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Analysis of Shareholder Claims in International Investments

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Abstract: *This article first explains the different types of the shareholder claims through a case presentation. Secondly, the paper analyses and examines the indirect claims of shareholders. The paper compares the indirect claims of shareholders with the direct claims of shareholders. By way of illustrating classic cases, the paper introduces the indirect claims of shareholders under customary international law and the indirect claims of shareholders under international investment arbitration. The paper also analyses and explains the problems that may arise from the exercise of shareholders' indirect claims. The above approach provides a deeper understanding of the indirect claims of shareholders. Then, the article analyses the issue of whether the corporate veil is revealed, which is a critical issue in shareholder claims. The paper provides examples of cases where the tribunal reveals the corporate cover and cases where the tribunal does not reveal the corporate veil to better understand whether the corporate veil is revealed. Finally, the article analyses some measures to address the issue of shareholder claims.*

Keywords: *shareholders claims, ICSID, indirect corporate investment*

1. Introduction

With the increase in international investment, international investment law has also been improving and developing in recent years. Shareholder claims are an essential issue in international disputes between state investors. This is because the type of shareholder affects whether the ICSID tribunal has jurisdiction over the case and whether the shareholder can assert their claim through the ICSID.

2. Claims by different types of shareholders

2.1 Shareholder control of a locally incorporated company in the host country

Typically, suppose a foreign investor has a locally incorporated company in the host country. In that case, if a shareholder claim arises, the local domestic law of the host country should be followed because the company is incorporated in the host country. There are, of course, exceptions. Under paragraph 2 of Article 25 of the ICSID Convention, "national of the other Contracting State" means (b) any legal person having the nationality of a Contracting State other than the State which is a party to the dispute at the date on which the parties to the conflict agree to submit the dispute to conciliation or arbitration. Any legal person having the nationality of a Contracting State which is a party to the debate at the said date, and which legal person is subject to foreign control, the Parties agree that it shall be deemed for this Convention to be a national of the other Contracting State. Under paragraph 2(b) of Article 25 of the ICSID, the investor may agree with the host State that because the company established in the host State is controlled by a company based in a third Contracting State, the company established in the host State may be treated as a company of the third Contracting State, i.e., the nationality of the company may be agreed. Reading this provision, this clause contains two substantive conditions: 1. The locally incorporated company must be effectively controlled by a national of the other Contracting State. 2. By mutual agreement[1-2].

The case of Amco Asia Corporation and others v. the Republic of Indonesia demonstrates the ICSID tribunal's interpretation of paragraph 2(b) of Article 25 of the ICSID. PT Amco was an Indonesian firm. Amco Asia controlled the PT Amco. Pan American Development Limited, a Hong Kong-based firm, was Amco Asia's controller. PT Amco, an Indonesian corporation, was considered a foreign entity in this case. The fact that the Indonesian government did not contest that PT Amco was a company controlled by foreign capital during its examination of the investment application created an implied agreement between PT Amco and the Indonesian government to recognize PT Amco as a company of another contracting state for the ICSID, according to the tribunal. Furthermore, a company whose name incorporates the word "PT" is deemed a foreign company under the Indonesian Corporations Act, a clear statement by the Indonesian government to differentiate foreign companies from domestic companies in Indonesia. As a result, the parties' agreement met the agreement required in paragraph 2(b) of Article 25 of the ICSID. Furthermore, Amco Asia controls PT Amco, satisfying paragraph 2(b) of Article 25 of the ICSID's control requires that a locally established firm be effectively controlled by a person of the other Contracting State. So, Amco Asia was able to file a claim against the Indonesian government. A domestically established firm in the host State is a foreign corporation if the two conditions laid out in paragraph 2(b) of Article 25 of the ICSID are met, as evidenced in Amco Asia Corporation and others v. the Republic of Indonesia. The person in control of the locally incorporated company in the host State may bring a claim against the ICSID in a State investor dispute with the host State.

