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State-Owned Enterprises in Investor-State Dispute Settlement

Las Empresas Estatales en la Solución de Diferencias entre Inversionistas y Estados

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Abstract

This essay examines whether state-owned enterprises (SOEs) qualify as investors under the Investor-State Dispute Settlement (ISDS) provisions of the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) and the United States-Mexico-Canada Agreement (USMCA).

Keywords: United States-Mexico-Canada Agreement (USMCA), Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), Investor-State Dispute Settlement (ISDS), State-Owned Enterprises (SOEs)

Resumen

Este ensayo examina si las empresas estatales se pueden calificar como inversionistas en virtud de las disposiciones sobre solución de controversias entre inversionistas y Estados (ISDS, por su sigla en inglés) del Acuerdo Integral y Progresista de Asociación Transpacífico (CPTPP) y el Tratado entre México, Estados Unidos y Canadá (T-MEC).

Palabras clave: Tratado entre México, Estados Unidos y Canadá (T-MEC), Acuerdo Integral y Progresista de Asociación Transpacífico (CPTPP), Solución de Controversias entre Inversionistas y Estados (ISDS), Empresas estatales

1. Introduction

Over the past few years, the field of international investment law has been notably reshaped by the growing involvement of state-owned enterprises (SOEs) in foreign investments (Blyschak, 2016, p. 5). This trend has prompted significant regulatory actions from major host states. One critical issue arising from this development is the question of whether SOEs are entitled to the same international investment protections as private entities, including access to the investor-State dispute settlement (ISDS) mechanism (Nalbandian, 2021, p. 7).

The main question is whether SOEs can be classified as "investors" – and their assets as "investments" – under international investment treaties (IIAs) (Feldman, 2016, pp. 26-27). Many earlier-generation IIAs do not clearly define whether SOEs fall into the category of investors (Nalbandian, 2021, p. 14). In contrast, modern IIAs, such as the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP)[1] and the United States-Mexico-Canada Agreement (USMCA)[2], directly address this matter (McLaughlin, 2019, p. 16). However, these treaties take distinctly different approaches, which affect the eligibility of SOEs for ISDS.

This essay aims to explore possible perspectives on the inclusion of foreign SOEs in the ISDS framework. To achieve this, section 2 examines different views on the eligibility of SOEs under first-generation IIAs. Section 3 highlights the broader regulatory scope provided to States by newer IIAs and analyses the pertinent rules concerning the standing of SOEs, under both the CPTPP and the USMCA. Section 4 offers a brief conclusion summarizing the findings.

[1]Comprehensive and Progressive Agreement for Trans-Pacific Partnership (2018). 3337 UNTS.

[2]United States-Mexico-Canada Agreement (USMCA) (2018). Not available at UNTS.

2. The Standing of State-Owned Enterprises under First-Generation IIAs

The issue of whether SOEs qualify as investors is related but distinct from whether they have standing in investor-State arbitration (Feldman, 2016, p. 27). This relationship arises because treaty provisions concerning investor-State arbitration often refer to the definition of "investor" to determine which investors can bring claims against the host State (Mohtashami, Reza; El-Hosseny, Farouk, 2016, pp. 380-384). Therefore, SOEs can only benefit from treaty protection if they are recognized as covered investors. When treaties explicitly include SOEs in their definitions of investors, these entities have the standing to enforce their treaty rights through investor-State arbitration (Feldman, 2016, p. 26). Conversely, if the treaty does not explicitly address this issue, SOEs may still have standing if the tribunal determines that the definition of investor encompasses state-owned entities and contracting parties (Nalbandian, 2021, p. 14).

Approximately 81 %-84 % of IIAs do not specify whether SOEs are eligible for substantive treaty protections. This is because they do not explicitly distinguish based on the ownership of a legal person (McLaughlin, 2019, pp. 15-16). This ambiguity creates significant uncertainty, as arbitral tribunals have considerable discretion in determining whether SOE investments fall under the protections of these treaties (Nalbandian, 2021, pp. 16-22). In particular, tribunals may adopt different interpretative approaches regarding the fact that SOEs are not explicitly excluded from the definition of "investor."

