the ECT negotiation phases; that is, its replacement the phrase "*state that is not a Contracting Party.*" According to the tribunal, such interpretation was also supported by the context, in which such term was used in the ECT. Within such context, except for Articles 7 and 17, the term "third state" appeared to be used together with the term "Contracting Party/Parties" in the way to provide a contradistinction, from which the tribunal concluded that such use of the term "third state" implied its ordinary meaning in the ECT.[264]

Also, it was found by the tribunal that such use was required by the context of Article 7 that foresaw three actors, which are "*a first state (the state of origin) and a second state (the state whose territory is being transited),*" and a third state that had to be a contracting party for Article 7 to be meaningful and functioning. Moreover, since such definitions were made "*for the purposes of*" Article 7, as stated in the provision, it would not be suitable to transfer such meanings to other Articles, stated by the tribunal.[265]

[263] *Libananco v. Turkey*, para. 552.
[264] *Ibid.*, para. 553.
[265] *Ibid.*, para. 554.

The last argument examined by the tribunal was that it would be possible for Article 17(2) to be of effect only via the interpretation that the term encompass contracting parties as well.[266] The tribunal rejected such argumentation finding it in contradiction with the rationale behind Article 17(2): the investment was foreseen to be made directly by the actors of the ECT contracting parties, while its "*ultimate beneficial owner or controller*" was required to be a national of a third state as set forth under Article 1(7) of the ECT.[267]

Therefore, in the referred case, the tribunal rejected to read the third state contracting parties into the term "third state" in the DOB provision.[268]

III. Procedural Requirements of DOB Clauses

The DOB requirements examined in the previous part were regarding the determination if a putative investor would be subsumed under the denied category of DOB clauses or not. In this part, the procedural requirements that have to be fulfilled by the denying party to be able to invoke DOB rights will be addressed.

A. Automatic Application v. Exercisable Right

Depending on the formulation of DOB clauses, there appears to be a distinction based on whether the relevant rights automatically apply, or they need to be exercised by the right-holder party state. This difference determines, *inter alia*, whether the

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266 *Ibid.*, para. 555.
267 *Ibid.*, para. 556.
268 The same line of reasoning had been followed by the *Yukos* cases in a briefer manner. See, *Yukos* cases, para. 544. Also, for the same conclusion arrived at by the tribunal of the *Plama* case, see, *Plama*, para. 170, where the tribunal stated the following: "*A "third state" being a non-Contracting State under the ECT, it would not include France (as a Contracting State)…*"

denying party may be granted the advantages of such clauses automatically at the time the DOB requirements are met or not.[269]

DOB provisions are subsumed under the said categories based on their wordings. It could be assumed that the denying party must exercise the DOB right if the relevant clause states that such party "*reserves the right to deny*" or "*may deny*" the benefits. To the contrary, when the relevant formulations include the wording requiring such benefits "*shall be denied,*" then such provisions would be deemed to be automatically applying.[270]

As an example of exercisable DOB provisions, Article 17 of the ECT beginning with the wording "*Each Contracting Party reserves the right to deny the advantages of this Part,"* is acknowledged by arbitral tribunals to require the denying party's exercise of there-included rights, with the further reasonings summarized below.

The *Plama v. Bulgaria* tribunal, analyzing the referred article, observed that the existence and exercise of a right are different notions. In other words, there may "*exist*" rights, which are not (*or even will never be*) exercised by the persons possessing it.[271] Upon the foregoing observations, the tribunal added the following as an explanation of the rationale, *i.e, ratio legis*, behind the ECT's approach: Such unambiguous language of Article 17(1) was in alignment with the ECT's approach encompassing a wide spectrum of state policies with regard to the invocation of DOB

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[269] Mistelis / Baltag (Investment Treaty Arbitration), p. 13.
[270] *Ibid.*; *Plama*, para. 156.
[271] *Plama*, para. 155.

rights thereunder, which may have ranged from the most permissive approach to the most restrictive one.[272]

Also, the tribunals of the *Plama v. Bulgaria* and the below-referred *Khan Resources v. Mongolia* cases concurrently pointed out that had the contracting states targeted at automatic application of Article 17 of the ECT, they could easily have drafted the DOB provision in a manner explicitly requiring such[273] or they could have inserted such exceptions into the investor definition, under Article 1(7).[274]

The *Plama* case tribunal referred to Article 6 of the ASEAN Framework Agreement on Services of December 1995 to demonstrate such automatic-application formulations had already been adopted in practice: "*The benefits of this Framework Agreement shall be denied to a service supplier who…*" As a result, the tribunal ruled that it would not be a proper approach under such circumstances to "*re-write Article 17(1) ECT in the Respondent's favor.*"[275]

The above-referred consequence was reached also by the *Yukos* tribunal reasoning that the use of the phrase *"reserves the right"* requires such exercise for the effective application of Article 17 of the ECT.[276]

The *Liman Oil v. Kazakhstan* tribunal observed that there were not any differences between the parties with regard to whether Article 17 of the ECT had implied a notification requirement to invoke the rights therein or not. The tribunal

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[272] In the tribunal's words, *"The **language of Article 17(1) is unambiguous**; and that **meaning is consistent with the different state practices** of the ECT's Contracting States under different bilateral investment treaties: certain of them applying a **generous approach** to legal entities incorporated in a state with no significant business presence there (such as the Netherlands) **and** certain others applying **a more restrictive approach** (such as the USA). **The ECT is a multilateral treaty with Article 17(1) drafted in permissive terms**, not surprisingly, in **order to accommodate these different state practices**."* [Emphasis added]: *Plama*, para. 155.
[273] *Plama*, para. 156; *Khan Resources*, para. 419.
[274] *Khan Resources*, para. 419.
[275] *Plama*, para. 156.
[276] *Yukos* cases, para. 456.

settled this matter in the affirmative and stated that inferring such requirement from the provision was the only way to construe the wording "*reserves the right to deny the advantages...,"* because, in the tribunal's commonly cited wording: *"To reserve a right, it has to be exercised in an explicit way."*[277] The *Ascom v. Kazakhstan* tribunal, following the same line of reasoning, stated that only in case where the denying party exercises its right, Article 17 of the ECT would apply.[278]

The tribunal in *Khan Resources v. Mongolia,* examining the matter in a sub-section entirely dedicated thereto, also determined that Article 17 of the ECT does not serve as an "*automatic denial of benefits.*" The tribunal, beyond what set forth by the above referred ones, went into details in respect of the interpretation of the provision, commencing with the statement that the ECT, as an international treaty, would be expected to be interpreted considering the relevant rules under Article 31 and 32 of the VCLT.[279] The tribunal, from the wording "*reserves the right,*" concluded that such right is "*kept*" by the contracting parties to exercise in the future. Furthermore, the tribunal also determined that such interpretation would be in accordance with the treaty's "*object and purpose.*" Referring to Article 2 of the ECT, formulizing the treaty object and purpose by stating that the *"Treaty establishes a legal framework in order to promote long-term cooperation in the energy field,"* the tribunal highlighted that such interpretation of DOB clause could enable the referred long-term cooperation by

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[277] See, e.g., *Liman Caspian Oil BV and NCL Dutch Investment BV v. Republic of Kazakhstan*, ICSID Case No. ARB/07/14, Award (Excerpts), 22 June 2010, para. 224, https://jusmundi.com/en/document/decision/en-liman-caspian-oil-bv-and-ncl-dutch-investment-bv-v-republic-of-kazakhstan-award-tuesday-22nd-june-2010#pa_42043 (accessed on 22 August 2022) (*Liman Caspian v. Kazakhstan*).
[278] *Ascom v. Kazakhstan*, para. 745.
[279] *Khan Resources*, para. 417.

providing an incentive to states, with differing policies on subject-matter entities falling within the scope of Article 17, to sign the ECT.[280]

B. The Manner of Exercise and Interstate Requirements in DOB Provisions

The tribunals finding for DOB provisions to be actively exercised by respondent states have faced with another question to settle: In what manner such exercise should be carried out and is there any interstate requirements to be fulfilled before the exercise of DOB rights? Such question is addressed by tribunals depending on the formulation given place in DOB provisions:[281] whether they had explicitly required any specific procedure, whereby the DOB rights should be exercised, or they had kept silent with regard to such matter, as in the ECT.[282]

For the sake of clarity, one must distinguish two different types of procedural pre-conditions foreseen in DOB clauses: The manner of application of DOB rights, which deals with how a denying state should exercise such rights against putative investors, and the consultation and/or notification requirements that should be fulfilled by and between the contracting parties to the relevant IIA.[283] While the former is typically formulated in a form of notification to investors, e.g., the provision of *"publicity or other notice,"*[284] the latter refers to collaborative actions by or between contracting states, i.e., notification and/or consultation requirements. Since both are

[280] *Khan Resources*, para. 421. In the same line, it is argued that such formulation would provide the respondent state with the discretion to make a decision based on its policies and needs. See, Behlman, p. 422.
[281] Baltag (Denial of Benefits), p. 3.
[282] Mistelis / Baltag (Energy Charter Treaty), p. 1319.
[283] Mistelis / Baltag (Investment Treaty Arbitration), p. 16.
[284] For the referred term used in the way to cover such requirements in a general way, see, *Plama*, para. 157.

intertwined notions,[285] and they aim at the effective and correct application of DOB rights,[286] they are given place under the same topic in this topic.

As for the manner of DOB rights' exercise against putative investors, they are submitted to be more controversial than the interstate requirements and in close connection with the timing requirements of such exercise.[287] Having said that, as would be seen in the below-referred decisions, different formulations mostly and solely effect the type of interpretation conducted by the tribunals to arrive at the same conclusion. That is, in either case where the interpretation is carried out solely based on the language or also considering the object and purpose of the treaty; unless otherwise explicitly stated in the provision, the denying party would need to actively exercise such rights by taking certain actions.[288]

To be more precise, in the ECT jurisdiction, tribunals, following the below-examined *Plama* decision, have required a prior publicity and/or notification of the exercise of DOB rights addressing putative investors.

Answering the recited questions in the *Plama* case, where the DOB provision (i.e., Article 17 of the ECT) was silent as to such procedural requirements, the tribunal found that such exercise would necessitate a "*publicity or other notice so as to become reasonably available to investors and their advisers.*" Exemplifying the foregoing, the

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[285] Mistelis / Baltag (Investment Treaty Arbitration), p. 16.

[286] Such effective and correct application of DOB provisions is explained by Mistelis and Baltag stating:

> "*[O]n one hand, the interests of the parties to the relevant IIA are preserved and benefits of the treaty are granted to proper investors, and, on the other, investors investing in the host State and committing significant resources in this respect, are protected from any abusive invocation of the 'denial of benefits' clause.*"

See, Mistelis / Baltag (Investment Treaty Arbitration), p. 17.

[287] *Ibid*.

