

## State Enterprises And The Presumption Of Statehood In Investment Arbitration

*Nasr A. Ashoush*

*PHD Candidate*

*University of Burgundy (CREDIMI), France*

[Ashoush48@gmail.com](mailto:Ashoush48@gmail.com)

**Abstract:** A foreign investor rarely contracts with the state itself in the context of international economic connections, but rather with one of the state's instrumentalities "that possesses a legal identity separate and autonomous from the State." State enterprises, regulatory bodies, infrastructure agencies, development agencies, and municipal governments are all examples of state instrumentalities. Those instruments must be separated from state institutions, and the existence of legal personhood is central to that separation. An organ is an entity that is not independent of the state and has that status under that state's domestic legislation.

The fact that it is closely linked to the state has always fueled debate about the identity of such an enterprise. Whether it is a truly independent entity or merely a state organ hiding behind its legal personality to carry out the state's policies? In response to this question, some argued that the classic distinction between organ and enterprise should be maintained, while others argued that the latter should be a state organ. In this paper, we will focus on the answer provided by investment arbitration jurisprudence (II) to this question, and then we will look at how some recent and important free trade agreements have approached the issue in order to create their own *lex specialis* set of rules on the subject (III).

**Keywords:** State Enterprises, Investment, Arbitration, *Lex Specialis*.

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## **I. Introduction**

In the framework of international economic relationships a foreign investor is rarely contracting with the state itself but mostly with one of its instrumentalities “that possesses a legal personality distinct and autonomous from the State”<sup>1</sup>. There are varieties of state instrumentalities such as State enterprises, regulatory bodies, infrastructure agencies, development agencies and local authorities. Those instrumentalities are to be distinguished from state organs and the existence of legal personality is at the crux of that distinction. An organ is an entity that is not separate from the state and has that status under the domestic law of that state<sup>2</sup>.

One of the renowned state instrumentality is the state enterprise, the magic tool that is “clothed with the power of government but possessed of the flexibility and initiative of a private enterprise”<sup>3</sup>. The fact that it’s closely linked to the state foment always the controversy about the identity of such enterprise. Whether it’s a real independent entity or it’s merely a state organ behind its legal personality the state is hiding to implement its policies? In answering this question some maintained the classic distinction between organ and enterprise<sup>4</sup> while others argued that the latter should be a state organ<sup>5</sup>.

The distinction between the two entities is relevant for the purpose of attribution of the instrumentality’s conduct and thus responsibility. While a state is always liable for the conduct of its organ whether it’s commercial or governmental, this is not the case for a state enterprise whose commercial acts, in theory, don’t incur the liability of the state. The extreme example quoted by Gallus explains it clearly “A Ministry's purchase of office equipment, such as pencils, is attributable to the State. If the Ministry's conduct in its office equipment purchases is inconsistent with the

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<sup>1</sup> Luca Schicho, “Attribution and State Entities: Diverging Approaches in Investment Arbitration,” *The Journal of World Investment & Trade* 12, no. 2 (January 1, 2011): 283–98, p.284.

<sup>2</sup> E Silva ROMERO, « Are state liable for the conduct of their instrumentalities » in *IAI series on international arbitration: State entities in international arbitration (E. Gaillard and J. Younan eds.,2008)*, Juris publishing, Paris, 2011, p.33.

<sup>3</sup> Nick Gallus, “State Enterprises as Organs of the State and BIT Claims,” *The Journal of World Investment & Trade* 7, no. 5 (January 1, 2006): 761–79, p.777.

<sup>4</sup> See cases below.

<sup>5</sup> GALLUS, *supra*, footnote 3, p.778.

State's international law obligations, the conduct entails the international responsibility of the State. Conversely, a State agent's [state enterprise]<sup>1</sup> purchase of office equipment is normally not attributable to the State, as it is not exercising any governmental authority. Consequently, a person harmed by the agent's purchase of office equipment cannot seek remedies in international law, even if the agent's conduct in the purchase would have amounted to a breach of international law if performed by a State organ."<sup>2</sup>Hence, an investment arbitration tribunal sitting to judge a dispute involving a state enterprise has primarily to determine whether or not that enterprise is a state organ in order to know which conducts are to be attributable to the state.

In this paper we will focus on the answer provided to this issue by the investment arbitration jurisprudence (II) and then we will see how some recent and important free trade agreements had tackled the question to create their own *lex specialis* set of rules on the matter (III).

## **II. The attribution of state enterprises' acts to the state in investment arbitration jurisprudence:**

Before tackling the related jurisprudence to the issue (B) we have to pass through a quick reminder of the international law commission's articles on state responsibility (ILC's articles) (A). It's thus necessary to make a brief reminder of those articles and see how some jurisprudence used it correctly while others combined them without a clear vision on the ground chosen to attribute the conduct.

### **A. Different grounds for attribution in the ILC's articles:**

#### *Article 4*

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

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<sup>1</sup> Emphasis added by us.

<sup>2</sup> GALLUS, *supra*, footnote 3, p.765.

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*of the State. 2. An organ includes any person or entity which has that status in accordance with the internal law of the State.”<sup>1</sup>*

This is the ground used to attribute to the state the conducts of ministries<sup>2</sup>, provinces and federated states<sup>3</sup>. Once the tribunal is certain that, according to the state law, the entity is not an article 4 organ it has to proceed to article 5 which attributes the conduct on a functional (material) basis.