However, being a qualified investor under an IIA does not automatically guarantee access to international investment arbitration. The investor must also meet the requirements of the applicable arbitration rules (Cortesi, 2017, pp. 110-115). According to Article 25 of the Convention on the Settlement of Investment Disputes between States and Nationals of

other States (ICSID Convention)[3], only investments made by nationals of member States are typically within the jurisdiction of International Centre for Settlement of Investment Disputes (ICSID). This raises the question of whether SOEs, which could be considered extensions of their home States, can be considered "nationals" in this context (Blyschak, 2016, p. 6).

The principle that SOEs lack standing in ISDS when acting in a governmental capacity has been recognized since ISDS's inception (Schreuer, 2009, p. 161). In a lecture delivered at The Hague Academy of International Law in 1972, Aron Broches, one of the principal drafters of the ICSID Convention, argued that SOEs should generally be allowed to bring claims against States under the Convention. However, he outlined two exceptions: when an SOE is "acting as an agent of the government" or "performing an essentially governmental function." This framework is commonly referred to as the "Broches test" (Mohtashami, Reza; El-Hosseny, Farouk, 2016, p. 372).

Despite increasing attention to the role of SOEs in international arbitration, the issue of their standing remains unresolved. While some SOEs have initiated claims against host States pursuant to ICSID arbitration, few tribunals have thoroughly examined whether these SOEs qualify as "investors" under the relevant treaties or whether they meet the ICSID Convention's test of being "nationals" of a contracting State (Mohtashami, Reza; El-Hosseny, Farouk, 2016, pp. 384-387). In these cases, the Broches test has not always been applied, and when it has been used, tribunals have generally concluded that the SOEs were performing commercial rather than governmental functions (Schreuer, 2009, p. 162). Meanwhile, the academic literature has suggested alternative approaches to address this issue.

The Preamble of the ICSID Convention excludes States from being considered investors (Schreuer, 2009, p. 161). The Preamble refers to "the role of private international investment", implying that only private individuals or corporations, and not States, can be considered investors. In addition, the Report of the Executive Directors, which is a foundational document that provides essential context and guidance for interpreting and applying the ICSID Convention, frequently mentions "private international capital" and "private international investment" (International Bank for Reconstruction and Development, 1965). Such interpretations, however, are not entirely persuasive (Schreuer, 2009, p. 161). According to Article 31 of the Vienna Convention on the Law of Treaties, a treaty is usually and primarily be interpreted based on its ordinary meaning (Nalbandian, 2021, p. 13). The ICSID Convention's Preamble does not expressly exclude public investors, despite emphasis the necessity of for international economic cooperation and the role of private investment. This is also supported by the Comment to the Preliminary Draft, which allows a company that is "wholly or partially government-owned company to be a party to proceedings brought by or against a foreign State" (Schreuer, 2009, p. 161).

When a SOE invests abroad and potentially engages in governmental functions, it is crucial for the tribunal to assess whether this capacity "prevents a claimant from qualifying as an investor" (Feldman, 2016, p. 35). However, Feldman seems to favor the standing of SOEs in ISDS by suggesting that the absence of an explicit exclusion of SOEs in most definitions of "investor" should be interpreted as an implicit inclusion (2016, pp. 26-27).

The position of SOEs in ISDS may be based on a different rationale. The competence of arbitrators to resolve investor-State disputes involving SOEs is rooted in the principle of party autonomy, which underpins investment arbitration by design. Furthermore, since many arbitrators have experience in international commercial arbitration, they are generally "more proactive in the use of their powers" (Cortesi, 2017, p. 137).

[3]Convention on the settlement of investment disputes between States and nationals of other States (1965). 575 UNTS 159.

SOEs investing abroad may pursue objectives beyond commercial interests, such as geopolitical purposes or public service obligations, which could suggest that they act as State agents rather than private investors (Nalbandian, 2021, p. 6). In such scenarios, if SOEs are deemed eligible for investor-State arbitration, this could "contribute to the undermining of [ISDS's] institutional legitimacy in the eye of policymakers and civil society" (Nalbandian, 2021, p. 29).

In any case, it is unlikely that an ICSID tribunal would reject jurisdiction over claims brought by SOEs based on the Broches test, given current foreign investment practices: "(i) (...) the Broches test has been infrequently invoked in arbitrations involving SOEs, and (ii) (...) tribunals have never upheld its application" (Mohtashami, Reza; El-Hosseny, Farouk, 2016, p. 387). These authors emphasize that, in order to properly evaluate the admissibility of SOEs as claimants in ISDS, new parameters must be considered. Traditional criteria, such as the Broches test, may no longer be sufficient to address the complexities of modern investments and the evolving roles of SOEs.