[288] With respect to the treaties not requiring any preconditions for the exercise of DOB rights, tribunals had been inclined not to read any prerequisites into the DOB provisions before the *Plama* case, which has changed with the controversial conclusion arrived at by the tribunal therein. See, Baltag (Denial of Benefits), 3.

tribunal cited "*a general declaration in […] the official gazette,*" "*a statutory provision*" in the relevant laws, and "*an exchange of letters*" addressing a specific investor or investor group as devices satisfying such publicity or notice requirement.[289] In terms of such publicity requirement, the tribunal categorized Article 17(1) itself as "*at best only half a notice,*" stating that it would be reliant on a "*further notice of its exercise by the host state*."[290]

In the way objectifying the *Plama* tribunal's finding, the tribunal in *Masdar v. Spain*, another ECT case, provided that such publicity or other notice requirement should have been fulfilled before the dispute arises by a legislation declaring such denial in a general or sector-specific manner, or via the promulgation of measures addressing certain investors in a specific way.[291]

While the referred interpretation under the ECT is submitted by authors to be more investor friendly; it also attracts legal and practical criticisms, which will be addressed in the following parts hereof.[292]

As for the interstate requirements, if and when they take part in a DOB provision, then the denying contracting party to the IIA is obliged to fulfill them to be able to exercise the subject-matter rights. In the absence of such an explicit inclusion, it would be interpreted in the way to empower the denying party's position against putative investors by not implying such obligation to be performed before the denial.[293] In its presence, on the other hand, its being either mandatory or discretionary, and their

[289] *Plama*, para. 157.
[290] This approach was also concurred with by *Khan Resources* tribunal. See, *Khan Resources*, para. 423. For the criticism in the way such general declaration in an official gazette would amount to a reservation to the ECT, which is forbidden under the ECT Article 46, see, Mistelis / Baltag (Energy Charter Treaty), p. 1320.
[291] *Masdar v. Spain*, para. 239.
[292] Mistelis / Baltag (Investment Treaty Arbitration), pp. 17-18.
[293] *Ibid.*; Mistelis / Baltag (Energy Charter Treaty), p. 1320. Such interstate requirements rarely take place in DOB provisions; see, Côté, p. 8.

manner of application could be a matter of interpretation.[294] Such requirements could include a collaborative process to be carried out by party states—i.e., consultations—and/or one-sided actions addressing the other party state—i.e., notifications.[295]

The most widely given example of such IIAs seems to be NAFTA, which provides both notification and consultation requirements. Article 1113 of NAFTA sets forth that the benefits of the chapter, where the referred article locates, may be denied subject to prior notification and consultation in accordance with the provisions dealing therewith (i.e., Article 1803[296] and Article 2006[297]). The Australia-Vietnam BIT (1991) and Australia-Czech Republic BIT (1993), both examined above in the

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[294] Also, it is submitted that the IIAs without specific provisions dealing with the manner of application of such requirements, unlike NAFTA, pose a hardship in practice. Mistelis / Baltag (Investment Treaty Arbitration), p. 17. Also, in the literature, it is submitted that the legal implications of such interstate requirements is not clear, and the tribunals handling the related issues have not brought about conclusive conclusions, see, Côté, p. 8.

[295] Mistelis / Baltag (Investment Treaty Arbitration), p. 15.

[296] Article 1803 (*Notification and Provision of Information*) that takes part in Chapter 18 of NAFTA, titled "*Publication, Notification and Administration of Laws,*" is as the following:

> "*1. To the maximum extent possible, each Party shall notify any other Party with an interest in the matter of any proposed or actual measure that the Party considers might materially affect the operation of this Agreement or otherwise substantially affect that other Party's interests under this Agreement.*
> *2. On request of another Party, a Party shall promptly provide information and respond to questions pertaining to any actual or proposed measure, whether or not that other Party has been previously notified of that measure.*
> *3. Any notification or information provided under this Article shall be without prejudice as to whether the measure is consistent with this Agreement.*"

See, *supra* fn. 156.

[297] Article 2006 (*Consultations*) takes part in Section A "*Institutions*" under Chapter 20 of NAFTA, titled "*Intstitutional Arrangements and Dispute Settlement Procedures.*" This Article, after stating that "***Any Party may request*** *in writing* ***consultations*** *with any other Party* ***regarding any actual or proposed measure or any other matter that it considers might affect the operation of this Agreement***" [Emphasis added] in the first sub-paragraph, provides instructive rules aiming for a "*mutually satisfactory resolution*," under its fifth sub-paragraph, which reads as the following:

> "*5. The consulting Parties shall make every attempt to arrive at a mutually satisfactory resolution of any matter through consultations under this Article or other consultative provisions of this Agreement. To this end, the consulting Parties shall:*
> *a. provide sufficient information to enable a full examination of how the actual or proposed measure or other matter might affect the operation of this Agreement;*
> *b. treat any confidential or proprietary information exchanged in the course of consultations on the same basis as the Party providing the information; and*
> *c. seek to avoid any resolution that adversely affects the interests under this Agreement of any other Party.*"

See, *supra* fn. 156.

previous chapter, require a joint consultation of party states in the case a company of a contracting party is owned or controlled by the nationals of a third-party state: "*the Contracting* ***Parties may decide jointly in consultation*** *not to extend the rights and benefits of this Agreement to such company."* [Emphasis added].

Also, the method and timing of the interstate requirements have also been addressed by some tribunals. By the *Ampal v. Egypt* tribunal the DOB provision in the US-Egypt BIT (1982) was analyzed, specifically in this context. Such provision, given place in Paragraph 1 of the Protocol to the BIT, set forth that the denying party, once making the determination that the treaty benefits are to be denied, should "*promptly consult*" with the home state for a "*mutually satisfactory resolution*" of the issue concerned. As stated in the paraphrased part of the provision, it does not only refer to a consultation requirement, but it also requires it to be carried out promptly. To gain insight into the application of such promptness requirement, the "*factual matrix of the case*," in the words of the tribunal, should have been addressed, as have been conducted by the tribunal:[298] on 18 May 2011, the claimant submitted a letter to Egypt authorities that advised the latter of the dispute and requesting that the amicable resolution methods apply before it has to file a suit before an arbitral tribunal in accordance with the US-Egypt BIT (1982).[299] On 2 May 2012 the request for

[298] *Ampal v. Egypt*, para. 130 *et seq*.
[299] *Ibid.*, para. 135. As noted by the tribunal in para. 134, Article 7 of the US-Egypt BIT (1982) foresees an amicable dispute resolution mechanism, i.e., consultation and negotiation, and sets for the arbitration process if such amicable ways do not result in settlement in the way described in the referred Article. To this effect, Article 7 of the US-Egypt BIT (1982) provides the following:
"…

> *2. In the event of a legal investment dispute between a Party and a national or company of the other Party with respect to an investment of such national or company in the territory of such Party,* ***the parties shall initially seek to resolve the dispute by consultation and negotiation****. The Parties may, upon the initiative of either of them and as a part of their consultation and negotiation, agree to rely upon non-binding, third-party procedures.* ***If the dispute cannot be resolved through consultation and negotiation, then the dispute shall be submitted for***

arbitration was filed.[300] Thereafter, on 27 January 2013, Egypt submitted a letter to the claimant indicating that it had exercised the DOB provision of the treaty.[301] On the following day, 28 January 2013, Egypt notified the US for the first time and indicated that it would be available for "*prompt consultation,*" as foreseen by the treaty.[302]

The tribunal stated that the consultation requirement of the treaty was clear, and it had brought about the obligation for contracting parties to consult with each other "*in order to search for a mutually satisfactory resolution of the matter and such consultations must be held promptly.*"[303] Based on such initial premise and determining that Egypt submitted its first letter on the day following its exercise of the DOB provision, it found that there had been a "*fait accompli*" for the US in lieu of an invitation to consultation with regard to the matter.[304] Therefore, given that Egypt had

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> ***settlement in accordance with the procedures upon which a Party and national or company of other Party have previously agreed****…*
> *3.*
> *a.*
> ***In the event that the legal investment dispute is not resolved*** *under procedures specified above,* ***the national or company concerned may choose to submit the dispute to the International Centre for the Settlement of Investment Disputes*** *("Centre") for settlement by conciliation or binding arbitration,* ***if, within six (6) months of the date upon which it arose: (i) the dispute has not been settled*** *through consultation and negotiation…"* [Emphasis added].

See, *supra* n. 135.

300 *Ampal v. Egypt*, para. 136.

301 *Ibid.*, para. 137.

302 *Ibid.*, para. 139.

303 *Ibid.*, para. 145-147.

304 *Ibid.*, paras. 148-149.

exercised its rights before commencing a consultation process,[305] the tribunal decided that the exercise of the DOB provision was invalid.[306]

Last, but not least, as for the interstate requirements, it is submitted that they may take part in IIAs as either mandatory or discretionary components. Such difference in IIAs was examined in *Ampal v. Egypt*, the tribunal of which clarified the reasoning for its departure from the *Pac-Rim v. El Salvador* decision where CAFTA was the governing treaty and the exercise of DOB rights was found to be effective.[307] In summary, in Article 10.12.2 of CAFTA, the DOB provision was held "*[s]ubject to Articles 18.3 (Notification and Provision of Information) and 20.4 (Consultations)*" of the treaty, and Article 20.4.1 formulated the consultation requirement in a discretionary way.[308]

Therefore, in the *Pac-Rim* decision, it was submitted that the consultation requirement in the CAFTA DOB provision was discretionary. Reminding the referred

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[305] The tribunal elaborated on whether it would practically be possible for the respondent side to carry out the referred consultations with the home state, i.e., the US, before the exercise of the DOB provision. In this context, it evaluated that the respondent state had had a six-month interval for such consultations, which covered the period set for the amicable settlement attempts under Article VII(2) and (3) of the treaty. The tribunal found, as a result, that it would have fulfilled the promptness requirement had the respondent commenced the consultation process within this period, instead of waiting for more than twenty months. *Ampal v. Egypt*, para. 161.

[306] *Ampal v. Egypt*, para. 151. Also, whether the consultation requirement and the exercise of DOB provision was foreseen in a sequential manner was discussed by the parties and tribunal. The "*shall promptly consult*" requirement had been formulated as "*shall first consult"* before the amendment dated 11 March 1986 made on the BIT. See, *Ampal v. Egypt*, paras. 133, 152. According to Professor Vandevelde's expert opinion referred to by the respondent side, such modification implied that the requirement was to be considered regardless of the sequence of events all around the dispute settlement process, e.g., any notification, the conduct of any procedural action, etc.; that is, the said consultations could take place after the exercise of DOB rights. See, *Ampal v. Egypt*, para. 153. However, the tribunal disagreed with this opinion by observing that the meaning of such requirement was "*evident*," and its purpose was "*seeking a mutually satisfactory resolution.*" The tribunal, therefore, determined the following: "*The object and purpose of the mandatory consultation is to find a satisfactory resolution, not to discuss whether a decision previously taken by one Party should be endorsed and accepted by the other Party. In this respect, the Tribunal finds that the State Parties' final statements in their correspondence fall short of an acceptance on the part of the United States that Egypt was entitled to deny Ampal the benefits of the Treaty.*" See, *Ampal v. Egypt*, para. 154.

[307] *Ampal v. Egypt*, para. 156.

[308] The referred Article 20.4.2 of CAFTA reads as the following: "***Any Party may request** in writing* ***consultations with any other Party*** *with respect to any actual or proposed measure or any other matter that it considers might affect the operation of this Agreement.*" [Emphasis added]. See, *supra* fn. 161.

DOB provision in CAFTA and the above-given interpretation, the *Ampal v. Egypt* tribunal observed that the governing BIT in the case had set forth a mandatory consultation requirement, unlike CAFTA.[309] The practical consequences of the foregoing differentiation in DOB formulations seem to be self-evident: Only the failure to conduct consultations that are formulated as a mandatory component in DOB provisions would result in the ineffectiveness of DOB rights.[310]

IV. The Effects and Timing Requirements of DOB Provisions

A. The Effect: Retrospective or Prospective?

Whether DOB provisions' application results in retrospective or prospective effect has been discussed by many and various authors and tribunals.[311] Such discussion addresses the question regarding the point in time on which such application of DOB rights would be deemed to be effective. The alternative responses provided by the tribunals of the below-referred disputes are as following: when the rights are exercised, the subject-matter benefits are activated, or, when the requirements set forth under the IIA is fulfilled.