#### *Article 5*

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

The text of article 5 raises some questions; the first is in respect of what is considered as governmental authority? An issue that depends on “the particular society, its history and traditions”<sup>4</sup>. The second is whether or not the entity is empowered to exercise elements of governmental authority? And the third is whether the disputed conduct involves governmental authority? In many cases tribunals found entities to be empowered to exercise governmental authority but didn’t held them liable as the disputed conduct didn’t entail a governmental authority<sup>5</sup>.

#### *Article 8*

*“The conduct of a person or group of persons shall be considered an act of a State under international law if the person or group of persons is in fact acting on*

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<sup>1</sup> Draft Articles on Responsibility of States for Internationally Wrongful Acts, with Commentaries – 2001.

<sup>2</sup> ROMERO, *supra* note 2, p.33.

<sup>3</sup> Compañía de Aguas del Aconquija S.A. and Compagnie Générale des Eaux (Vivendi Universal) v. Argentine Republic (ICSID Case No. ARB/97/3), Award, Nov. 21, 2000, 5 ICSID REP. 296, ¶ 49, at 313 (2002).

<sup>4</sup> *Supra* note 8, at 43.

<sup>5</sup> Jan de Nul v. Egypt, Award, 6 November 2008, paras. 169-171; Bayindir v. Pakistan, Award, 27 August 2009, para. 123; EDF v. Romania, Award, 8 October 2009, para. 195. Discussed below.

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*the instructions of, or under the direction or control of that State in carrying out the conduct.”*

The conduct of an entity may be attributed under this article for reasons such as instructions given to members of the board of directors, authorization from the government for particular decisions, and decision-making bodies that are composed of State officials<sup>1</sup>.

The aim here is to clarify that those articles exclude one another so that a tribunal cannot base its decision on several articles. Hence, a conduct cannot be “empowered” to the entity by the state and simultaneously be “controlled” by the latter<sup>2</sup>, it’s either “empowered” so that attribution could be made under article 5 or “controlled” by the state and thus attributed to it under article 8. If it has been substantiated that the entity at stake is an article 4 organ, there would be no need to check the applicability of the two other articles. As mentioned earlier a state is responsible for every act of its organs whether commercial or governmental.

This differentiation between the attribution grounds is respected by some tribunals while ignored by others. Regarding the latter the well-known Maffezini case made a good example thereof. The tribunal, based on a structural or formal test, stated that “a finding that the entity is owned by the State, directly or indirectly, gives rise to a rebuttable presumption that it is a State entity”.<sup>3</sup> After finding that the state enterprise may take many forms and thus deciding the issue solely on the structural criteria wouldn’t be conclusive the tribunal proceeded to assess the functional test<sup>4</sup>. The tribunal stated the analysis of the CSOB case and held that “By the same token, a private corporation operating for profit while discharging essentially **governmental functions** delegated to it by the State could, under the functional test, be considered as an **organ of the State** and thus engage the State’s international responsibility for wrongful acts.”<sup>5</sup> The confusion between the two grounds, structural (article 4) and functional (article 5), is very obvious in

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<sup>1</sup> See cases in Luca, *supra* note 1, p.288.

<sup>2</sup> Emilio Augustin Maffezini v. Kingdom of Spain ((ICSID Case No. Aim/97/7), Award, 13 November 2000. 5 ICSID Rep., para. 71.

<sup>3</sup> Emilio Agustín Maffezini v. Kingdom of Spain (ICSID Case No. ARB/97/7), Decision on Jurisdiction, Jan. 25, 2000, 16 ICSID REV. 212 (2001); 40 I.L.M. 1129 (2001), para 77-79.

<sup>4</sup> *Id.* para 79.

<sup>5</sup> *Ibid.* para 80.

the last paragraph. A private corporation seeking profits and meanwhile discharging governmental functions is a state entity “which is not an organ of the state” in terms of article 5.

Finally the tribunal decided that SODIGA (the entity at issue) fulfilled both structural and functional tests and is thus a “state entity acting on behalf of the state”<sup>1</sup>. What seems interesting in this award is that the tribunal didn’t give much weight to the state internal law which, it said, “is not necessarily binding on an international arbitral tribunal”. It added that “Whether an entity is to be regarded as an organ of the State... is a question of fact and law to be determined under the applicable principles of international law”<sup>2</sup> this plainly contradicts the text of article 4. Maybe, as mentioned by Manciaux, the fact that the ILC’s articles had not yet been adopted when these decisions were rendered had affected the tribunal’s decision<sup>3</sup>.

In *Encana vs Ecuador*, Petroecuador is a State-owned enterprise created to conclude participation contracts with foreign investors to exploit natural resources. The tribunal found that the entity was subject to instructions from the President and to the power of the Attorney-General "to supervise the performance of [...] contracts and to propose or adopt for this purpose the judicial actions necessary for the defense of the national assets and public interest". This power extended to "supervision and control of Petroecuador's performance of the participation contracts and to their potential renegotiation". The tribunal held the conduct complained of to be attributable to the State as it was related to the entering into, performing and renegotiating of those participation contracts. It concluded that it "does not matter for this purpose whether this result flows from the principle stated in Article 5 [...] or that stated in article 8 the result is the same"<sup>4</sup>.

A similar hesitation between attribution grounds is noticed in *Waste management vs Mexico*. In respect with article 4 the tribunal noted that “from the material

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<sup>1</sup> Ibid para 89.

<sup>2</sup> Ibid. para 82.