2.2 Partial shareholding shareholders in the host country incorporated companies

In the case of a shareholder holding a portion of the shares of the host country incorporated company. If the host State causes damage to the shareholder holding a part of the shares, the shareholder may, subject to certain conditions, bring a claim before the Arbitral Tribunal as a claimant. The claimant, GAMI, a company incorporated in the United States, held a 14.18% interest in GAM, a locally incorporated Mexican company. The Mexican government subsequently appropriated a portion of GAM's shareholding, and GAMI commenced international arbitration against Mexico. The tribunal held that GAMI's minority ownership of GAM qualified as an "investment" under Article 1139 of NAFTA. The tribunal noted that if the claimant was the wholly owned parent company of GAM, it did not need preliminary relief from the respondent's court when seeking relief for the respondent's NAFTA violations. Similarly, where the claimant qualifies as an investment, the claimant's right to seek relief through international arbitration is not affected even if the claimant is a minority shareholder, whether the claimant is provided with preliminary relief by the respondent's court or not. The tribunal held that the claimant's rights were not affected by the practices of other shareholders and that the rights of foreigners under the regime established by NAFTA were not necessarily the same as those of their citizens, even about the same type of assets. In this case, the claimant was entitled to seek relief through international arbitration. Whether the respondent court agreed with the claimant's arguments did not change the claimant's right to seek relief through international arbitration. As to the relationship between the respondent's jurisdiction and the arbitration proceedings under NAFTA, the tribunal noted that the respondent court had based its decision on the law of that State, whereas this tribunal had relied on NAFTA. The tribunal said that, where possible, it would establish its decision with deference to the decision taken by the respondent court and avoid concluding that domestic law was inconsistent with international law. However, each adjudicating body is responsible for the legal norms within the scope of its exercise of competence. Article 27 of NAFTA provides that a party may not invoke the provisions of its domestic law as justification for its failure to perform a treaty. Therefore, how the domestic courts applied the domestic law was not relevant to the case. The tribunal further noted that if the applicant's claim under Article 1105 of NAFTA were based solely on the alleged "arbitrary and discriminatory nature of the expropriation of GAM's sugar mills", the jurisdiction of the case would be more contentious, as the applicant would not be entitled to assert a claim instead of GAM. However, the claimant's claim was not so but was directed to its investment, consistent with the definition of investment under NAFTA.

2.3 Shareholders with indirect shareholdings

In some cases, the claimant is not a direct shareholder of the company. In such cases, the investor can claim, through the intermediary of another company, for the damage suffered by the company in which it owns shares. In other words, if investor A owns shares in company B and company B owns shares in company C, can investor A claim for damage caused to company C by the host country. For example, in Siemens A.G. v. The Argentine Republic, the ultimate controlling shareholder, Siemens, through another German company, Siemens Information Systems, wholly owned, established a subsidiary, Siemens Technical Services, to invest in Argentina. The tribunal found all three companies to have German nationality. As all control relationships between the investor and the investment were not required in the German-Argentine BIT, the tribunal ruled that Siemens was an eligible plaintiff in the case[3-4].

Another example of indirect shareholder ownership is the case of Enron Corp. and Ponderosa Assets, L.P. v. the Argentine Republic. The claimant's involvement involved the privatization of Transportadora de Gas del Sur (TGS), one of the leading networks for the transportation and distribution of natural gas produced in the southern provinces of Argentina. The claimant owns 50% of CIESA, an Argentinian