The below-surveyed arbitral decisions demonstrate the main divergence between the ECT and non-ECT jurisprudence regarding the retrospective v. prospective effect of DOB provisions—with a few exceptions, though.[312] While the latter is permissive as to the retrospective effect of DOB rights, the former accords only prospective effect to the exercise of DOB rights,[313] in which case putative

[309] *Ampal v. Egypt*, para. 156.
[310] Mistelis / Baltag (Investment Treaty Arbitration), p. 17.
[311] Baltag (Denial of Benefits), p.3. See, e.g., Mistelis / Baltag (Investment Treaty Arbitration), p. 26.
[312] See, e.g., *Ampal v. Egypt*.
[313] Mistelis / Baltag (Investment Treaty Arbitration), p. 29.

investors will have been benefiting from the advantages of the relevant IIAs by the time the DOB rights are exercised by denying states, and they will be able to claim for their damages stemming from the state's breaches of such treaty protections up to such date.[314]

Naturally, such controversial divergence emerges when DOB provisions are silent with regard to their effects. In light of the fact that most of the unsuccessful DOB cases result from the retard in the invocation of DOB rights, the importance of such division becomes self-evident.[315]

1. The Jurisprudence Finding for Prospective Effect

In the ECT jurisprudence, tribunals have found for the prospective effect of the DOB clause of the ECT (i.e., Article 17) up to the present, and they have required its invocation before the commencement of arbitration in order for it to be effective regarding such proceedings.[316] The principal reasoning for such finding has always been the object-and-purpose interpretation of the ECT based on its Preamble and Article 2.

In addition to the arbitral decisions surveyed below, it is also submitted in the literature that such interpretation was naturally required in the light of the referred parts of the ECT. In line with the foregoing, three principal reasons justifying such approach were set forth: the establishment of power balance between the state and investor parties, the wording preference expressed in the ECT—i.e., the contracting parties

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[314] *Ibid.*, pp. 26, 28.
[315] Côté, p. 5.
[316] *Ibid.*

reserving such rights—and the preservation of the investors' legitimate expectations.[317]

Within such context, in the *Plama* case, the tribunal analyzed the requirements for the exercise of DOB rights beforehand in the light of the object and purpose of the ECT, and it found that for investors to have a predictability regarding varying state practices, Article 17(1) should have been construed in the way requiring the exercise of the DOB rights before their application to the relevant investor.[318]

Also, in the foregoing line, the said tribunal, conducting an object-and-purpose interpretation as formulated under Article 31 of the VCLT,[319] reasoned that the investors would have legitimate expectations for treaty benefits until the DOB rights are exercised by the host state. It proceeded from this reasoning to the determination that, to protect such expectations, a reasonable notice to the effect of the said exercise should have been provided before the relevant investment is made. As a result of such notice, in the tribunal's view, the investor could arrive at a decision as to whether to make such investment or not at all or in the host state. This is because after the investment is made, the investor would be left with more limited range of alternatives, and it would be more defenseless against the host state's conducts, which was called the "*hostage factor*" by the tribunal. Therefore, the tribunal reached the conclusion that the putative investor should have the treaty protection, which it had planned to have before the investment is made, until the exercise of DOB rights. Such a conclusion was based on the object-and-purpose interpretation by the tribunal, and it

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[317] See, e.g., Ramachanderan, pp. 222, 224.
[318] *Plama*, para. 157.
[319] *Ibid.*, para. 160.

was noted that "*It is not easy to see how any retrospective effect is consistent with this "long-term" purpose,*" as referred to in Article 2 of the ECT.[320]

To sum up, the *Plama* tribunal concluded that while the prospective application is in accordance with the "*good faith interpretation of the… wording of Article 17(1) in the light of ECT's object and purpose,*" the retrospective application does not accord with that.[321]

Summarizing the above-given argumentation, the tribunal ruled that the object and purpose of the ECT would require the exercise of DOB rights to have prospective effect. This is because an investor not well-*informed and -advised* regarding the exercise of DOB rights could not have had the opportunity to devise its investment strategy based on predictable circumstances before the investment, which would result in severe consequences for such investor. Accordingly, in the tribunal's view:

> "*The investor could not plan in the "long term" for such an effect (if at all); and indeed such an unexercised right could lure putative investors with legitimate expectations only to have those expectations made retrospectively false at a much later date…*"[322]

In the same line of reasoning, the tribunal in the *Yukos* cases also observed that the exercise of DOB rights would result in prospective effect from the date of its exercise onward, without determining any time requirement as to when DOB rights

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[320] *Ibid.*, para. 161.
[321] *Ibid.*, para. 164. Also, in the same line of conclusion, *Ascom v. Kazakhstan* tribunal, interpreting Article 17 of the ECT, explicitly stated that "***Art. 17 ECT would** only **apply if** a state **invoked** that provision to deny benefits to an investor **before a dispute** arose…*" [Emphasis added]. See, *Ascom v. Kazakhstan*, para. 745. For another decision requiring the invocation of DOB rights before a dispute arose, see, *Isolux Infrastructure Netherlands B.V. v. Kingdom of Spain*, SCC Case No. V2013/153, Award, 12 July 2016, para 715, https://jusmundi.com/en/document/decision/es-isolux-infrastructure-netherlands-b-v-c-reino-de-espana-laudo-sunday-17th-july-2016 (accessed on 22 August 2022) (*Isolux v. Spain*).
[322] *Plama*, para. 162.

should have been exercised.[323] An interpretation to the opposite effect could prejudice the objectives and principles of the ECT, in addition to its purpose recited under Article 2, stated by the tribunal. The tribunal also held that such effect would contradict with the promotion and protection terms foreseen in Article 10 of the ECT, as prominent elements of such objectives and principles.[324]

The tribunal in *Liman Oil v. Kazahstan*, based on the prior notification requirement for the invocation of DOB rights under the ECT,[325] arrived at the conclusion that such requirement "*can only lead to the conclusion that the notification has prospective but no retroactive effect.*"[326]

The tribunal in *Khan Resources v. Mongolia*, while examining if Article-17 rights in the ECT could be exercised after the commencement of arbitral proceedings, determined that such matter is not clarified in Article 17, which required an object-and-purpose analysis of the treaty.[327] Centering its interpretation around the predictability aimed to be provided by the ECT, the tribunal assessed that it could only be realized through the investors' advance knowledge on whether they would be able to benefit from the protection under the ECT: If the ECT benefits are denied to an investor fulfilling the criteria under Article1(7)—*the investor definition of the ECT*—after its investment, then it would result in an unpredictable environment for such investor. Likewise, it could impede the investor's ability to carry out an accurate assessment in respect of such investment beforehand.[328]

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[323] *Yukos* cases, para. 458.
[324] *Ibid.*
[325] *Liman Caspian v. Kazakhstan*, para. 224.
[326] *Ibid.*, para. 225. Apart from such inference from the notice requirement allegedly implied in Article 17(1) of the ECT, the tribunal followed the same argumentation as the tribunal of the *Plama* case.
[327] *Khan Resources*, para. 425.
[328] *Ibid.*, para. 426.

Also, in addition to the object-and-purpose analysis conducted by the above-referred tribunals, it also is pointed out that the prospective effect of DOB provisions would be in more compliance with the "*transparent conditions*" to be provided by contracting states.[329]

The tribunal in *Masdar v. Spain* also followed the reasoning put forth by the above-referred decisions in the way connecting the prospective effect of DOB provisions with the publicity and/or notification requirement allegedly implied in Article 17(1) of the ECT. Following the determination that the retrospective effect would contradict with the ECT text and purpose, it stated: "*That would be contrary to **the transparency, co-operation and stability objectives of the ECT** and it would lead to anomalous results.*"[330] [Emphasis added].

When DOB provisions are drafted in the way to include ISDS mechanisms as a subject of denial and become a factor to be considered with regard to the jurisdiction of the tribunal, the effects of DOB rights may be evaluated in conjunction with the components of jurisdiction, such as the parties' consent to arbitration, as had been done by the tribunal in *Ampal v. Egypt* finding for prospective effect in a non-ECT case.

Within such context, the tribunal in *Ampal v. Egypt*, where the US-Egypt BIT (1982), and Egypt-German BIT (2005)[331] were applicable treaties—that is, outside the ECT jurisprudence—also found that the DOB rights should have had prospective effect for the following line of argumentation:

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[329] *Ibid.*, para. 427.
[330] *Masdar v. Spain*, para. 239.
[331] Egypt - Germany BIT (2005) , adopted on 16 June 2005, https://jusmundi.com/en/document/treaty/en-egypt-germany-bit-2005-egypt-germany-bit-2005-thursday-16th-june-2005 (accessed on 22 August 2022) (Egypt-Germany BIT (2005)).

The tribunal needed to address this issue (i.e., retrospective v. prospective effect of the DOB) in relation to its jurisdiction. The contended question centered on whether the retrospective application of DOB provisions would amount to the unilateral withdrawal of consent to jurisdiction, which was explicitly precluded by Article 25(1) of the ICSID Convention, or it would only result in the application of a reservation within such consent. In this context, to justify the retrospective application of DOB rights, the respondent put forth that the contracting states' consent to arbitration was subjected to the DOB rights and, therefore, such treaty protection had always been conditional since the very beginning.[332] Therefore, in the respondent's view, its exercising the DOB rights would not result in the withdrawal of such consent unilaterally, but rather it would be the application of the rights reserved in it.[333] In opposition to this view, the claimant argued that the jurisdiction of the tribunal—dependent on the parties' consents—should have been determined considering the time when the both parties' consents have been provided; that is, when "*the request of arbitration is registered.*" From this argument, the claimant concluded that the exercise of DOB rights must be deemed to be of prospective effect; otherwise, it would be tantamount to the unilateral withdrawal of a party's consent in contravention of Article 25(1) of the ICSID Convention providing "*no Party may withdraw its consent unilaterally.*"[334]

The tribunal, going with the claimant's argument regarding the time to be taken as a basis for jurisdiction,[335] found that "*[w]hen jurisdiction has crystallized, "no Party*

[332] *Ampal v. Egypt*, para. 163.
[333] *Ibid.*, para. 164.
[334] *Ibid.*, para. 165.
[335] *Ibid.*, para. 167.

may withdraw its consent unilaterally", says plainly Article 25(1)."[336] In the tribunal's view, given the BIT "*read in the light of the ICSID Convention,… there cannot be an embedded conditionality in the Treaty which could be triggered after the submission of the dispute to arbitration*"[337] and "*[s]uch denial, to be effective, must be made prior to the filing and registration of the Request for Arbitration.*"[338] Therefore, the tribunal rejected the application of the DOB rights in the way retrospectively stripping the tribunal off its jurisdiction.[339] The *Ampal v. Egypt* decision is criticized in the literature for, as a non-ECT case, being in contradiction with the DOB provision applying in the case.[340]

2. The Jurisprudence Finding for Retrospective Effect: The Criticism of Prospective Effect Approach

Since the criticisms against the prospective approach brought about in the literature and the reasonings put forth by the tribunals for the retrospective approach are well aligned, in this part they will be addressed and included together. In addition to the foregoing, the prior publicity and notice requirements with regard to putative investors—as a matter closely connected with the prospective v. retrospective effect issue—is examined in terms of relevant argumentations in this part.

[336] *Ibid.*, para. 168.
[337] *Ibid.*, para. 169.
[338] *Ibid.*, para. 170.
[339] *Ibid.*, para. 173. On the other hand, the tribunal in *Pac Rim v. El Salvador* case, a CAFTA dispute, agreed with the respondent's argument that the DOB provisions would not be interpreted as a unilateral withdrawal of the consent due to its being conditional since the very beginning. See, *Pac Rim v. El Salvador*, para. 490.
[340] See, e.g., Côté, p. 6.