<sup>3</sup> Sebastien Manciaux, “The Relationships between States and Their Instrumentalities in Investment Arbitration”, in *IAI series on international arbitration: State entities in international arbitration* (E. Gaillard and J. Younan eds.,2008), *op.cit*, p.220.

<sup>4</sup> *EnCana v. Ecuador*, (Lem Case No. UN3481), Award, 3 February 2006, para 154.

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available to the tribunal, it was doubtful whether Banobras is an organ of the Mexican State within the meaning of Article 4”. And added that “The mere fact that a separate entity is majority-owned or substantially controlled by the state does not make it ipso facto an organ of the state”. Regarding article 5 it declared that “Nor is it clear that in its dealings with the City and the State in terms of the Line of Credit it was exercising governmental authority within the meaning of Article 5 of those Articles”. As for article 8, it stated that “A further possibility is that Banobras ... was acting “under the direction or control of” Guerrero or of the City...” And it concluded by saying that “one way or another the conduct of Banobras was attributable to Mexico for NAFTA purposes.”<sup>1</sup>

On the other hand other jurisprudence differentiates duly between the attribution grounds. In *Jan de Nul v. Egypt*, after finding that, under domestic law, the Suez Canal authority (SCA) is not qualified as a state organ the tribunal proceeded to article 5<sup>2</sup>. The tribunal noted that SCA was empowered to exercise governmental authority, however it held that acts complained of were of commercial nature and not “*prérogatives de puissance publique*”<sup>3</sup>. At the third phase of assessment the tribunal held that “there was no evidence of any instructions given in regard to the specific acts complained of, these could not be attributed pursuant to Art. 8”. And thus it concluded that the conduct wasn’t attributed to the state.<sup>4</sup>

Another good example for the distinction between the attribution grounds is *Bayindir v. Pakistan*. Per article 4 the tribunal noted that “The fact that there may be links between NHA and some sections of the Government of Pakistan does not mean that the two are not distinct. State entities and agencies do not operate in an institutional or regulatory vacuum.” It added “Because of its separate legal status, the Tribunal discards the possibility of treating NHA as a State organ under Article 4 of the ILC Articles.”<sup>5</sup> The tribunal then moved to article 5 and decided that “It is not disputed that NHA is generally empowered to exercise elements of

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<sup>1</sup> *Waste Management Inc. v. United Mexican States (ICSID) Additional Facility Case No. Akts(AF)/00/3*, Award, 30 April 2004, 43 ILM 967 (2004). Para 75.

<sup>2</sup> *Jan de Nul v. Egypt (ICSID Case No. ARB/04/U)*, Award, 6 November 2008, para 162.

<sup>3</sup> *Ibid.* para 169.

<sup>4</sup> *Ibid.* para 174.

<sup>5</sup> *Bayindir v. Pakistan (ICSID Case No. Ann/03/29)*, Award, 27 August 2009 (available at: <http://ita.law.uvic.ca/documents/Bayandiraward.pdf>), para 119.

governmental authority”. However, it found that the NHA wasn’t acting in the exercise of elements of the governmental authority.<sup>1</sup> Finally, the tribunal has reviewed the parties' arguments and evidence to conclude that “NHA's conduct is attributable to Pakistan under Article 8 of the ILC Articles.”<sup>2</sup>

## **B. Proper ground for attribution of state enterprises’ conduct to the state:**

Here we come to the core issue that is to know the status of a state enterprise; an “article 4 state organ”, as explained by some authors<sup>3</sup>, or an “article 5 entity” that is only charged with some governmental authorities. The scenario concern almost an enterprise that is, according to the state internal law, incorporated as commercial company with its own legal personality, meanwhile is structurally shaped as a state organ and functionally serves public purposes. Here we will analyze a range of tribunals’ decisions demystifying this point.

### **Salini vs Morocco**

This dispute arose out of a road building contract between ADM (Societe Nationale des Autoroutes du Maroc) and the Italian contractor (Salini). Due to some unforeseen circumstances Salini was obliged to bear more expenses and to complete the project 4 months earlier than expected. After receiving no reply from ADM regarding the compensation for the additional expenses, Salini decided to lodge a claim against the government of Morocco before ICSID<sup>4</sup>.

In respect of the status of ADM, the kingdom of Morocco argues that it’s a private legal entity holding its own assets. It added that “the fact that the State exercises its rights as shareholder and licensor should not have any effect on the legal autonomy of ADM”<sup>5</sup>. However, Salini claims that ADM is a public legal entity despite its incorporation as a limited liability company. Salini referred to “the

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<sup>1</sup> Ibid. para 123.

<sup>2</sup> Ibid. para 125.

<sup>3</sup> See Gallus, *supra* note 3.

<sup>4</sup> Salini Costruttori S.p.A. and Italstrade S.p.A. v. Kingdom of Morocco (ICSID Case No. ARB/00/4), Decision on Jurisdiction, July 23, 2001, 42 I.L.M. 609 (2003); 6 ICSID REP. 400 (2004); French original in 129 J.D.I. 196 (2002) (observations by E. Gaillard at 209). Paras 1-5.

<sup>5</sup> Ibid. para 28.

composition of its assets and its Board of Directors at the time of its creation and the direct involvement of the Minister of Infrastructure in all fundamental decision-making relating to the contract establish the active participation of the State”<sup>1</sup>.