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incorporated company that controls TGS by owning 55.30% of the shares. The claimant's participation in CIESA is held by two wholly owned companies, EPCA and EACH. The Claimants, through EPCA, EACH and another company controlled by the Claimants, ECIL, also own 75.93% of another Argentine company, EDIDESCA, which owns 10% of TGS; they also acquired an additional 0.02% of TGS through EPCA. It was explained that these investments amounted to 35.263% of TGS. In summary, the Claimants' shareholding in TGS was indirect. What is more, the Claimants held their shares in TGS through an intermediary in the host country. This contrasts with Siemens v. Argentina, where the claimant had its shares through an intermediary in the investor's home country. The tribunal stated: "While investors may bring claims in their own rights under the treaty terms, it is necessary to establish a cut-off point beyond which claims are not permitted because they have only a remote connection to the affected company. As this is essentially a question of the admissibility of the claim, the answer lies in determining the extent of the host State's consent to arbitration. If consent is given to the investor and the investment, it is reasonable to conclude that the claims made by that investor and the investment are admissible." In this case, the tribunal found that the claimant had made the investment at the invitation of the host government, Argentina, and therefore had standing as a claimant. But the issue of the cut-off point referred to in the case was hotly debated. Since there is no specific law governing the cut-off point, this cut-off point's determination became a controversial issue.

3. Shareholder indirect claims issues

When the relationship between the investor and the investment is one of equity, the investment takes the form of a company and shares. A distinction must be made between two different types of claims: firstly, shareholder direct claims: direct arbitration brought by a shareholder in their name for direct losses, where the direct losses are those suffered as a direct result of the equity interest. Secondly, indirect shareholder claims derivative arbitrations brought by shareholders in the company's name for indirect losses, where the indirect losses are the damage to the value of the shareholding itself. In the case of direct shareholder claims arbitration, the arbitral tribunal determines the shareholder's identity as the subject of the arbitration in the same way as other investors. In the case of shareholder indirect claims arbitration, the key to determining the appropriate shareholder investor is whether the shareholder has an indirect claim right, i.e. whether the shareholder has the right to initiate arbitration in the name of the company as a result of the loss suffered by the company. The unique feature of the indirect claim is that the shareholders file the arbitration claim on behalf of the company, not in the traditional sense where the shareholders suffer a direct loss in their own rights and seek relief in their name.

3.1 Differences between indirect and direct claims

Although both indirect and direct claims are brought by shareholders and are directed against the wrongful acts of the host country, there are the following differences. Direct claims: In a direct claim, the shareholder suffers a loss due to violating their rights. In addition, direct claims may be brought against the host country for the violation of the rights of foreign shareholders in a local company if the wrongful act of the host country violates the rights of the shareholders under customary international law and direct investment agreements between the host country and the country of nationality of the shareholders. Indirect claims: In an indirect claim, the shareholder's rights have not been violated per se; the value of the shareholder's shares may fluctuate due to the violation of the company's rights. In addition to this, indirect claims brought by shareholders cannot be exercised through the diplomatic protection route.

3.2 Shareholder indirect claims under customary international law

In traditional international law, shareholders are entitled to claim compensation when the host country infringes on their direct rights. The availability of protection when a shareholder's indirect interests are infringed is controversial, as there is a significant difference between an infringement of ownership and a loss of interest. When the host State infringes the corporation's rights, diplomatic protection can, in principle, only be exercised by the State of the nationality of the corporation. The State of the nationality of the shareholders is not entitled to exercise diplomatic protection in respect of consequential damages suffered by them. The Barcelona Traction case is an important case in international law concerning the diplomatic protection of a corporation by the State of the nationality of the shareholders in respect of an injury to the indirect interests of the shareholders. The arbitral tribunal noted that, since international law had not established any clear rules on the treatment of the rights of States concerning corporations and

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shareholders, only the State of the nationality of the corporation was authorized under the general rules of international law to bring a compensation claim. Although the State of the nationality of a shareholder of a company may be exempted from these general rules in exceptional cases where the rights of the shareholder of the company itself have been violated, where the company has ceased to exist, where the State of the nationality of the company cannot act on behalf of the company or where the State of the nationality of the company is the responsible State, these exceptions did not exist in this case. Finally, the Court held that Belgium did not have the right to bring the case before the Court on behalf of its shareholders and dismissed Belgium's application. In short, in traditional international law, only in very exceptional circumstances would shareholders be allowed to break through to the corporate level to pursue their claims. In short, under customary international law, shareholders are usually not entitled to exercise indirect claims, excluding only in very exceptional circumstances.