First, except for the *Ampal v. Egypt* decision, the prevailing view in the non-ECT jurisprudence is inclined to accept the retrospective effect of DOB rights:[341] such rights may be exercised during arbitration proceedings and result in retrospective effect.[342]

The prospective effect approach, also evaluated in relation to the prior publicity and notice requirements, is submitted by some authors to be more investor friendly. This is because, according to them, investors could not be supposed to make a commitment and invest if they are exposed to the probability of being denied of IIA-provided benefits at any time without warning.[343] On the other hand, however, this approach draws widespread and mounting criticisms, which derives from the legal and practical points of view,[344] and, in essence, setting forth only in the case of retrospective application would DOB provisions be of a meaning and purpose.[345]

First, it is submitted that such interpretation reading the prospective effect into DOB provisions seems arguably to disregard the fundamental principles of treaty interpretation, as codified under the VCLT. It is argued that tribunals should be prudent in reading notification and/or time limit requirements into DOB provisions;[346] *that is,* the object-and-purpose interpretation of the treaty should not be carried out in the way contradicting with the textual interpretation of the relevant provision.[347] This is because, according to the referred standpoint, the contracting parties to IIAs would and, more importantly, *could* have inserted such elements into the provisions,[348] had

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[341] *Ibid.*
[342] *Ibid.*
[343] Mistelis / Baltag (Investment Treaty Arbitration), p. 17.
[344] *Ibid.*
[345] Behlman, p. 22.
[346] Mistelis / Baltag (Investment Treaty Arbitration), p. 18.
[347] *Ibid.*
[348] *Ibid.*

they wished to provide such investor-friendly conditions with absolute predictability.[349]

Also, that the prospective effect approach is in accordance with the object and purpose of the ECT by the way of serving the "*long-term cooperation*" is also questioned by some authors. According to them, since it could lead investors to be "*upfront about ownership, nationality and citizenship,*" the retrospective effect approach would benefit the "*long-term cooperation*" more than the prospective effect approach.[350]

Another criticism brought about on the application of DOB clauses in a prospective way is regarding the possibility and reasonableness of such implementation with regard to the investors not raising disputes.

The right provided by DOB clauses is submitted to be a type of measure that can be, and reasonably would be, considered and taken upon the invocation of treaty benefits, i.e., when the request of arbitration is served.[351] This is because only after such invocation of the benefits of arbitration the respondent state would and could examine if the requirements of a DOB clause are fulfilled and, if so, decide whether to apply it or not.[352] The only logical exceptions to the foregoing would be the cases the

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[349] Roe / Happold / Dingemans, p. 85.
[350] Chalker, J.: *Making the Energy Charter Treaty Too Investor Friendly: Plama Consortium Limited v. The Republic of Bulgaria*, Transnational Dispute Management, Vol. 5, 2005, p. 17, available at www.transnationaldisputemanagement.com/article.asp?key=874 (accessed on 22 August 2022), as cited in, Mistelis / Baltag (Energy Charter Treaty), p. 1321.
[351] Mistelis / Baltag (Investment Treaty Arbitration), pp. 18, 22; Mistelis / Baltag (Energy Charter Treaty), p. 1315.
[352] The tribunal in *Guaracachi v. Bolivia* further provided the following: *"…[T]he Tribunal agrees that the denial can and usually will be used whenever an investor decides to invoke one of the benefits of the BIT. It will be on that occasion that the respondent State will analyse whether the objective conditions for the denial are met and, if so, decide on whether to exercise its right to deny the benefits contained in the BIT, up to the submission of its statement of defence."* [Emphasis added]. See, *Guaracachi v. Bolivia*, para. 378.

subject-matter investments are publicly known, made in collaboration with governmental bodies,[353] and/or dependent on the host state authorization,[354]

Furthermore, it would not be a sound expectation for a state to conduct a scrutiny over the fulfillment of DOB requirements before any disputes even ignite.[355] Even assuming that such examination might have been conducted during the course of an investment process, it would be an investment non-friendly measure to provide a notice to such effect.[356] In other words, the prospective application of DOB clauses in a way to compel states to conduct such examination and provide a notice before the emergence of a dispute would result in such implications in contradiction with the very purpose of IIAs.[357] More, such approach seems to disregard the complexity of modern international corporate structures[358] and the fact that corporate restructuring processes may take part within very short periods of time and frequently.

In *Pac Rim v. El Salvador*, where CAFTA DOB provision was applied by a tribunal for the first time[359], the US, in its submission as a non-disputing party, stated that reading such an additional time limit for the exercise of DOB rights into the DOB provision of CAFTA (i.e., Article 10.12.2) would impose an excessive burden on party states to *"to monitor the ever-changing business activities of all enterprises"* in other party states before, during, and/or after they make investments in the respondent state.

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353 Kang, p. 40.
354 Mistelis / Baltag (Investment Treaty Arbitration), p. 22.
355 *Ibid.*, p. 18.
356 *Guaracachi v. Bolivia*, para. 379. Kang, p. 40.
357 Côté, p. 7.
358 Kang, p. 40.
359 *Pac Rim v. El Salvador*, Para. 4.3; Badini, p. 293. Very briefly, in the referred case, the tribunal rejected to follow the previous cases under other IIAs, specifically the ECT, due to, in the tribunal's opinion, "*different wording, context, and effect*" of the CAFTA provision. See, *Pac Rim v. El Salvador*, para. 4.3, cited in Behlman, p. 401. Therefore, the tribunal became the first one finding for the application of the DOB provision under CAFTA and NAFTA, which is argued by some authors to be due to the correct application of the relevant VCLT articles. See, e.g., Behlman, p. 402.

Such constant investigation would encompass "*factual research*" on such enterprises' corporate structures and quality of business activities in the states of their incorporation. Also, such practice would entail with the obligation for the enterprises to disclose confidential and non-public information to host states. Therefore, the US concluded that assigning such tasks to CAFTA parties in order for them to be able to invoke DOB rights before the commencement of arbitration would be detrimental to the purpose of CAFTA Article 10.12.2.[360]

As a result of the mentioned concerns, it would be more convenient to expect that states evaluate if the DOB requirements are met and decide to apply it or not following a dispute arises,[361] which would also serve "*a more balanced approach*" in compliance with the interpretation conducted based on the relevant customary rules formulated in the VCLT.[362]

Reading backward the foregoing argument, an over restrictive approach adopted by tribunals could also be detrimental to the balance endeavored to be set up by IIAs. It is submitted that DOB provisions are devised to notify investors of the possibility that they may be denied treaty benefits if DOB requirements are met in a case. In the sense of such requirements, investors are argued to have the most accurate and comprehensive knowledge on the relevant pre-conditions—specifically concerning the ownership and control structures of them. Therefore, arguably, it is not the respondent's objections that make the putative investor fall within the scope of DOB

[360] For the part in *Pac Rim v. El Salvador* citing the submission, see, para. 4.56. Also, in the referred decision, the tribunal found that the retrospective effect of DOB rights could not be equalized with the unilateral withdrawal of party consents in the sense of ICSID Convention Article 25 since such eventuality had been given place within the consent provided. This analysis of the tribunal deems to be in disagreement with the reasoning in the *Ampal v. Egypt* case. See, respectively, *Pac Rim v. El Salvador*, para. 4.85; *Ampal v. Egypt*, para. 173.
[361] *Guaracachi v. Bolivia*, para. 379.
[362] Mistelis / Baltag (Investment Treaty Arbitration), p. 18.

provisions, but their own structure and conducts. In the light of the foregoing line of argumentation, Sornarajah observes that the present attitude of the ECT tribunals could result in the renouncement of the contemporary international investment system by states since such application may result in the rightful question marks regarding whether the tribunals have seriously taken the purposes of states while inserting DOB provisions into IIAs into consideration in their decisions.[363]

According to some authors and tribunals, that DOB clauses should apply retrospectively does stem from by definition and its very nature. For example, as assessed by the tribunal in *Guaracachi v. Bolivia*, since the party states did consciously not put forth any restrictions on the application of DOB provision[364] in these terms (i.e., the prospective v. retrospective), such right aiming at the withdrawal of treaty benefits should be deemed to be exercised at the time the relevant benefits are claimed.[365]

Another criticism brought about against the prospective effect approach is specifically related to the ECT, under which reading a prior notification requirement, confirming the prospective effect of DOB rights, into the DOB clause is evaluated to be problematic in the light of Article 46 –*Reservations*. The referred article puts forth that "*[n]o reservations may be made to this Treaty*." Therefore, it submitted that a notification to the universal effect could be interpreted in the way it brings about a reservation in contravention of the referred article.

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[363] Sornarajah (Good Faith), p. 137.

[364] The DOB provision –*Article 12*- of the US-Bolivia BIT (1998) is as the following:

> *"Each Party reserves the right to deny to a company of the other Party the benefits of this Treaty if nationals of a third country own or control the company and:*
> *a. the denying Party does not maintain normal economic relations with the third country; or*
> *b. the company has no substantial business activities in the territory of the Party under whose laws it is constituted or organized."*

See, *supra* fn. 140.

[365] *Guaracachi v. Bolivia*, paras. 376-377.

Another argument, based on which such retrospective v. prospective effect issue is analyzed, concerns the legitimate expectations and legal certainty to be provided to investors by IIAs.[366] For the sake of preciseness, the protection of legal expectations is argued to serve the purpose of "*stable legal and business environment*."[367] Another relevant concept, legal certainty, is defined and described in a close connection with the notion of "rule of law," and it requires that legal norms have certain degree of accessibility allowing the subjects to be able to arrange their conducts in a foreseeable and predictable environment, in other words, without being exposed to potential arbitrary practices of relevant authorities.[368]

Among the tribunals finding that the retrospective application of DOB provisions would prejudice the legal certainty and legitimate expectations of investors, the *Plama* tribunal takes place. In the referred case, the respondent argued that the existence of the ECT Article 17(1) would constitute a prior notice to the putative investor advising it of the possibility that it may be denied the treaty benefits if the relevant requirements are met, as a result of which the said investor could not be argued to have any legitimate expectations upon the fulfillment of such requirements. However, the tribunal found that such interpretation would jeopardize the legal certainty on the side of the investor with regard to its rights and the respondent's treaty obligations.[369]

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366 Verburg, p. 426.
367 See, Miles, K.: The Origins of International Investment Law: Empire, Environment and Safeguarding of Capital, Cambridge University Press, Cambridge, 2013, p. 168. Also, the "legitimate expectations" concept has always been of utmost significance specifically for the determination fair and equitable treatment standard. Therefore, in the literature, the notion is closely analyzed in relation to the said protection standard. For such analysis in detailed, see, Miles, pp. 168-172.
368 Verburg, p. 426.
369 *Plama*, para. 163.

As indicated in the referred paragraph, the tribunal disagreed with the idea that Article 17 of the ECT would itself have constituted a notice requiring investors to act in a prudent manner so as to prevent the application of the provision. Addressing this argument, the tribunal only decided that such interpretation would result in imperspicuity on the side of the investor with regard to the treaty benefits, which means the tribunal seems not to provide any supporting arguments and sufficient elaboration.