The tribunal commenced from a presumption that “any commercial company dominated or predominantly controlled by the State or by State institutions, whether it has a legal personality or not, is considered to be a State-owned company”<sup>2</sup>. The tribunal embraced the same line of reasoning as *Maffezini* and assessed both the structure and the functions of ADM to conclude that the latter “is distinguishable from the State solely on account of its legal personality” and that it is “a State company, acting in the name of the Kingdom of Morocco.”<sup>3</sup>. We notice that the tribunal deemed ADM as a state company despite its private character under Moroccan law. Same as *maffezini’s* decision the *Salini’s* tribunal didn’t give much weight to the classification of the entity under domestic law. The same approach was embraced by the same tribunal in *R.F.C.C. v. Morocco* which had arisen out of the same dispute<sup>4</sup>.

It’s noteworthy that the status of the entities at issue, in both *Maffezini* and *Salini*, was addressed at the jurisdiction phase apart from the question of attribution which the *maffezini’s* tribunal treated at the merits phase. As such the question of attribution hadn’t been tackled neither by *Salini* nor by *RFCC*. The latter tribunal decided that there had been no treaty violation and therefore there is no need to decide the question of attribution<sup>5</sup>. The former one was discontinued and thus didn’t reach a final award<sup>6</sup>.

Although they didn’t address directly the question of attribution and ILC’s articles thereon, these 3 decisions represent the stream that favors substance over form in international law. In other words, the line of preference of international law over internal law approach in investment arbitration disputes.

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<sup>1</sup> Ibid. para 29.

<sup>2</sup> Ibid. para 31.

<sup>3</sup> Ibid. para 35.

<sup>4</sup> Consortium R.F.C.C. v. Morocco, ICSID, Decision on Jurisdiction, 16 July 2001, paras 34-40.

<sup>5</sup> Consortium R.F.C.C. v. Morocco, ICSID, Award, 22 December 2003, para 109.

<sup>6</sup> See [Salini Costruttori S.p.A. and Italstrade S.p.A. v. Kingdom of Morocco \[II\], ICSID Case No. ARB/00/4 | italaw](#), accessed on 25/12/2020.

**Noble ventures vs Romania**

The state ownership fund (SOF-Romanian state entity which later became APAPS) had sold shares in a steel mill to an American investor. SOF committed in the share purchase agreement to undertake its "best efforts" to secure debt restructuring of the mill. The investor claimed that neither SOF nor APAPS fulfilled the said obligation which amounted to a breach, attributable to Romania, of the USA-Romania BIT.

The claimant contended that the entity at stake is an organ of the state and based his argument on the *Maffezini's* structural/functional test<sup>1</sup>. On the other hand the defendant replied, as usual, by relying on the classification of SOF, under its domestic law, as a separate legal entity whose commercial acts don't entail the responsibility of the state<sup>2</sup>.

The tribunal simply stated that SOF and APAPS, under Romanian law, aren't article 4 organs as they were separate legal entities. However, it stated that "This rule concerns attribution of acts of so-called de jure organs which have been expressly entitled to act for the State within the limits of their competence<sup>3</sup>". It's true that the term "de jure organ" is a bit confusing that makes the reader think about the fate of "de facto organ's" actions and whether they could be attributed under article 4<sup>4</sup>. Though the confusing situation, the tribunal made it plain that it relies on Romanian law to disqualify SOF and APAPS as state organs, moreover it attributed their conduct to Romania under article 5. Likewise one might think that by "de jure" the tribunal meant organs qualified as such by internal law and didn't intend to address the stance of "de facto organs" as opposed to "de jure organs".

**EDF v Romania**

This dispute concerned the attribution of alleged breaches of contractual obligations relating to the use of commercial spaces in an airport by two State-owned enterprises. The tribunal commenced by stating that "once it is established

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<sup>1</sup> Noble Ventures v. Romania (ICSID Case No. ARH/OI/11), Award, 12 October 2005, para 64.

<sup>2</sup> Ibid. paras 66-67.

<sup>3</sup> Ibid. para 69.

<sup>4</sup> Gallus, *supra* note 3, p.768.

that an entity is an organ of the State, the presumption is that all of its acts are attributable to the State unless the contrary is proven”<sup>1</sup>

Then it criticized the undecided stance of the claimant who “characterizes AIBO and TAROM as entities “acting as an agent of the Romanian state in their conduct with EDF”, a position that points to the functional test of attribution within the meaning of ILC Article 5 rather than to the structural test under ILC Article 4. However, in its Post-Hearing Brief, Claimant relies on the attribution of AIBO’s and TAROM’s conduct to Romania “under the structural and control test” (para. 55), therefore referring again also to ILC Article 4 (the structural test)”<sup>2</sup>. Based on the Romanian law, the tribunal decided that neither of the two entities is seen as a state organ as both of them possessed a legal personality distinguishing them from the state itself<sup>3</sup>.

Regarding the attribution of the conduct under article 5 the tribunal emphasized that the article refers only to the empowered governmental authority regardless the ownership, the participation of the state in the enterprise’s capital and the executive control of the state over the enterprise<sup>4</sup>. At the end the tribunal attributed the conduct to the state under article 8 concluding that only the conduct complained of was under the control of the state within the meaning of the said article<sup>5</sup>.

### *AMCO V Indonesia*

In this case the Claimants sought to attribute to Indonesia the seizure of his investment by PT Wisma, a company owned and run by Inkopad which was connected to the Indonesian army. The latter enterprise was established in order to provide social services to the Indonesian Army members. Its Articles of Association provided that it was entirely owned and controlled by the State. According to Article 19 thereof Inkopad “is under the government's guidance and supervision which is carried out by the Government Official and Army Leadership”<sup>6</sup>.