3.3 Shareholder indirect claims under international investment arbitration

In contrast to customary international law, shareholders are entitled to bring indirect claims based on the investment agreement in international investment agreements. Moreover, the prohibition on the exercise of indirect claims by shareholders under customary international law does not prevent shareholders from exercising their indirect claims based on the investment agreement. This is because customary international law has a separate and distinct jurisdiction from international investment arbitration. Customary international law applies to diplomatic protection, as in the Barcelona Traction case, which was decided based on customary international law. But international investment arbitration is governed by international investment agreements. Provisions from international investment agreements authorize the exercise of indirect claims by shareholders.

3.4 Issues arising from a shareholder's indirect claim

A shareholder's right to indirect recourse means that the shareholder can bring a derivative arbitration in the name of the company to cover the company's losses. Apart from the potential damage to the separate personality regime of the company, this approach would broaden the scope of eligible investors in investor-state arbitration. This is because indirect claims extend the relationship between the investor and the investment, and some investment losses that would not otherwise belong to the shareholder are subsumed under the shareholder's investment losses by the existence of an indirect claim. The extended investor-investment relationship is critical in determining whether a shareholder is entitled to an indirect claim. The extended relationship makes more shareholders eligible for an indirect claim, even those who would not otherwise be entitled to an indirect claim under an international investment treaty. The implications of the expansion of the investor-investment relationship are significant. In addition to the positive effects of attracting investment, we should be wary of specific adverse effects, particularly the forced multilateralism of the investment relationship. For example, the involvement of the country of nationality of the shareholders, in the investment relationship between the original host country and the company's home country complicates an otherwise simple investment relationship.

Under different investment agreements, various shareholders can claim for the same violation against the host country, which inevitably results in multiple claims and thus increases the likelihood of conflicting awards. Lauder v. The Czech Republic and CME v. The Czech Republic are typical examples of multiple claims by shareholders. In Lauder v. The Czech Republic, Lauder, a US citizen, effectively controlled a Dutch CME company, while CME held 99% of the equity of a local Czech company, CNTS. Subsequently, the local company was involved in an investment dispute with the Czech government, and Rhodes initiated an arbitration claim. The arbitral tribunal found that jurisdiction over the case was recognized under the US-Czech Republic BIT. However, six months later, Rhodes, through CME Corporation, initiated another investment arbitration. Although based on the same facts, the arbitral tribunal reached opposite conclusions on the two arbitrations. The tribunal found that the plaintiffs in the two arbitrations were different, one being a controlling shareholder of CME and the other being a CME company. Although the two arbitrations used various bilateral investment agreements, the tribunal found that the investment agreements gave the shareholders similar, rather than identical, investment protection and allowed indirect claims. As seen from these two cases, the system of indirect shareholder claims, while offering some benefits, can also lead to multiple claims and increase the likelihood of conflicting awards.

The recognition of shareholder investors as the subject of indirect claims can also exacerbate investors' incidence of treaty shopping. Treaty shopping is the process by which investors seek to obtain optimal protection under international investment treaties through nationality planning, usually between

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the host country in which they invest and another country whose nationality they do not otherwise possess and by which they obtain the nationality of the other country to enjoy optimal protection. In summary, the motivation behind treaty shopping is the desire for better treatment. Multinational companies often select treaties by creating shell companies or by restructuring their companies, both of which are essentially ways for investors to plan their subsidiaries' nationality to meet the nationality requirements of international investment treaties for investors. Where indirect and minority shareholders can also initiate derivative arbitration, it becomes extremely easy for investors who satisfy the nationality requirement but has no connection to the investment to take advantage of such mechanisms and thus fulfill the equity requirement in the treaty and successfully initiate arbitration as shareholders. Allowing shareholders to exercise indirect claims to initiate derivative arbitration enables multinational companies to select preferred targets for equity transfers from their preferred country of nationality, allowing home country investors who do not have an investor-investment relationship to become eligible investors under international investment treaties. In short, shareholders' possession of indirect claims may lead to treaty shopping abuses.