On the other side, for some authors and tribunals, it is arguable that the existence of DOB clauses in IIAs*, per se*, imposes a condition on the party states' consent to arbitration by providing that the referred treaty benefits, including the ISDS mechanisms in most cases, may be denied in some certain and predictable circumstances.[370] In other words, the putative investors would be expected to be well-conscious of the possibility that they may be denied of the treaty benefits if the pre-conditions in such conspicuous provisions are met. In the light of the foregoing, investors' legitimate expectations could not be deemed to be frustrated by the exercise of such right against them because they could (and naturally would) always guard against the application of DOB clauses by taking relevant measures, e.g., conducting substantial business activities.[371] Accordingly, even in the arbitral decisions implying

[370] In the same line, see, e.g., Ramachanderan, pp. 234-237. Also, the *Plama* tribunal's decision on the retrospective effect was comprehensively criticized in the literature. James Chalker argued that the legal standard established by the *Plama* case was over considerate toward the investor side, and the tribunal had considered the object and purpose of the ECT identical to the investor protection. Cited in Ramachanderan, p. 235, fn. 67.

[371] In the same line, see, *Guaracachi v. Bolivia*, para. 375. The tribunal in *Ulysseas v. Ecuador*, applying the US-Ecuador BIT, provided the following in the same line of reasoning:

> "***The Tribunal sees no valid reasons to exclude retrospective effects****. …[I]t may be noted that since the* ***possibility*** *for the host State* ***to exercise the right in question is known to the investor*** *from the time* ***when it made its the investment****, it may be concluded that* ***the protection*** *afforded by the BIT* ***is subject*** *during the life of the investment* ***to the possibility of a denial*** *of the BIT'S advantages by the host State.*" [Emphasis added].

See, *Ulysseas v. Ecuador*, para. 173.

that the retrospective application of DOB clauses should be preferred to protect the legitimate expectations of investors, it is stated that no state, regardless of its policy on treaty shopping, would keep itself from denying treaty benefits to a putative investor who had commenced arbitration and claimed for a significant amount of damages.[372]

The tribunal in *Guaracachi v. Bolivia*, reasoning in line with the foregoing,[373] summarized the rationale behind such approach in a very clear and concise wording: "*No one can accept more than what is being offered."*[374] The tribunal assessed that what the putative investor was offered was the treaty benefits accompanied by an explicit reservation, i.e., the potential denial of the treaty benefits upon the fulfillment of DOB clause requirements.[375] Thus, the tribunal proceeded to the following case-specific inference and stated that any US investor investing in Bolivia had already been informed of the possibility that the DOB rights could be exercised by Bolivia upon the fulfillment of the DOB requirements.[376] As a result, while the tribunal acknowledged that such approach would result in fragility in the investor's position because it could never be confident about whether such DOB rights would be exercised or not; however, on the other hand, the tribunal concluded that "*[a]t the same time, one cannot say that such a denial will come as a total surprise for the investor…*"[377]

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[372] For example, see, *Khan Resources*, para. 429. However, the tribunal in the foregoing case, reached a different conclusion based on such assumption:

> "*A good faith interpretation does not permit the Tribunal to choose a construction of Article 17 that would allow host states to lure investors by ostensibly extending to them the protections of the ECT, to then deny these protections when the investor attempts to invoke them in international arbitration.*"

See, *Khan Resources*, para. 429.

[373] In the same direction, see, *Guaracachi v. Bolivia*, para. 372.

[374] *Ibid.*, para. 373.

[375] *Ibid.*, para. 373.

[376] *Ibid.*, para. 373.

[377] *Ibid.*, para. 383.

Also, it is submitted that the present DOB formulation in a treaty, consciously agreed on by treaty parties who preferred it over any other conceivable alternative options, should prevail over any party expectations patently departing from the wording, regardless of the legitimacy degree of such. In other words, in the tribunal's view, the parties' agreement, which could have easily been reflected and formulated otherwise, should be honored.[378]

Another possible scenario, in which the relevant inquiry would relatively be more straightforward, is where the investment precedes the relevant treaty's entry into force, which was the case in *Guaracachi v. Bolivia*. In such cases, arguably, the putative investors would be deemed not to be in the expectation of treaty benefits since they had come to an investment decision even before such benefits exist.[379]

In addition to the above-given set of argumentations on the retrospective v. prospective effect issue, the facts submitted to be the root cause of such contrast—i.e., the difference in text and context of treaties—also represent a topic fraught with difficulties.

As demonstrated above, the divergence on the retrospective v. prospective effect of DOB rights mostly coincides with the treaty applying to the relevant cases. Therefore, it is submitted that the reason for such difference among tribunals hinges on the treaty language: If contracting parties "*reserve the right to deny*" or any of them "*may deny*" such benefits, both providing a discretion to party states. Although the treaty language must be considered to be the sole determinant of such effect, arguably, the referred difference is not likely to result in such divergence.[380]

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378 *Ibid.*, paras. 375,377.
379 *Ibid.*, para. 380.
380 Mistelis / Baltag (Investment Treaty Arbitration), p. 29; Côté, p. 8.

Apart from the foregoing, almost all the tribunals referred to above seem to establish their finding based on the object-and-purpose interpretation of the treaty applicable to the dispute of concern. However, one could also argue that there may not be such sharp variation among IIAs in terms of their objects and purposes, all of which emphasizes the need for predictable investment environment to be provided to investors, albeit in different languages: the promotion of long-term cooperation, as in Article 2 of the ECT, or "*a predictable commercial framework for business planning and investment,*" as in the Preamble of CAFTA.[381] Therefore, it would arguably be possible to recourse to both way, either prospective or retrospective effect approach, under any referred formulation.[382]

B. Timing Requirements

In practice, the timing requirement with regard to the exercise of DOB rights[383] by respondents; that is, whether such rights are exercised in a timely manner is determined according to the applicable treaty and arbitration rules.[384]

Within the said context, there seems to be a divergence based on the applicable IIA to a dispute, which manifests itself in the difference between the ECT and non-ECT jurisprudences. In other words, the retrospective v. prospective effect question is also predominantly decisive in the timing requirement as to the exercise of DOB rights.[385]

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381 Mistelis / Baltag (Investment Treaty Arbitration), p. 29.
382 *Ibid*.
383 In this section, the timing requirements concerning the exercise of DOB rights are examined in the way specific to the manner of such exercise with regard to putative investors. As for the timeliness, or promptness, of the interstate procedural requirements, i.e., the notification and/or consultation requirements. See, *Ampal v. Egypt*.
384 Mistelis / Baltag (Investment Treaty Arbitration), p. 23.
385 Ramachanderan, p. 94.

In this sense, under the ECT jurisprudence, although there is a consensus among tribunals as to the invocation of DOB rights before the commencement of arbitration, they have differing views on exactly when they should be exercised:[386] While the *Plama* case tribunal ruled that such exercise required a prior notice to investors that should have taken place before the relevant investment is made,[387] according to the *Ascom v. Kazakhstan* tribunal, such notice should have provided before the dispute emerges.[388]

Also, while not specifying the exact time to exercise the DOB rights, the tribunal in *Liman Caspian v. Kazakhstan* made a decision about the burden of proof regarding the facts causing the belatedness in the exercise of DOB rights. The tribunal found the invocation of the DOB rights under Article 17(1) of the ECT belated because it took place "*more than one year after… [r]equest for [a]rbitration*" submitted by the claimant. Based on such finding, the tribunal held that such exercise of DOB rights was not effective.[389] The tribunal further held that the respondent had the burden of proving the facts justifying such belatedness.[390]

When it comes to the non-ECT jurisprudence, tribunals ruled that such invocation of DOB rights should have been taken place until the "*time limit for the submission of jurisdictional objections under the applicable arbitration rules.*"[391] For

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386 Khachatryan, D.: *The Art of Sayind No: What are the Procedural Requirements of the 'Denial of Benefits' provision of the ECT?*, 2018, Uppsala Univestitet, Master's Thesis, p. 1.
387 *Plama*, para. 161.
388 *Ascom v. Kazakhstan*, para. 745.
389 *Liman Caspian v. Kazakhstan*, para. 226. Also, following the referred finding, in para. 227, the tribunal further held that the respondent had the burden of proving the facts justifying such belatedness, i.e., in the case, the facts resulting in the retarded invocation, its lateness in comprehending such facts, and the prior knowledge thereof would have result in such invocation.
390 In the case, such justifying facts were listed as follows: The facts resulting in the retarded invocation, the respondent's lateness in comprehending such facts, and that the prior knowledge thereof would have result in such invocation. *Liman Caspian v. Kazakhstan*, para. 227.
391 Gastrell / Le Cannu, p. 94.

example, the tribunal in *EMELEC v. Ecuador*, a US-Ecuador BIT case under ICSID Arbitration Rules, found that the proper stage for the invocation of DOB rights would be at the time when the respondent's jurisdictional objections are raised.[392]

The tribunal in *Guaracachi v. Bolivia,* considering Article 23(2) of the UNCITRAL Arbitration Rules 2010,[393] ruled that the invocation of DOB rights, i.e., the objection to jurisdiction, was made in "*good time*," and considered its introduction in the respondent's statement of defence sufficient. Therefore, under UNCITRAL Arbitration Rules, the tribunals of the non-ECT jurisprudence seem to be inclined to draw the time limit for the invocation of DOB rights at the point when the Statement of Defense is to be provided at the latest.[394]

Another tribunal examining the issue is that in *Pac Rim v. El Salvador*, a CAFTA case under the ICSID Arbitration Rules, who dedicated a specific sub-section to the matter.[395] In the case, El Salvador, the respondent, exercised its DOB rights under CAFTA more than two years after the commencement of arbitration.[396] In the decision,

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[392] *"**Ecuador announced the denial of benefits** to EMELEC **at the proper stage** of the proceedings, **i.e. upon raising its objections on jurisdiction**. **If the Tribunal should agree to hear the merits** of the present case, **only then would it be appropriate to examine the substantive requirements for the denial of benefits**, i.e. the determination of whether EMELEC has substantial business activities in the territory of the United States."* [Emphasis added]. See, *Empresa Eléctrica del Ecuador, Inc. (EMELEC) v. Republic of Ecuador*, ICSID Case No. ARB/05/9, Award, 2 June 2009, para. 71, https://jusmundi.com/en/document/decision/en-empresa-electrica-del-ecuador-inc-emelec-v-republic-of-ecuador-award-tuesday-2nd-june-2009 (accessed on 10 August 2022) (*EMELEC v. Ecuador*).

[393] As a set of rules widely referred to by IIAs, the relevant part of Article 23(2) of the UNCITRAL Arbitration Rules (2010) reads as the following: "***A plea that the arbitral tribunal does not have jurisdiction shall be raised no later than in the statement of defence*** *or, with respect to a counterclaim or a claim for the purpose of a set-off, in the reply to the counterclaim or to the claim for the purpose of a set-off…*"[393] [Emphasis added]. See, UNCITRAL (The United Nations Commission on International Trade Law) Arbitration Rules (2010), adopted on 15 August 2010, Article 23. 2, https://jusmundi.com/en/document/rule/en-uncitral-arbitration-rules-2010-uncitral-arbitration-rules-2010#pa_412 (accessed on 10 August 2022) (the UNCITRAL Arbitration Rules (2010)).

[394] The tribunal in *Ulysseas v. Ecuador*, preceding the *Guaracachi v. Bolivia* case, had provided the following to address the rules to be checked for such time limits: "…***Respondent*** *has* ***complied with*** *the* ***time limit prescribed by the UNCITRAL*** *Rules.* ***Nothing in*** *Article I(2) of the* ***BIT excludes*** *that* ***the right to deny*** *the BIT's advantages be exercised by the State* ***at the time when such advantages are sought by the investor through a request for arbitration****.*" See, *Ulysseas v. Ecuador*, para. 172.

[395] *Pac Rim v. El Salvador*, paras. 4.83-4.92.