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<sup>1</sup> EDF v. Romania (ICSID Case No. Atu; /05/13), Award, 8 October 2009, para 188.

<sup>2</sup> Ibid. para 189.

<sup>3</sup> Ibid. para 190.

<sup>4</sup> Ibid. para 193.

<sup>5</sup> Ibid. para 213.

<sup>6</sup> Amco Asia Corp. and others v. Republic of Indonesia (ICSID) Case No. ARB/81 /1, Award, 20 November 1984.

Notwithstanding the close relationship between the two enterprises and the Indonesian army, this fact doesn't, in the tribunal's opinion, justify the attribution of the acts to Indonesia. By reaching this conclusion "the Tribunal accepts that PT Wisma is registered as a limited liability company and that the acts of such entities are not normally to be attributed to their shareholders"<sup>1</sup>.

### **Tulip V Turkey**

In this case the claimant argued that Turkey acting through various entities, among which EMLAK that was 39% owned by TOKI (a state organ responsible for Turkey's public housing and operating under the auspices of the Prime Ministry of Turkey)<sup>2</sup> had violated its BIT's provisions with the kingdom of Netherlands.

The claimant referred to *Maffezini* and *Salini* to argue that the fact that "TOKI owned 39% of Emlak's shares and controlled over 99.9% of the shares" gives rise to the presumption of statehood<sup>3</sup>. Nonetheless, the tribunal sided with Turkey's argument that "there is no "quasi-state" organ for the purposes of Art 4. Given that Emlak is a separate, private, entity under Turkish law, it cannot be said that Turkish municipal law treats it as a State organ"<sup>4</sup>. What is interesting is that the tribunal didn't rely only on internal law but it relied on the Turkish Supreme Court of Appeal's opinion that "Public Economic Enterprises, since they set up and operate commercial undertakings, are merchants. The fact that their capital belongs to the state and there is a particular way in which appointments are made to certain of their managerial organs does not imbue these entities with public law establishment capacity and these bodies are civil law judicial persons and the provisions of private law apply to them."<sup>5</sup> The tribunal gave a considerable role for internal law and case law in determining whether EMLAK was a state entity.

Moreover, the tribunal hold that "there is no basis under international law to conclude that ownership of a corporate entity by the State triggers the presumption of statehood. The position of the Tribunal is that, whilst state ownership may, in

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<sup>1</sup> Ibid. para 162-163.

<sup>2</sup> Tulip Real Estate Investment and Development Netherlands B.V. v. Republic of Turkey (ICSID Case No. ARB/11/28), Award, 10 March 2014, paras 60-63.

<sup>3</sup> Ibid. para 253.

<sup>4</sup> Ibid. para 288.

<sup>5</sup> Ibid.

certain circumstances, be a factor relevant to the question of attribution, it does not convert a separate corporate entity into an ‘organ’ of the State”. The tribunal agreed with *EDF v Romania* tribunal on the relevancy of the distinct legal personality that preclude the enterprise from being a state organ<sup>1</sup>.

Finally the tribunal concluded that, under article 8, EMLAK acted as a private party on the basis of commercial considerations and that the contested acts were not attributed to Turkey<sup>2</sup>.

Thus we notice here the difference between the two lines of reasoning; the *Maffezini*’s approach which relies on the structural/functional tests and overlook state law. This is plainly stated in *Maffezini* “A domestic determination, be it legal, judicial or administrative, as to the juridical structure of an entity undertaking functions which may be classified as governmental... is not necessarily binding on an international arbitral tribunal. Whether an entity is to be regarded as an organ of the State and whether this might ultimately engage its responsibility, is a question of fact and law to be determined under the applicable principles of international law”<sup>3</sup>.

Clearly the rival approach is that of internal law, its disciples strictly follow article 4 regardless of the real stakeholder and shareholder availing from the corporations’ activities. In order to avoid the clash between the impunity of the state and the surpassing of its internal law a compromise has to be found. In this vein, some BITs provide a *lex specialis* approach on the status of state enterprises. The latter approach will help the tribunals to decide the question based upon the parties’ intention.

### **III. State enterprises in some Multilateral trade agreements:**

Given the plethora of bilateral investment agreements around the world<sup>4</sup>, we opted to tackle the question through the lens of multilateral and recent agreements. Primarily it has to be recalled that the issue concerns only commercial activities of the state enterprise, as anyway the governmental activities of any entity, organ or enterprise, are usually attributed to the state as noted above in the introduction.

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<sup>1</sup> Ibid. para 382.

<sup>2</sup> Ibid. para 313.

<sup>3</sup> Maffezini, *supra* note 15.

<sup>4</sup> See <https://investmentpolicy.unctad.org/international-investment-agreements>. Accessed on 28/12/2020.

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The Energy charter treaty (ECT)

The ECT didn't set out a definition for state enterprises, it merely states in article 22 (5) that "*For the purposes of this article "entity" includes any enterprise, agency or other organization or individual*"<sup>1</sup>.

The first paragraph of article 22 provides that "*Each Contracting Party shall ensure that any state enterprise which it maintains or establishes shall conduct its activities in relation to the sale or provision of goods and services in its Area in a manner consistent with the Contracting Party's obligations under Part III of this Treaty*"<sup>2</sup>.

