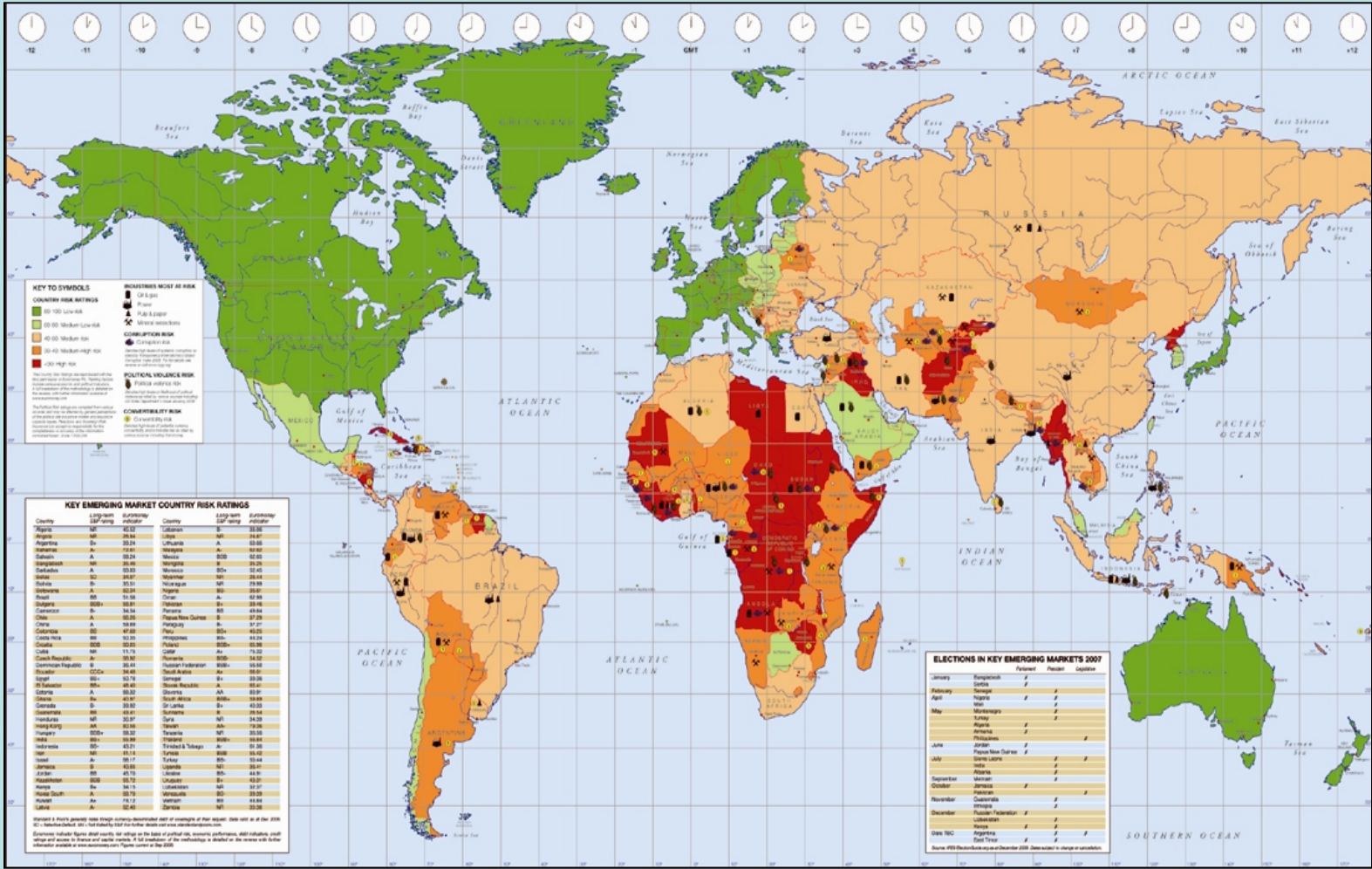


Political Risk Worldwide



Host State Interference and Non-protection: a Review of Recent Headlines

- “Foreign investors fear China law to curb monopolies”
Financial Times, August 31, 2007
- “Eni confirms Kashagan consortium to meet Kazakh authorities today”
Thomson Financial, August 27, 2007
- “WTO to probe China intellectual property protection”
Reuters, September 14, 2007
- “Zimbabwe bank chief warns over control of foreign firms”
AFP, October 2, 2007
- “Impact report clears Russian oil project”
New York Times, October 9, 2007
- “Finance ministry toughens stand on indirect FDI”
Business Standard (Mumbai) September 30, 2007