[396] *Ibid.*, para. 4.84.

where the applicable treaty was CAFTA, the tribunal observed that there had not been "*an express time-limit,*" regarding the exercise of DOB under Article 10.12.2, the DOB provision of the applicable treaty.[397] The tribunal went forward with the determination that, normally, the denial of the ISDS mechanism, as a benefit provided by the treaty, could otherwise have resulted in difficulties for the tribunal, which had not come about in the present case for certain reasons.[398]

First, according to the tribunal, having been the first exercise of the DOB rights under CAFTA by a contracting party thereto, such exercise would entail a "*particular attention by the Respondent, to be exercised upon sufficient and ascertainable grounds,*" which had required "*careful consideration*" and time. Also, in the tribunal's view, such retard had not provided any advantages to the respondent in the case.[399]

Second, the tribunal relied on ICSID Arbitration Rules, governing the arbitral process in the case and which required in Article 41(1) that such objections to the tribunal's jurisdiction are raised as early as possible, but not exceeding "*the expiration of the time limit fixed for the filing of the counter-memorial,*" under any circumstances.[400] According to the tribunal, the foregoing provision was the rule determining the time limits for the exercise of DOB rights in the case, and any earlier timing requirement was not given place or implied in the CAFTA provision, reading

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[397] *Ibid.*, para. 4.83.
[398] *Ibid.*
[399] *Ibid.*, para. 4.84.
[400] The referred provision, Article 41(1) of ICSID Arbitration Rules, sets forth:

> "*Any objection that the dispute or any ancillary claim is not within the jurisdiction of the Centre or, for other reasons, is not within the competence of the Tribunal shall be made as early as possible. A party shall file the objection with the Secretary-General no later than the expiration of the time limit fixed for the filing of the counter-memorial, or, if the objection relates to an ancillary claim, for the filing of the rejoinder—unless the facts on which the objection is based are unknown to the party at that time.*"

See, ICSID (International Centre for Settlement of Investment Disputes) Rules of Procedure for Arbitration Proceedings (2006), adopted on 10 April 2006, Rule 41. 1, https://jusmundi.com/en/document/rule/en-icsid-arbitration-rules-2006-icsid-arbitration-rules-2006 (accessed on 10 August 2022) (ICSID Arbitration Rules).

which into the provision would be in contradiction with the object and purpose of CAFTA due to the "*practical difficulties*" it could cause.[401]

To sum up, for the tribunals of the prospective-effect approach—i.e., the ECT tribunals—the DOB rights must be invoked either before the investment is made (as in the *Plama* case) or arbitration commences (as in the *Ascom v. Kazakhstan* case). On the other hand, in the view of the tribunals inclined to retrospective effect of DOB—i.e., the non-ECT tribunals—such rights, at the very latest, should be exercised at the same time as the objections to jurisdiction, under the applicable arbitration rules, in which case such exercise also could apply retrospectively. The only exception to the non-ECT jurisdiction at the moment seems to the *Ampal v. Egypt* case, where the BIT tribunal found that the respondent should have exercised DOB rights before the commencement of arbitration for not ending up in a position where it withdrew its consent unilaterally in contradiction with Article 25(1) of the ICSID Convention.[402]

V. Burden of Proof

The burden of proof regarding the fulfillment of the DOB requirements,[403] as a matter that may be determining the outcome of relevant cases,[404] is an exceptional procedural topic, on which tribunals and the literature have a consensus.[405]

The conventional theory of the burden of proof requires the alleging party to prove its allegations, i.e., the principle of "*actori incumbit probation,*" which is

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[401] *Pac Rim v. El Salvador*, para. 4.85.
[402]*Ampal v. Egypt*, para. 165.
[403] According to the tribunal in *Ulysseas v. Ecuador*, the interpretation rules codified in the VCLT should apply to determine which requirements are to be proven to exercise DOB rights. See, *Ulysseas v. Ecuador*, para. 166.
[404] Côté, p. 9.
[405] Mistelis / Baltag (Investment Treaty Arbitration), p. 30.

followed by tribunals as well.[406] Therefore, as for the proof of the facts meeting DOB requirements, such burden is to be borne by the respondent side.[407] However, on the other hand, the modern international corporate establishment with multi-layer and complex shareholding structure may require the submission of the relevant proofs by the claimant side via and in accordance with the relevant rules of evidence, as highlighted in the below-referred cases.[408]

The tribunal in *AMTO v. Ukraine* observed that while Article 17(2) of the ECT explicitly places the burden of proof on the respondent side as the denying party, Article 17(1) does not provide such clarity on the subject.[409] To clarify the matter, the tribunal referred to the general rule applicable in international arbitration, which was reflected with the maxim *"onus probandi actori incumbit"*—meaning the burden of proof weighs on the alleging party. Based on such principle, the claimant would be expected to prove that it falls within the investor definition of the ECT, and it controls in a direct or indirect manner the investment, as the subject matter of the alleged protection. On the other hand, however, the same principle would result in the placement of such burden on the respondent side when it comes to the proof of the allegation in the way the putative investor falls within the investor category included in the DOB provision.[410]

The tribunal, besides the foregoing, acknowledged the difficulties, possibly stemming from such burden, for the respondent side, specifically referring to the

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[406] Kang, p. 36.
[407] *Ibid.*
[408] *Ibid*. Also, tax havens practices are considered to take part alongside the complexity of corporate structures in complicating the respondent state's access to relevant and necessary information and proof. *Ibid.*, p. 9.
[409] *AMTO v. Ukraine*, para. 63.
[410] *Ibid.*, para. 64.

circumstances where the ownership or control structure is of transnational characteristics. Also, it was noted that such evidence could be collected and presented by the claimant side more easily. However, such acknowledgements did not bring the tribunal to the point where it poses such burden of proof on the claimant side. In the tribunal's wording, "*the relative accessibility of evidence would not seem to justify any modification to the normal rules regarding the burden of proof,*" yet it did not leave the respondent completely helpless. The tribunal stated that such evidence could be collected via document disclosure process, whereby the respondent could request from the claimant the inaccessible documentation, or, if agreed by the parties, the tribunal, itself, could request the relevant clarifications.[411] If the claimant does not provide such documentation or clarification, stated the tribunal, such non-performance could serve negative inferences against it. More, in the tribunal's view, the respondent itself could also compel the claimant side to provide such documentation and/or clarification by benefiting from the insufficiency and elusiveness of the existing evidence in its allegations.[412]

Such implementation is also conducted by tribunals based on the "*positive assertions*" v. "*negative assertions*" difference, in the case of the former, the party carrying out such assertions is under the burden of proof.[413] In the line of the foregoing, the tribunal in *Liman Caspian v. Kazakhstan* reasoned that although the general

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[411] *Ibid.*, para. 65. Also, because of the observed hardship with regard to the accessibility of evidence for the respondent side, some tribunals are inclined to assess that such burden is on the claimant; while such approach is criticized for having a confusion between the notions burden of proof and the claimant's duty to disclose information and evidence it possesses. Therefore, it is set forth in the literature that a "*preliminary burden of proof*" could be assigned to the respondent side for establishing "*a rebuttable presumption*" of the fulfillment of corporate substantive requirements, and thereafter, "*the evidential burden*" could be put on the claimant side "*to rebut the presumption,*" as followed by the tribunal of *Bridgestone v. Panama*, para. 289, as cited and explained in Côté, p. 10.
[412] *AMTO v. Ukraine*, para. 65.
[413] *Pac Rim v. El Salvador*, para. 4.60.

principle is that the burden of proof is usually on the side of claimants providing the factual basis of their claims, it shifts to the respondent side when it is expected to establish the facts requiring the application of the exceptions given place in their defenses, which was the case in the application of the ECT Article 17(1).[414]

The above conclusion was also applied for the third-party control determination, in addition to that of other DOB requirements, by the tribunal in *Generation Ukraine v. Ukraine*, and such burden of proof was placed on the respondent side since it was "*the party invoking the "right to deny" conferred by*" the DOB provision in the applicable treaty, i.e., the US-Ukraine BIT[415], entered into force on 16 November 1996.[416]

The tribunal in the referred case, therefore, held that the respondent's allegation in the way that the claimant could not have provided sufficient evidence concerning the DOB requirements was inopportune, and combining with the insufficiency of the respondent's submissions, it resulted in the tribunal's rejection of admissibility objection without going into any scrutiny regarding the claimant's business activities.[417]

The tribunal in *Ulysseas v. Ecuador* referred to the relevant UNCITRAL Arbitration Rules (1976) as the rules of arbitration governing the proceedings, which states "*[e]ach party shall have the burden of proving the facts relied on to support his claim or defence,*" in Article 24(1)[418]

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[414] *Liman Caspian v. Kazakhstan*, para. 164.
[415] Treaty Between Ukraine and the United States of America Concerning the Encouragement and Reciprocal Protection of Investments, adopted on 4 March 1994, https://jusmundi.com/en/document/treaty/en-treaty-between-the-united-states-of-america-and-ukraine-concerning-the-encouragement-and-reciprocal-protection-of-investments-ukraine-united-states-of-america-bit-1994-friday-4th-march-1994 (accessed on 22 August 2022) (*the US-Ukraine BIT*).
[416] *Generation Ukraine v. Ukraine*, para. 15.7.
[417] *Ibid.*, paras. 15.8-15.9.
[418] *Ulysseas v. Ecuador*, para. 166.

VI. Recent Developments in the ECT Modernization

A. Article 17 of the ECT: Problems and Proposals

The ECT provisions, naturally including Article 17, are found to be subject to inconsistent and contradictory interpretations and applications by tribunals and courts.[419] The above-examined controversies that emerge regarding the application of DOB provisions of IIAs are mostly related to the application and interpretation of Article 17 of the ECT: this naturally is argued to prejudice the legal certainty and "*stable, equitable, favourable and transparent*" environment aimed at by the ECT.[420]

While it is submitted elsewhere that the concentration of such differences on the referred Article derives from the erroneous interpretation by tribunals,[421] i.e., the misapplication of the VCLT,[422] it is also argued that this results mainly[423] from its drafting.[424] Besides, these two also may be inherently interrelated: "*Just as bad facts*

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[419] Verburg, pp. 425, 427; D'Allaire, D.: *The Nationality Rules under the Energy Charter Treaty: Practical Considerations*, Journal of World Investment & Trade, Vol. 10, No. 1, 2009, p. 68.
[420] Verburg, p. 427.
[421] Kunstyr, J.: *Denial of Benefits and Article 17 of the Energy Charter Treaty*, 2015, Charles University in Prague, Master's Thesis, p. 59.
[422] Behlman, p. 414 *et seq.*
[423] The word "mainly" here is used consciously: it is submitted that there are numerous reasons for the inconsistent interpretation and application of ECT provisions; such as, "*ad hoc nature of arbitration and lack of appeal mechanism," "textual deficiencies,"* the problems stemming from the very nature of investment arbitration (e.g., *"adversarial nature if investment arbitration" and "arbitrator remuneration"*), and *"lack of participation ECT contracting parties in the interpretation of the treaty,"* which are examined in detail in, Verburg, pp. 436-444. Because the main concern addressed by the ECT modernization process is concerning the textual deficiencies, it is preferred to be specifically addressed in this thesis.
[424] The ECT, as an MIA focusing on the energy sector, is indicated to be drafted and negotiated within a short period of time (i.e., in less than three years) despite the significance and extent of its subject matter. See, Mistelis / Baltag (Energy Charter Treaty), p. 1301; Kunstyr, p. 60. For a detailed analysis on the textual deficiencies of the ECT, see, Verburg, p. 437. In the same line, see, Verburg, p. 428, which provides the following precise dissection:

> *"...ECT tribunals sometimes explicitly criticise one another when examining comparable arguments. This issue arises in part due to the vague nature of various ECT provisions, which increases the likelihood of inconsistent interpretations. Another issue relates to the multiplicity of cases involving comparable matters, causing confusion when tribunals render contradictory awards in relation to the same challenged measure(s)."*

can make bad law, poor drafting can lead to poor interpretation."[425] In the sense of the latter, the misapplication of the interpretation rules, it is set forth that the manner of implementation carried out by the ECT tribunals caused the DOB provision to lose its "*purpose and effect*" by ending up with the non-applicability under any circumstances examined by the tribunals up to the present. This was, with the VCLT's words in Article 32(b), perceived to be "*manifestly absurd and unreasonable*" in the literature, which required the application of the "*supplementary means of interpretation,*" such as the *travaux préparatoires* and the circumstances of the conclusion of the ECT.[426] In the context of such supplementary means, it is submitted that there was nothing in the *travaux* aiming at any change in the traditional application of DOB clauses.[427]

Regardless of the causes of this problematic, the contracting parties to the ECT have severe difficulties in invoking Article 17,[428] which argued to have resulted in an ineffective solution against treaty shopping.[429] Addressing such concern, several solutions are proposed in the literature[430] and by institutional entities to make the invocation of the ECT DOB provision more straightforward and practical, in the way closing the gap between the ECT and non-ECT jurisprudence.[431]

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[425] Behlman, p. 414.
[426] *Ibid.*, p. 414, 415.
[427] Walde, T.W.: *Interpreting Investment Treaties: Experiences and Examples*, International Investment Law for The 21st Century: Essays In Honor Of Christoph Schreur (Eds.: Christina Binder *et al.*), Oxford University Press, 2009, p. 727, as cited in Behlman, p. 415.
[428] Up to the present, there had been no ECT case in which the DOB provision was succeeded to be invoked. See, Côté, p. 4.
[429] Behlman, p. 421.
[430] For a detailed explanation on such possible solutions addressing the inconsistent interpretation and application of the ECT provisions, see, Verburg, pp. 444-454, where the author proposed the followings: "*Amending the ECT*," to conclude an "*Energy Charter Protocol*," to such effect, "*Inter se Modification of the Treaty*," "*Energy Charter Declaration*," and providing the participation of "*Non-Disputing ECT Parties as Amicus Curiae*."
[431] For the definition and scope of such gap, see generally, e.g., Pinto.

In the literature, among other proposals, the *erga omnes* exercise of the ECT DOB rights via a general declaration made by contracting states was proposed to resolve the prospective effect question.[432] While the supporters of such proposal consider such declaration as a mere invocation of the DOB rights; however, such approach is indicated by others to be potentially problematic in the light of Article 46 of the ECT that requires "*[n]o reservations may be made to this Treaty.*"[433]

It is also submitted that, under the ECT, the legislation of a law to the effect of the denial of benefits in an "*abstract and general*" way could recuperate the difficulties stemming from the existing manner of application of Article 17 of the ECT. However, on the other hand, such enactment is argued to be pointless considering the same type of provision takes place in the ECT itself. Also, a validity question deriving from Article 46 of the ECT, stating *"[n]o reservations may be made to this Treaty,"* could be casted on such legislation. [434] Another possible solution for the narrow application of the ECT Article 17 seems to be its amendment as a way to provide a long-term solution.[435]

B. The ECT Modernization

At this point, the only way to carry out such amendment is through the modernization process of the ECT, which is under the responsibility of the Energy Charter Conference, established as a governing body according to Article 34 of the

[432] Kunstyr, p. 60.
[433] *Ibid.*, p. 60.
[434] Mistelis / Baltag (Energy Charter Treaty), p. 1320.
[435] Verburg, p. 445.

ECT and comprising one representative from each contracting party to the ECT.[436] Article 36 of the ECT, while determining the decision-making process of this organ, requires unanimity among the participants for the amendments to the ECT (except for those to Article 34 and 35 and Annex T). At this juncture, the Strategy Group, one of the sub-bodies founded by the Conference, was established in 2010 for the promotion of the Charter process modernization.[437]

Based on this establishment, and considering, *inter alia*,[438] the inconsistencies with regard to the implementation and application of investment provisions in the ECT,[439] the Energy Charter Conference decided to commence a collective evaluation process regarding the modernization of the ECT in its Ashgabat, Turkmenistan, meeting in November 2017.[440] Given that one of the main purposes of such process was to provide the consistency in the judicial and arbitral practice, clearing up the ambiguous facets of ECT provisions is deemed to the principal focus of such modernization.[441]

In the said context, while drawing the framework for such modernization, Article 17 of the ECT was also included therein, and it was observed that *"some IIAs specify that the denial of benefits clause can also be invoked once [i]nvestment*

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[436] "*The ECT established two permanent bodies: the Energy Charter Conference (Article 34) and the Energy Charter Secretariat (Article 35). The Charter Conference is the governing body, whilst the Secretariat undertakes an administrative role and assists the Conference in the performance of its duties.*": Roe / Happold / Dingemans, p. 22.
[437] *Ibid.*, p. 23
[438] Apart from the topics focused on in this thesis, "*substantial development, political proceedings and general criticism on investor-state and intra-EU arbitrations*" has been closely analyzed with such purposes of modernization, and the referred topics are considered to be taken place at the center of the modernization process examined here. For further details, see generally, Thiessen, P.V.: *Reforming the Energy Charter Treaty for sustainability?*, Journal of Energy & Natural Resources Law, p. 2, available at https://www.tandfonline.com/action/showCitFormats?doi=10.1080/02646811.2022.2040214 (accessed on 22 August 2022).
[439] Verburg, p. 428.
[440] For a detailed timeline for such modernization process, *see*, https://www.energychartertreaty.org/modernisation-of-the-treaty/. Also, see, Thiessen, P.V., pp. 4-5.
[441] Verburg, p. 440.

proceedings have started.”[442] As an outcome of the Energy Charter Conference in November 2018, the Conference approved the inclusion of the DOB provision, *among others*, to be included within the scope of the modernization.[443]

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[442] For the Decision of the Energy Charter Conference on the Modernisation of the Energy Charter Treaty (CCDEC2017 23), dated 28 November 2017, *see*, http://dev.energychartertreaty.org/fileadmin/DocumentsMedia/CCDECS/2017/CCDEC201723.pdf. Also, as for the observation included in the referred phrase, there may emerge a rightful question mark regarding whether the DOB provisions without such explicit authorization should be interpreted in the way disapproving the invocation thereof before the commencement of arbitration proceedings, via *argumentum a contrario*. The same question, in the literature, was dealt with in relation to such explicitly authorizing clauses taking part in a few modern Canadian BITs, and the author observed the following: “*These new explicit provisions on the retrospective scope of DoB clauses raise the question whether in the absence of such a mention, a DoB clause could be invoked during the arbitration proceedings. These provisions could reasonably be interpreted as only confirming explicitly, for greater certainty, the implicit retrospective scope of DoB clauses.”* Côté, p. 7.

[443] The Decision of the Energy Charter Conference on the Modernisation of the Energy Charter Treaty (CCDEC2018 18), dated 27 November 2018, https://www.energycharter.org/fileadmin/DocumentsMedia/CCDECS/2018/CCDEC201818_-_STR_Modernisation_of_the_Energy_Charter_Treaty.pdf. In the meanwhile, the EU, as a contracting party to the ECT, began its preparations regarding such modernization process, and released a “*EU text proposal for the modernisation of the Energy Charter Treaty (ECT),*” in which it proposed modifications addressing the specific provisions of the ECT. The referred proposal seems to have touched upon the most critical and controversial facets of Article 17 of the ECT. Within the scope of that, the amendments on Article 17 text seem to address, *inter alia*, the jurisdiction v. admissibility question and the retrospective v. prospective effect difference regarding the application of the provision. The original text of the referred proposal is as the following:

> “*(5) Each Contracting Party ~~reserves the right to~~ may deny the application ~~advantages~~ of this Part and of Articles 26 and 27 of this Treaty to an investor of another Contracting Party or to ~~(1) a legal entity if citizens or nationals of a third state own or control such entity and if that entity has no substantial business activities in the Area of the Contracting Party in which it is organised; or~~*
> *~~(2)~~ an Investment, if the denying Contracting Party ~~establishes that such Investment is an Investment of an Investor of a third state with or as to which the denying Contracting Party:~~*
> *~~(a) does not maintain a diplomatic relationship; or~~*
> *~~(b)~~ adopts or maintains measures related to the maintenance of international peace and security, including the protection of human rights, that:*
> *(i) prohibit transactions with Investors of that state; or*
> *(ii) would be violated or circumvented if the benefits of this Part were accorded to Investors of that state or to their Investments, including where the measures prohibit transactions with a legal entity or a national who owns or controls either of them.*
> *For greater certainty, a Contracting Party may deny such benefits without any prior publicity or additional formality related to its intention to exercise the right conferred by this Article.”*
> [Emphasis provided by the drafters in the referred proposal, in the way that the underlined parts are for newly inserted parts, and the struck-through parts are for removed parts.].

For the EU text proposal for the Modernisation of the Energy Charter Treaty (ECT), see, https://trade.ec.europa.eu/doclib/docs/2020/may/tradoc_158754.pdf, p. 9.
As it would be seen in the following steps taken toward the modernization of the ECT process, the foregoing was adopted by the Energy Charter Conference partly. Also, the EU's approach toward such modernization process is submitted to be based on three interacting reference points: The modernization of the protection mechanism's scope, sustainability, and the modernization of ISDS mechanism. See, Thiessen, p. 5. The referred DOB provision elaboration seems to emerge as a part tangentially related to the last one.

Thereafter, the Conference adopted the policy options for the modernization process, in which it gave place to the party states' approaches toward the modification and modernization of specific provisions.[444] At the end of the process, the Energy Charter Conference issued a "*Public Communication explaining the main changes contained in the agreement in principle,*" dated 24 June 2022, where it declared the proposal of the Conference in relation to Article 17 as the following:

> "*To ensure effectiveness of the provision, the Treaty envisages the timeline for invoking the denial-of-benefits clause, including possibility to invoke it after the commencement of an arbitral proceeding. The denial-of-benefits clause will not be subject to an advance formal notification. The new provision clarifies the situations when the protection to an Investment may be denied, notably for maintenance of international peace and security, including the protection of human rights.*"[445]

Therefore, first, if such proposal is accepted by the contracting states to the ECT, then the prospective v. retrospective effect controversy is very likely to be concluded in favor of the former; this is because such amendment would result in the application of DOB rights even after the commencement of arbitral proceedings. Also, the removal of the prior publicity and notification requirement would serve the same purpose as well. Last, such change includes the "*maintenance of international peace*

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[444] For the Decision of the Energy Charter Conference on the Adoption by Correspondence – Policy Options for Modernisation of the ECT (CCDEC2019 08), dated 6 October 2019, *see*, https://www.energycharter.org/fileadmin/DocumentsMedia/CCDECS/2019/CCDEC201908.pdf, pp. 26-27.

[445] For the Decision of the Energy Charter Conference on Public Communication explaining the main changes contained in the agreement in principle (CCDEC2022 10), dated 24 June 2022, *see*, https://www.energycharter.org/fileadmin/DocumentsMedia/CCDECS/2022/CCDEC202210.pdf.

and security" within the diplomatic substantive requirement in line with other modern IIAs. Therefore, such modification and modernization seem to reflect, albeit up to a certain point, the *lege ferenda* that had been proposed in the literature until the commencement of such process.