This means that the state would be responsible if one of its enterprises, in an energy transaction, acted inconsistently with the state obligations under part III of the treaty<sup>3</sup>. It's quite clear that the treaty attributed the violation of commercial obligations to the state. By the same token the "regulatory, administrative or other governmental authority" are also attributed to the state under paragraph (4) of the same article. Thus the generality of the text allows us to deduce that under the ECT a state enterprise is a state organ, particularly that there is no clear definition of what is meant by a state enterprise.

This stance is far from being a compromise on the status of state enterprises, it's rather a clear willingness of the state parties to treat them as state organs. This could be justified by the peculiarity of the energy sector investment that is oscillating throughout the world between private sector and public one. It also takes into account the influence of a state enterprise and ensured that it's not greater than its private counterparts<sup>4</sup>. In accordance with article 55 of the ILC's articles, this

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<sup>1</sup> The energy charter treaty.  
[https://www.europarl.europa.eu/meetdocs/2014\\_2019/documents/itre/dv/energy\\_charter/\\_energy\\_charter\\_en.pdf](https://www.europarl.europa.eu/meetdocs/2014_2019/documents/itre/dv/energy_charter/_energy_charter_en.pdf)

<sup>2</sup> Ibid.

<sup>3</sup> Part III obligations are: Non expropriation-compensation for losses-non-discriminatory treatment.

<sup>4</sup> RAFAEL LEAL-ARCAS, "COMMENTARY ON THE ENERGY CHARTER TREATY," December 28 2018, Edward Elgar publishing, p.312.

solution to the attribution question neutralized the ILC's articles in this regard and represents a relief to ECT tribunals<sup>1</sup>.

In *Nykomb Synergetics v Latvia*, the Swedish company concluded a transaction with a joint stock company called Latvenergo in which the republic of Latvia holds 100 per cent of the shares. The Latvian energy law defined Latvenergo as a national economy object of the state that shall not be privatized. According to the agreement Nykomb had to build a cogeneration plant in order to produce electric power to be purchased by Latvenergo and distributed over the national grid. After the plant was built, a dispute arose over the purchase price to be paid by Latvenergo. Many amicable settlement attempts didn't reach a viable solution, afterwards Nykomb filed an arbitration request on December 2001 before the Stockholm Chamber of Commerce (SCC) pursuant to article 26.4.c of the ECT<sup>2</sup>.

The tribunal noted that the company is totally owned by the state and found also that “*the enterprise had no commercial freedom with respect to the matters at issue but was bound to follow legislation and the regulatory bodies*” determination of the price to be paid for power generated by plants. “*Latvenergo could not be considered to be an independent commercial enterprise, but clearly a constituent part of the republic's organization of the electricity market and a vehicle to implement the republic's decisions*”. Therefore the tribunal decided that “*the Republic must be found responsible for Latvenergo's failure to pay the double tariff*” and added that “*for this finding it is not necessary to rely on the supplemental rule in Article 22 (1) of the Treaty contended by the Claimant*”.<sup>3</sup>

The tribunal relied on both the structural (state ownership) as well as functional (absence of commercial freedom) to conclude that Latvia is responsible for Latvenergo acts. An analysis akin to that of *Maffezini*. It's not clear why did the

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<sup>1</sup> These articles do not apply where and to the extent that the conditions for the existence of an internationally wrongful act or the content or implementation of the international responsibility of a State are governed by special rules of international law.

<sup>2</sup> Rafael, *supra* note, p.308.

<sup>3</sup> *Nykomb Synergetics Technology Holding AB v The Republic of Latvia*, SCC, Award, 16 December 2003, para 4(2).

tribunal avert the reliance on article 22 directly, although the latter makes the states directly liable for the actions of its enterprises<sup>1</sup>.

On the other hand, in *Petrobart v the Kyrgyz republic*, the Kyrgyz state gas company (KGM) failed to pay the price of some gas deliveries to Petrobart, a company based at Gibraltar. The latter filed a claim before the SCC claiming the breach of state obligations under part III of the ECT.

In this case the tribunal was clearer and got directly to the point by citing article 22 and stating that it “*placed certain obligations on the Republic in regard to KGM’s conduct of its business activities*”. In other words, KGM’s conducts are attributed to the state. Then on the non-payments the tribunal decided that article 22 mustn’t be seen as an “*effective sovereign guarantee by the Kyrgyz Republic of KGM’s debt*”<sup>2</sup> and that it didn’t fail to ensure “*that KGM conducted its business in a manner consistent with Part III of the Treaty.*”<sup>3</sup> Nevertheless, it held Kyrgyz republic liable for transferring KGM’s property to other entities and for the interference of the Vice Prime Minister with the court proceedings aiming to the stay of execution of a judgment in favor of Petrobart<sup>4</sup>.

### **The North America free trade agreement (NAFTA) and United states-Mexico-Canada agreement (USMCA)**

A state enterprises is defined by NAFTA, unlike the ECT, as “an enterprise that is owned, or controlled through ownership interests, by a Party”<sup>5</sup>.

This definition becomes more detailed in USMCA, the amended version of NAFTA released on the 30<sup>th</sup> of November 2018. According to article 22.1 thereof:

“*A state-owned enterprise means an enterprise that is principally engaged in commercial activities, and in which a Party:*

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<sup>1</sup> Thomas Waelde and Patricia Wouters, “State Responsibility and The Energy Charter Treaty: The Rules Regarding State Enterprises, Entities, and Subnational Authorities,” *Hofstra Law & Policy Symposium* 2, no. 1 (January 1, 1997), p.128.

<sup>2</sup> *Petrobart Limited v. The Kyrgyz Republic*, SCC, Award, 29 March 2005, p 54.