The Investment Treaty Solution to Political Risk

“Corporations are reported to begin structuring their transactions in such a way as to be able to benefit from the provisions of different BITs”

— ICSID, OECD, UNCTAD (2005)

BIT Planning: the basics

Agreements – Conventions and Treaties

- Bilateral Investment Treaties (BITs)
- Washington (ICSID) Convention
- NAFTA
- Energy Charter Treaty
- Recent Free Trade Agreements (FTAs)

Washington (ICSID) Convention

- Purpose: to increase international investment by facilitating settlement of investment disputes between governments and foreign investors
- An ICSID award is as enforceable in each contracting State as a final judgment of the domestic courts of that State
 - (but sovereign immunity still applies)
- 144 State Parties
 - But, not Brazil, India, Mexico, Angola or Canada (yet)
- Recent reported changes – Ecuador, Venezuela and Bolivia

ICSID Jurisdiction

- “The jurisdiction of the Centre shall extend to *any legal dispute arising directly out of an investment, between a Contracting State . . . and a national of another Contracting State*, which the parties to the dispute *consent in writing* to submit to the Centre...” (Art. 25)
- The convention does not define “investment”
- Note the requirement for written consent to submit a particular dispute to ICSID arbitration - ratifying the convention does not equal consent to arbitration at ICSID of any investment dispute

ICSID Jurisdiction: Nationality

- "*National of another Contracting State*" means:
 - any natural or juridical person with the nationality of another Contracting State; or
 - any juridical person with the *same* nationality as the respondent Contracting State, but which *because of foreign control*, the parties have agreed should be treated as a national of another Contracting State

Bilateral Investment Treaties (BITs)

- At the last count, there were over 2,500 BITs
- BITs:
 - contain the consent of state parties to arbitrate
 - define “investment”
 - set standards of protection for investments

BIT Definitions of “Investment”

- Typically, the definition of “investment” in a BIT provides that it means every kind of asset, including:
 - Movable and immovable property, as well as rights such as mortgages, license, pledges
 - Shares of companies and other kinds of interest in companies
 - Claims to money ... Claims to any performance having economic value
 - Intellectual property: copyrights, industrial property rights, know-how, goodwill
 - Public law business concessions, *e.g.*, concessions to search for or extract natural resources

BITs Define Protection

- Treatment:
 - “Fair and equitable treatment”
 - Non-discrimination
 - National treatment
 - Most-favored nation
- No expropriation without compensation
- Umbrella clauses
- Transfers

Protections and Reservations

Measures Tantamount to Expropriation

- One definition:
 - Effect of state's measures taken has been to substantially deprive the owner of title, possession or access to the benefit and economic use of his property

Treatment: Other Protections

- Ghana/UK BIT, Article 3:
 - Investments of nationals or companies of each Contracting Party shall at all times be accorded fair and equitable treatment and shall enjoy full protection and security in the territory of the other Contracting Party
 - Neither Contracting Party shall, in any way, impair by unreasonable or discriminatory measures the management, maintenance, use, enjoyment or disposal of investments in its territory of nationals or companies of the other Contracting Party

Violating Fair and Equitable Treatment

- Very fact-intensive
- Preamble in many BITs ties fair and equitable treatment with stable framework for investment
- Investor argues: depriving investor of guarantee or right that investor reasonably relied on when deciding to invest
- Has succeeded when expropriation claim fails
- Role of international law “minimum standard” topic of debate

Violation of Fair and Equitable Treatment

- Acting dishonestly and in bad faith
- Lack of transparency – government fails to inform investors of changes that will be made to fundamental legal regime

Protection: Umbrella Clause

- Turkey/USA BIT, Art. 2(3):
 - “Each Party shall observe any obligation it may have entered into with regard to investments”



Purpose & Effect

- Assures that State will perform obligations under its own law with regard to specific investment agreements
- Argument: any violation of these obligations or of a state contract is a treaty breach



Shareholder Claims

- “Direct” shareholders’ claims
- Indirect shareholders’ claims
- Minority shareholders’ claims allowed
- Special purpose vehicles

“Denial of Benefits”

- Denial of benefits clauses aim to eliminate treaty protection for “mailbox” companies
 - States can *deny* protection to “a legal entity if citizens of nationals of 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.*” (Energy Charter Treaty)
- Only operates prospectively

Assigning to Create Nationality?