The referred decision was planned to be communicated to the contracting parties to the ECT by 22 August 2022 for its adoption by the Energy Charter Conference planned to be held on 22 November 2022, and if accepted there unanimously as foreseen under Article 36.1(a) of the ECT, it is to "*enter into force 90 days after the ratification by three-fourths of the contracting parties*" in accordance with Article 42 of the ECT.[446]

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[446] The Decision of the Energy Charter Conference on Public Communication explaining the main changes contained in the agreement in principle (CCDEC2022 10), dated 24 June 2022, *see*, https://www.energycharter.org/fileadmin/DocumentsMedia/CCDECS/2022/CCDEC202210.pdf. Also, for the view in the way such mechanism would be unlikely to produce effective outcomes because of its resting upon the unanimity, see, Verburg, p. 445.

CONCLUSION

This thesis, as explained above, aims at a comprehensive and systematic analysis of the interpretation and application of DOB clauses in the international settlement of energy disputes. In such elaboration, first, one must recall that one of the most prevailing phenomena in international investment law since the beginning of the second half of the 20th century has been the tremendous expansion of BITs and accompanying access to MIAs, albeit in a very limited number, as the legal instruments devised to provide foreign investors with substantial and procedural protection mechanisms. Within such context, the ISDS mechanism has played a pioneering role in opening the doors of dispute settlement to investors, in their capacity of private law persons, by the provision of *ius standi*.

However, such opportunity has entailed with a number of attempts to abuse such protections, one of which—and the subject-matter of DOB clauses—is treaty shopping via mailbox companies. Addressing such concern, the DOB clauses came into the picture of international investment protection regime.

In this thesis, after the determination of the definition, purpose, scope, and boundaries of DOB clauses, the evolution of their formulations and components are analyzed. As a result of such analysis, it was set forth that their elements and wordings have been getting closer and uniformed as the time passed by, and such evolution has reflected the conversion of states' attitudes toward foreign investment in the way evolving from a protectionist standpoint to a position where they utilize such mechanism solely to prevent IIA abuses.

However, although DOB provisions seem to be formulated in a more and more harmonized manner; it is determined in this thesis that, in their interpretation and application by different tribunals, there may be major differences—specifically on the grounds of the ECT and non-ECT jurisprudences.

The first such divergence emerges in relation to the matter whether the invocation of DOB provisions should be evaluated as a jurisdictional or admissibility-related issue. Since Article 17 of the ECT only refers to the denial of benefits included in Part III, and Article 26 including the ISDS mechanism takes place under Part V; under the ECT jurisprudence, the tribunals have considered the invocation of the DOB provision as an admissibility-related issue. On the other hand, under the non-ECT jurisdiction, since the DOB provisions set forth a denial of benefits in the whole treaty or the chapter—where the ISDS provisions are given place as well—the tribunals decided that such denied benefits would include the benefit of ISDS mechanism as well; and, therefore, they ruled that the DOB invocation would be a jurisdictional issue. The fundamental difference between the two end lies in the reviewability of jurisdiction-related arbitral decisions, while the admissibility, as a part of merits, cannot be challenged.

After dealing with the foregoing matter, this thesis examined the criteria that needs to be fulfilled in order an investor and/or investment to be subsumed under the category denied of treaty benefits: the substantive requirements of DOB provisions. In this sense, first, the requirement to be under the ownership or control by a third-state national was examined. Within the scope of the ECT, the *Plama* case foresees that the ownership requirement would embrace the indirect and beneficial ownership, and the control requirement would be determined on a case-by-case basis considering if there is a substantial influence on the management and operations of the relevant legal entity. Another case, examined as a non-ECT jurisprudence representative, took the ultimate controller of the claimant and its nationality to account in the scrutiny of control in the case.

Following the requirement of the ownership or control by a third-state national, substantial business activity requirement was examined. The fundamental aspect of this inquiry seems not to diverge based on the ECT and non-ECT jurisprudences: the substantiality refers to the quality, but not the quantity, of the business in concern, which should be determined on a case-by-case basis, and it simply means that the legal entity with substantial business activities is the one that is not a mailbox company.

As for the third state/party definition, as an element with a central position in the other substantial requirements, the ECT and non-ECT jurisprudences do not differ: under BITs and MIAs the term has been considered to be referring to non-parties.

Having gone through the substantive requirements of DOB clauses, this thesis covered the procedural requirements that are to be fulfilled by respondent host states in order for them to be able to invoke the DOB rights and the application of DOB provisions by tribunals with regard to its effects. The essential issues in this context differing in the ECT and non-ECT jurisprudences, *inter alia*, are found to be as the following:

In the ECT jurisprudence, the tribunals ruled that the DOB rights should have been actively exercised; while in a part of the cases under non-ECT jurisprudence, the tribunals decided that the DOB clause was of an automatic effect upon the fulfillment of DOB requirements. Such difference seems to be dependent on the language employed by DOB provisions. The exercisable DOB provisions, including Article 17 of the ECT, explicitly states that parties reserve their right to deny or may deny the treaty benefits, while the provisions of automatic application states that such benefits shall be denied upon the meeting of pre-conditions therein.

At the point the DOB provision requires the active exercise on the side of the denying party, another question emerging there is how such exercise should take place. This question addresses two sides of the same coin: The manner of exercise against the putative investor and the requirements for party states to notify or consult with each other. As for the former, the ECT jurisprudence requires a prior publicity or notice to such effect, while the non-ECT jurisprudence does not foresee such requirement. As regards the latter, while a number of BITs and MIAs require a prior notification and/or consultation by and between the host state and home state, the ECT provision does not put forth such kind of interstate requirement.

Another question with regard to the application of DOB clauses is about the effect of invocation thereof: *retrospective v. prospective*. This is argued to constitute the most controversial and significant difference between the ECT and non-ECT jurisprudences. Unlike the non-ECT jurisprudence, the tribunals from the ECT jurisprudence determined that the invocation of DOB rights would result in prospective effect, which means the treaty protection that had been benefited from by the putative investor until the moment the DOB rights are exercised would not be affected by such exercise. The argumentation provided for such view is mainly based on, among others, the legitimate expectations of the putative investor for the protection of their investments under the applicable IIA regime. This view has been severely criticized for numerous reasons, mainly grounded on two major arguments: First, the respondent state could not be expected to inquire whether the DOB requirements are fulfilled or not before a dispute emerges or even a request for arbitration is served; and second, the DOB provision *per se* is a reservation in the relevant IIA, because of which the putative investor could not be assumed to have a legitimate expectation for its not being exercised. In practice, it appears that the DOB rights cannot be invoked mostly due to such approach of ECT tribunals. Therefore, the Energy Charter Conference included Article 17 within the scope of the modernization process that began in 2017 and proposed to re-formulate the ECT DOB formulation in the way enabling its invocation after the commencement of arbitration and not requiring a prior notification.

In a nutshell, Article 17 of the ECT in its present form, regardless of the relevant ECT modernization process, seems to practically disenable denying party to invoke it. Also, for certain reasons, including the language, systematic, and object-and-purpose formulation of the ECT, the ECT jurisprudence arguably differ from the non-ECT one in terms of almost all the critical aspects referred to above. In this sense, this divergence could be taken as a question mark casted on the argument that international energy investment law is "*an integral part of general international investment law*."[447]

In the light of the foregoing summary, in the author's view, the formulation, interpretation, and application of the ECT Article 17 cumulatively form the ground, on which the invocation of the DOB provision becomes almost impossible and impracticable for contracting parties to the ECT. In other words, considering the ECT's principal role in the global energy investment regime—resulting from the number of

[447] Shill, W. S.: *Concluding Observations: Foreign Investment in the Energy Sector: Lessons for International Investment Law*, Foreign Investment in the Energy Sector: Balancing Private and Public Interests (Eds.: De Brabandere, E. / Gazzini, T.), Brill Nijhoff, 2014, p. 268.

contracting parties and the scope of the treaty—host states have almost no protection against the described type of abuses of the liberal investment system.

In this sense, having analyzed the root cause of the foregoing problem, it appears that the interpretation and application of the substantive requirements is not a major part of the complication; since it mainly depends on the language employed by an IIA, and the ECT jurisprudence does not highly diverge from the non-ECT one in terms of the text and context of such requirements.

However, when it comes to the procedural facets of the DOB application in practice, the main difference emerges with regard to the nature of the DOB rights—that is, unlike the non-ECT jurisprudence, accepted to be an admissibility-related issue in the ECT jurisprudence—and the effect of the exercise of the DOB provision—that is considered to be of only prospective effect in the ECT jurisprudence. Although the manner of exercise and timing requirements also differ when it comes to the ECT jurisprudence, such difference mainly results from the prospective effect approach of tribunals.

In the quest for the normalization of the ECT DOB regime in terms of the referred two principal divergences, therefore, all the potentially functioning options should be taken into consideration: Redrafting the provision and academic support for a change in its interpretation by tribunals.

The above-described ECT modernization process aims at the former: redrafting Article 17 in the way confronting the highly restrictive application of the DOB rights. However, the final formulation achieved by the Energy Charter Conference only enables the exercise of DOB rights after the commencement of arbitration and aims at the removal of prior-notification requirement read by tribunals into Article 17. In this context, the admissibility-related nature of the DOB provision remains to be a divergence from the non-ECT jurisprudence. Such an approach is highly questionable when it is considered that Article 26 of the ECT—the ECT ISDS mechanism—only deals with the breach of the protections provided under Part III, which constitutes the sole scope of the DOB provision. Therefore, it would be more practical and result-oriented to include an indication that the invocation of such clause would also cover the benefit of arbitrating under Article 26 of the ECT.

Additionally, another issue that could be addressed and clarified by the way of amendment could and should be the definition of the third-state concept. Although it seems that there is a consensus among tribunals that such term refers to the non-parties to the ECT in the light of the *travaux préparatoires*, in the author's view, such approach brings about a gap that stems from the ECT's main characteristics of being an MIA. More precisely, as a MIA, the ECT brings more than two states together, unlike BITs, and in terms of the signature and ratification process, such states cannot interfere with each other: it is practically not possible for a state to disapprove the signature or ratification of the treaty by another state. This specifically draws importance in respect of the states not recognizing each other. Therefore, the present interpretation of the third-state term in Article 17, in the author's view, avails the non-recognized-state nationals to benefit from the ECT for taking the advantages of the investment protection to be provided by the contracting states, which would be beyond the purpose of such states while ratifying the treaty and constitute the abuse of such ECT protection that would otherwise have not been available to such investors. Therefore, as a result, such third-state definition could also be revised to include the third contracting-party states, with whom the host state does not maintain diplomatic relations.

Apart from the amendment option of the ECT, academic support for a change in Article-17 interpretation by tribunals seems to be another—if not the only—viable way to put the ECT DOB regime on the right track. In this sense, among others, specifically the prospective approach is of utmost importance; this is because it seems to be the principal factor turning the ECT Article 17 to be an impractical provision. At this point, one may recall that the ECT tribunals set forth several reasons for the application of prospective effect, the most prominent of which seems to be the protection of investors' legal expectations. However, it has been an argument on which the non-ECT tribunals frequently casted a doubt. That is, in the view also accorded by the author, the very existence of Article 17 itself would be considered as a prior notice to potential investors, and an investor being aware of such DOB provision in an IIA could not be considered to have any legitimate expectation in the way such provision would not be applied by the host state if the requirements are fulfilled. Also, the tribunals finding for the prospective effect mostly base such approach on the object-and-purpose interpretation of the ECT, which, in their view, foresees a "*long-term cooperation in the energy field*" under Article 2 that requires the prospective application of DOB rights. However, on the other hand, it could be argued that such an interpretation resulting in the impracticality of DOB rights for host states could result in their renunciation of the ECT system; therefore, it is questionable whether such prospective-effect approach serves or jeopardize the object and purpose of the ECT. This is, yet a hypothesis to be tested if the ECT modernization process fails around November 2022.

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