<sup>3</sup> *Ibid.* p.77.

<sup>4</sup> *Ibid.*

<sup>5</sup> North American free trade agreement, p.5. <https://www.trade.gov/north-american-free-trade-agreement-nafta>. Accessed on 31/12/2020.

(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.*

(d) *Holds the power to appoint a majority of members of the board of directors or any other equivalent management body.*

Beside the very well detailed definition of a state enterprise, the other positive point is that the commercial activity of the enterprise is emphasized by the article. This will cut the road off to any pleading from the state that the enterprise is a private commercial entity, and thus is not part of the state as contended by the Spanish government in *Maffezini*<sup>1</sup>. This kind of detailed definitions illuminates the parties' intention and restrain the arbitrators' discretionary power.

Moreover, article 1503 (3) of NAFTA states that “*Each Party shall ensure that any state enterprise that it maintains or establishes accords non-discriminatory treatment in the sale of its goods or services to investments in the Party's territory of investors of another Party.*” Same as in the ECT, this article resolve the attribution question. However, the material scope of this article is limited to the non-discriminatory treatment of the state enterprise in its commercial transactions. A similar, but more detailed, article is provided in USMCA<sup>2</sup>.

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<sup>1</sup> Maffezini, supra note, para 73.

<sup>2</sup> Article 22(4): Each Party shall ensure that each of its state-owned enterprises, when engaging in commercial activities: (a) acts in accordance with commercial considerations in its purchase or sale of a good or service, except to fulfil the terms of its public service mandate that are not inconsistent with subparagraphs (b) or (c)(ii); (b) in its purchase of a good or service: (i) accords to a good or service supplied by an enterprise of another Party treatment no less favorable than it accords to a like good or a like service supplied by enterprises of the Party, of any other Party or of a non-Party, and (ii) accords to a good or service supplied by an enterprise that is a covered investment in the Party's territory treatment no less favorable than it accords to a like good or a like service supplied by enterprises in the relevant market in the Party's territory that are investments of investors of the Party, of another Party or of a non-Party; and (c) in its sale of a good or service: (i) accords to an enterprise of another Party treatment no less favorable than it accords to enterprises of the Party, of any other Party or of a non-Party, and (ii) accords to an

Given the newness of USMCA there hasn't been yet any arbitral decision tackling this *lex specialis* on state enterprise<sup>1</sup>. So we will proceed with the United Parcel of America v Canada which concern allegations of unfair competition from Canada Post (state owned company) and the failure of Canada to regulate claimant argued that "Whether Canada Post's conduct falls under article 4 or under article 5 there is clear and undeniable state responsibility attributable to Canada"<sup>2</sup>.

But the tribunal referred to article 1503 of NAFTA and stated that "*Several features of these provisions read as a whole lead the Tribunal to the conclusion that the general residual law reflected in article 4 of the ILC text does not apply in the current circumstances. The special rules of law stated in chapters 11 and 15, in terms of the principle reflected in article 55 of the ILC text, "govern" the situation and preclude the application of that law*"<sup>3</sup>. Then the tribunal concluded that the acts of Canada post are not attributed to Canada<sup>4</sup>. We mentioned above the hesitation of another NAFTA tribunal, Waste management vs Mexico which didn't rely on the *lex specialis* provided in the treaty but instead relied on a mixture of ILC's articles.

There are also some recent trade agreements but we cannot find arbitral decisions related to them concerning state enterprises. Nevertheless those agreements represent a considerable authority in international law as their member states constitute a large portion of the global economy. This fact, alongside with the newness of these agreements, will shed much light on the approach states intend to embrace regarding their enterprises in international investment law.

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enterprise that is a covered investment in the Party's territory treatment no less favorable than it accords to enterprises in the relevant market in the Party's territory that are investments of investors of the Party, of another Party or of a non-Party.

<sup>1</sup> However, there is a consultation request presented by the USA officials to Canada regarding Tariffs rate quotas on dairy products. See <https://www.macaubusiness.com/us-files-usmca-complaint-against-canada-over-dairy-exports/>. Accessed on 28 December 2020.

<sup>2</sup> UNITED PARCEL SERVICE OF AMERICA V. GOVERNMENT OF CANADA, ICSID, Award, May 24 2007, para 49.

<sup>3</sup> Ibid. para 59.

<sup>4</sup> Ibid. para 62.

In the Comprehensive and progressive transpacific partnership (CPTPP)<sup>1</sup>, state enterprises' provisions are akin to those of USMCA. Their acts are attributed to the state, the commercial character of its activities is emphasized and the definition is roughly detailed in the same way<sup>2</sup>.

In the comprehensive economic and trade agreement (CETA)<sup>3</sup>, a state enterprise “means an enterprise that is owned or controlled by a Party”<sup>4</sup>. Unlike the detailing approach followed by USMCA and CPTPP, this agreement follows a broad approach that unleash the adjudicators' discretionary power regarding the threshold of ownership and the nature of control. As for attribution CETA attributes to member states the actions of state enterprises<sup>5</sup>.

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<sup>1</sup> Signed by trade ministers on 8 March 2018. Form a trading bloc representing 500 million consumers and 13.5% of global GDP. And includes in its membership 11 country: Canada, Australia, Japan, Mexico, New Zealand, Singapore, Vietnam, Brunei, Chile, Malaysia and Peru. See [https://www.international.gc.ca/trade-commerce/trade-agreements-accords-commerciaux/agr-acc/cptpp-ptpgp/cptpp\\_explained-ptpgp\\_apercu.aspx?lang=eng](https://www.international.gc.ca/trade-commerce/trade-agreements-accords-commerciaux/agr-acc/cptpp-ptpgp/cptpp_explained-ptpgp_apercu.aspx?lang=eng). Accessed on 31/12/2020.