- Dutch-Venezuela BIT
- Government notes negotiated to Netherlands Antilles holder; no dispute on nationality
- Claim on note
- Held, notes are “investment” under BIT and Washington Convention
- Can one assign an “investment?” Maybe

When to Plan Nationality?

- Structuring up the deal
- Post-signing, pre-dispute is not too late (at least under ICSID)

BIT Planning and Tax Planning

The Tax Caveat

ARTICLE XIII

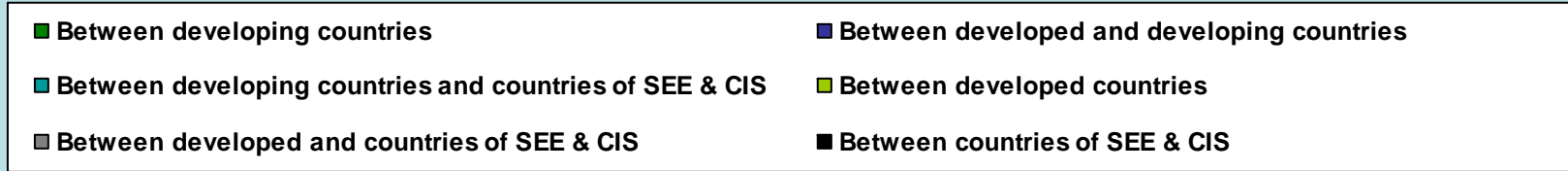
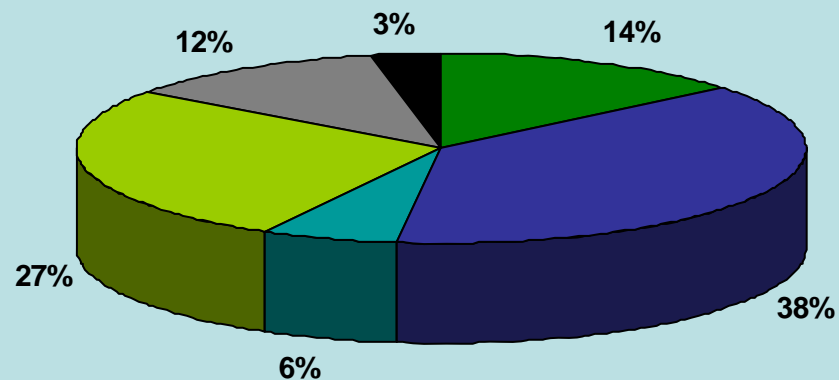
1. No provision of this treaty shall impose obligations with respect to matters, except that:
 - a) Articles III, IX and X will apply with respect to expropriation; and
 - b) Article IX will apply with respect to an investment or an investment authorization.
2. A national or company, that asserts in an investment dispute that a tax matter involves an expropriation, may submit that dispute to arbitration pursuant to Article IX(3) only if:

Tax Planning

- BIT planning can work hand in hand with tax planning
- One tip: check whether “home” country BIT extend to tax-advantaged former colonies, *e.g.*, Dutch Antilles, Bermuda, British Virgin Islands