4. Lifting the corporate veil issue

4.1 Tribunal refuses to lift the corporate veil

The arbitral tribunal refused to lift the corporate veil in the case of Tokios Tokelés v. Ukraine. The plaintiff, a company registered in Lithuania, had invested by establishing a subsidiary in Ukraine and subsequently had an investment dispute with the Ukrainian government and sought to initiate arbitration under the BIT between Lithuania and Ukraine. The defendant argued that the plaintiff, although registered in Lithuania, was 99% controlled by Ukrainian nationals and had no substantial business activities in Lithuania and therefore did not meet the nationality requirement for an investor. However, the tribunal held that the investor's nationality should be determined by the BIT provisions in question, which in this case provided that the Lithuanian investor was any entity established in the territory of Lithuania under Lithuanian law and without other conditions. Thus, although Ukrainian nationals substantially controlled the plaintiff, it was sufficient to be installed in its region under Lithuanian law. The investor's nationality was determined strictly by the provisions of the BIT. In this case, the tribunal refused to lift the corporate veil.

4.2 Tribunal upholds the lifting of the corporate veil.

In TSA Spectrum de Argentina S.A. v. Argentine Republic case, the tribunal upheld the lifting of the corporate veil. The plaintiff was an Argentine subsidiary wholly owned by a Dutch company, which was ultimately owned by an Argentine national. The tribunal, in this case, held that the corporate veil should be lifted to determine whether there was genuine foreign control, thereby finding that the plaintiff's ultimate beneficial owner was an Argentine national and therefore plaintiff did not have right to claim over the case. In this case, the tribunal not only lifted the corporate veil but also held that the arbitrator should explore who exercised ultimate control over the company in dispute, i.e., lift multiple layers of veils. Apart from that, In SOABI v. the State of Senegal case, SOABI was a company incorporated in Senegal. Still, the parent company controlling SOABI was NAKIDA, a company incorporated in Panama, which was not a member of ICSID. A Belgian company controls NAKIDA. The problem then arises that if the corporate veil is not lifted, the company controlling SOABI is NAKIDA, registered in Panama. Since Panama is not a member of the ICSID, the ICSID has no jurisdiction over the case. If the corporate veil is lifted, the ultimate beneficial owner of the SOABI is a Belgian company, and NAKIDA, registered in Panama, is seen as a platform used by the Belgian company for investment purposes, and ICSID has jurisdiction over the case. The tribunal ultimately found that the Belgian company was the controller of SOABI and that the tribunal had jurisdiction over the case. It can be seen that the arbitral tribunal, in this case, argued for the lifting of the corporate veil.

For arbitral tribunals, whether to lift the corporate veil depends on the tribunal's value proposition. However, in today's practice, the inconsistency of the decisions of the various arbitral tribunals has led to the question of whether to lift the corporate veil becoming more acute or not. There is much debate about how many layers of the corporate veil should be lifted before the end. In short, if the tribunal had only considered the level of the foreign company controlling the host company and had not conducted an in-depth investigation, it would not have resulted in an endless investigation and a decision that would have been contrary to the original intent of the ICSID legislation. However, based on the current conflicting cases and the trend of ICSID decisions, if only the level of the foreign company controlling

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the host company is considered, other factors need to be further considered to ensure the security of the international investment structure. For example, to prevent problems such as the emergence of shell companies.