<sup>2</sup> Article 17.1: state-owned enterprise means an enterprise that is principally engaged in commercial activities in which a Party.

(a) directly owns more than 50 per cent of the share capital;

(b) controls, through ownership interests, the exercise of more than 50 per cent of the voting rights;

(c) holds the power to appoint a majority of members of the board of directors or any other equivalent management body

Article 17.4: Each Party shall ensure that each of its state-owned enterprises, when engaging in commercial activities: (a) acts in accordance with commercial considerations in its purchase or sale of a good or service, except to fulfil any terms of its public service mandate that are not inconsistent with subparagraph (c)(ii)...

<sup>3</sup> Concluded between the European Union and Canada on the 30<sup>th</sup> of October 2016. <http://urbis.europarl.europa.eu/urbis/document/ceta-eu-canada-free-trade-agreement>

<sup>4</sup>Article 1.1 of The Comprehensive Economic and Trade Agreement. See [https://ec.europa.eu/trade/policy/in-focus/ceta/ceta-chapter-by-chapter/index\\_fr.htm](https://ec.europa.eu/trade/policy/in-focus/ceta/ceta-chapter-by-chapter/index_fr.htm). Accessed on 31/12/2020.

<sup>5</sup> Article 18.4: Each Party shall ensure that in its territory a covered entity accords non-discriminatory treatment to a covered investment, to a good of the other Party, or to a service supplier of the other Party in the purchase or sale of a good or service.

The most recent agreement is the regional comprehensive economic partnership (RCEP)<sup>1</sup>. This agreement is a swing back as it totally avoided state enterprises. Only one provision might be relevant, Article 1.2(n) “*juridical person means any entity constituted or organized under applicable law, whether or not for profit, and whether privately-owned or governmentally-owned, including any corporation, trust, partnership, joint venture, sole proprietorship, association, or similar organization*”. This article equates private entities to public ones under the umbrella of “juridical person”. Such approach entails that any potential RCEP tribunal will have no choice but to recourse to ILC’s articles in case of a dispute involving a state enterprise.

### **Conclusion:**

One cannot deny that state enterprises are often closely linked to the state so that they could be, sometimes, seen as state organs. A state remains a state<sup>2</sup> and contracting with it has always its peculiarities. However, its capacity to create entities mustn’t be a mean to avoid liability simply by arguing that the entity isn’t a state orange under internal law<sup>3</sup>. On the other hand, the will to equate states with private parties<sup>4</sup> mustn’t go too far to ignore systemically the legal personality that has been accorded by the state to an enterprise for a specific purpose, so how can we strike a balance?

Although article 4 relies on internal law as mentioned above, the commentary thereon provides that “*On the other hand, it is not sufficient to refer to internal law for the status of State organs. In some systems the status and functions of various*

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<sup>1</sup> Signed on 15 November 2020. Its members are: China, Japan, South Korea, Australia, New Zealand and the 10 members of the Association of South East Asian Nations (ASEAN): Brunei, Vietnam, Laos, Cambodia, Thailand, Myanmar, Malaysia, Singapore, Indonesia and the Philippines. It covers nearly a third of the global population and about 30% of its global gross domestic product. See <https://financialpost.com/pmnbusiness-pmn/what-happens-now-the-rcep-trade-deal-has-been-signed>

<sup>2</sup> Carlo de Stefano, *Attribution in International Law and Arbitration*, Oxford University Press, 2020, p.1.

<sup>3</sup> Responsibility draft, *Supra* note 8, p.42.

<sup>4</sup> Charles Leben, “La Théorie Du Contrat d’État et l’évolution Du Droit International Des Investissements” *Collected Courses of the Hague Academy of International Law* (Volume 302), February 2, 2003, p.258.

*entities are determined not only by law but also by practice, and reference exclusively to internal law would be misleading*” This means, according to some<sup>1</sup>, that state organs “include”, but not limited to, those designated by internal law. We see that embracing simultaneously two distinct approaches is not an answer.

The primary reference for an investment tribunal is the treaty from where it derives its jurisdiction. Nonetheless, Most of the tackled award didn’t find, in the related BIT, provisions regulating the standing of state enterprises<sup>2</sup>. Until states agree, through their investment and trade agreement, on the standing of state enterprises, the question will remain somehow dependent on the ILC’s articles and arbitrators’ discretionary power and ideological background. Whether he’s a proponent of the untouchable state sovereignty, including its national law, or is a believer in the force of private firms as a development wheel of the whole society.

The impeccable balance is the *lex specialis* created by the abovementioned agreements<sup>3</sup> that is in our opinion a sort of compromise taking into account the sovereignty of the state to create commercial enterprises that are not organs of the state. And the interests of foreign investors by attributing to the state the potential violation, by its enterprises, of the BIT obligations.

The novelty and the wide scale population covered by these agreements could pave the way toward a uniform approach in respect of state enterprises, unless other agreements take different approaches<sup>4</sup>.

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<sup>2</sup> Noble, *supra* note 38, para.69. Maffezini, *supra* note 15, para 74.

<sup>3</sup> Notably USMCA.

<sup>4</sup> Like RCEP.

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