IIAs and Tax Treaties will Increasingly Interact

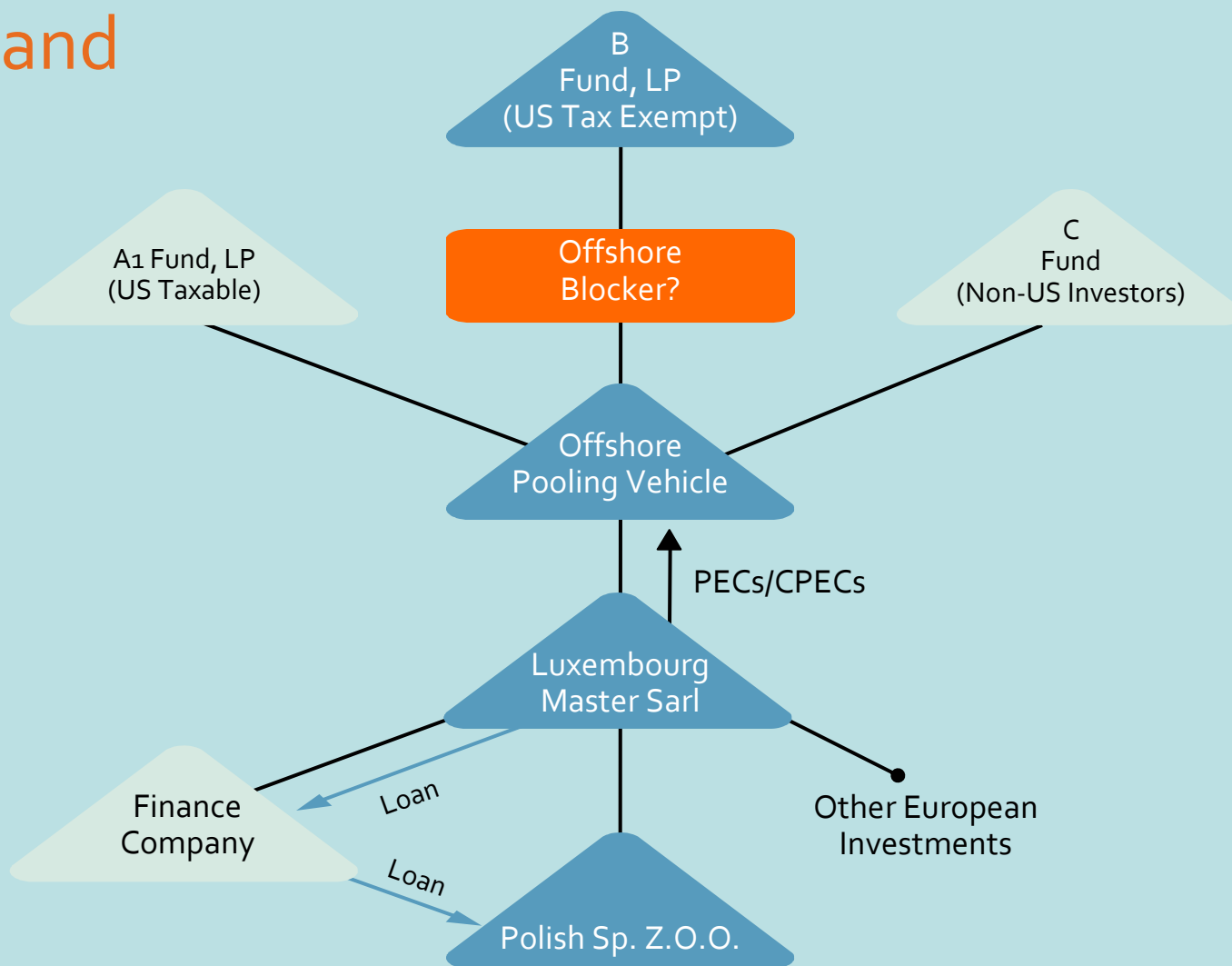
Figure 4. Total DTTs concluded, as of end-June 2006, by country group



How to Combine Tax and BIT Planning

- Savvy investors structure investments to leverage host-country BITs
 - If investor's home state has no BIT with host-state, channel through an entity located in a country that does
 - Even if investor's home state has a BIT with the host-state, the host state may have BITs with other countries that offer greater protections
 - Try to structure investment through those countries
 - Try to take advantage of most-favored nation clause
- Can structure deal to stack treaty protection
 - Multiple claims under different treaties before separate tribunals – more bites at the apple (*e.g., Lauder and CME*)

Example: Poland



Relationship Between Tax and BIT Structure

- US BIT protects US companies' investments, but is there an "investment"?
 - If "pass through," does BIT cover partnerships?
 - Is "indirect" investment expressly covered?
- Belgium/Luxembourg BIT protects lower down
 - But is there an "investment?"
 - Is there a "denial of benefits?"
- The finance company lending to the Polish entity
- Loans usually covered
- Nationality of lender?