5. Some attempted measures to prevent shareholder claims

5.1 Introduction of a consolidated arbitration clause

The introduction of a consolidation clause is enshrined in NAFTA. Under Article 1126 of NAFTA, consolidation of arbitration provides that an arbitral tribunal constituted by this Article may, after a hearing of the parties to the dispute, decide to consolidate jurisdiction to resolve claims fairly and efficiently where there are common questions of law or fact in the arbitration, and to state the reasons for such a decision to consolidate jurisdiction. Under this provision, the host State may apply for the consolidation of arbitrations brought against it by multiple shareholders based on the same investment dispute. This would reduce the pressure on the host country to focus on one consolidated case rather than having to spread out similar arbitrations. In addition, the consolidation of similar cases can go a long way toward avoiding inconsistent decisions. Consolidated arbitration clauses are gradually being adopted in FTAs and BITs concluded by NAFTA members. In addition, there are also cases of consolidated arbitration based on the provisions of NAFTA in the practice of investor-State investment dispute arbitration.

Consolidated arbitration has the following advantages. Firstly, consolidation may, in some cases, be more efficient than separate arbitration hearings and may save on legal fees, arbitrators' fees, witness time, preparation of the case, and other similar costs incurred in litigation. The negative impact of shareholders exercising their indirect claims is curbed by having a consolidation clause. Secondly, consolidation provides a practical and helpful way of avoiding conflicting awards to a large extent by bringing some cases together before the same tribunal. In short, creating a consolidation clause can prevent the harmful effects of the exercise of indirect claims by shareholders.

5.2 Introduction of a waiver clause

A waiver clause can go some way to avoiding the problem of duplication of remedies in shareholder claims. Under Article 1121 of NAFTA, both the shareholder and the local company submitting the investment arbitration must waive their domestic remedies in the host country. Having a waiver clause can reduce investors' abuse of their claims and prevent investors from seeking duplicative relief in different settlement procedures. Currently, many investment agreements have provisions similar to those in NAFTA. In IIAs, many contracting states will have waiver clauses to protect their national interests and prevent investors from abusing their right to sue. However, it is essential to note that an investor's waiver of other forms of relief must comply with its requirements in form and substance. In practice, however, waiver clauses have also revealed some drawbacks for investors and have posed a specific risk to them. In practice, until the arbitral tribunal reviews the substance, the investor cannot determine whether the host government has acted in breach of its obligations under the investment agreement. In this case, the investor has waived other remedies through a waiver. If the tribunal rejects the shareholder's request for arbitration, the shareholder will not have access to other remedies. This is equivalent to a waiver of the shareholder's right to seek redress by other means in advance. Therefore, in practice, it is essential to use the waiver clause reasonably to protect the shareholder's right to claim compensation and avoid the duplication of remedies.

6. Conclusion

Shareholder claims are an essential issue in state investor dispute arbitration. The right of shareholders to indirect claims is critical in shareholder claims issues. When the host government infringes an equity interest, the shareholder can claim compensation from the host government under the IIA. A study of international investment arbitration cases shows that some arbitral tribunal cases have recognized the right of shareholders to indirect claims. Although indirect claims by shareholders may conflict with customary international law, arbitral tribunals have primarily recognized the legitimacy of indirect claims. Arbitral tribunals have also recognized indirect claims by the minority, majority, and indirect shareholders. The right of shareholders to exercise indirect claims has some benefits. But it also raises several questions. In addition to this, whether to lift the corporate veil is also an essential issue in

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the context of shareholder claims. An analysis of cases relating to whether or not to lift the corporate veil shows that whether or not to lift the corporate veil depends to some extent on the value proposition of the arbitral tribunal. In international investment arbitration practice, some responses to the problems posed by shareholder claims have been proposed, such as the creation of consolidation arbitration clauses and the creation of waiver clauses. In conclusion, in the practice of international investment arbitration, States should pay due attention to the provisions of international investment agreements entered into externally to shareholder claims. Countries should work together to create a friendly investment environment.

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