Finally, there is a distinction between the "substantial" and "formalist" approaches to determining the jurisdiction of investment tribunals over cases involving SOEs. While Zhang does not take a firm position on whether SOEs should have standing in ISDS, his analysis of international investment case law concerning Chinese SOEs offers a useful framework for exploring this issue (Zhang, 2018).

Thus, the disordered and unsystematic nature of the definition of "investor" and the variability in the language of first-generation IIAs naturally lead to diverse interpretations and divergences among scholars.

3. The Standing of State-Owned Enterprises under the CPTPP and the UMSCA

In contrast, many newly concluded agreements tend to expressly include state enterprises and even States as qualified investors (McLaughlin, 2019, p. 21).

In analyzing the objectives of new-generation IIAs, both developed and developing countries share an interest in reducing the protections afforded to foreign investors, thus providing greater regulatory scope for States (Tijmes, 2023, pp. 454-455). During the negotiation of the USMCA, US President Trump aimed to modify the existing ISDS mechanism to "shift some power away from the international level, toward the national" (Lester & Manak, 2018, p. 167). Similarly, the CPTPP introduces a number of innovations that limit the application of ISDS, such as the distinction between "investor of a Party" and "investor of a non-Party", the notion of covered investment and more specific definitions of the content and scope of treaty standards (Toro-Fernández & Tijmes-Ihl, 2021, pp. 151-152, 158).

The concern for protecting States' regulatory space is also reflected in the detailed regulation of SOEs. Both the CPTPP and the USMCA include a comprehensive chapter that establishes a regulatory framework for SOEs "designed mainly by the US to constraint [sic] certain Asian economies engaged in state capitalism" (Iglesias Mujica, 2021, p. 312). Additionally, unlike the first-generation IIAs, and in contrast to the analysis made by the authors discussed in the previous section, the CPTPP and the USMCA directly address which and how SOEs qualify as investors.

In this context, the CPTPP provides that "investor of a Party" means "a Party, or a national or an enterprise of a Party, that attempts to make, is making, or has made an investment in the territory of another Party" (Article 9.1 CPTPP); and "enterprise" means

> any entity constituted or organised under applicable

> law, whether or not for profit, and whether privately or governmentally owned or controlled, including any corporation, trust, partnership, sole proprietorship, joint venture, association or similar organisation" (Article 1.3 CPTPP).[4]

Therefore, according to the CPTPP's definitions, I note that it is generally possible to assert that SOEs have standing to initiate an ISDS claim, notwithstanding the various limitations on the ISDS system, including those outlined *supra*.

The USMCA presents a different scenario. Although the definitions of "investor" (Article 14.1 USMCA)[5] and "enterprise" (Article 1.5 USMCA)[6] are nearly identical to those in the CPTPP, certain SOEs do not have standing due to the exclusion outlined in the definition of "claimant" (Article 14.D.1 USMCA). That provision defines claimant as

> an investor of an Annex Party that is a party to a qualifying investment dispute, excluding an investor that is owned or controlled by a person of a non-Annex Party that, on the date of signature of this Agreement, the other Annex Party has determined to be a non-market economy for purposes of its trade remedy laws and with which no Party has a free trade agreement.[7]

The exclusion of entities potentially influenced by non-market principles is likely intended to prevent investors whose conduct may be affected by government influence from benefiting from ISDS (Nalbandian, 2021, pp. 23-24). Consequently, the USMCA aims to ensure that ISDS is accessible mainly to private investors rather than SOEs, which might have distinct strategic and political motivations.

Indeed, this provision prompted China to invoke Annex 14-D USMCA at the World Trade Organization Committee, seeking clarification on its implications (World Trade Organization Committee on Regional Trade Agreements, 2021). Both Mexico and the United States lack a formal free trade agreement with China, as the U.S.–China Phase One trade deal does not fulfill the requisite criteria. Consequently, under Annex 14-D USMCA, an ISDS claim may be excluded if a US company investing in Mexico or a Mexican company investing in the United States is "owned or controlled by a person" from China.

4. Conclusion

The qualification of SOEs as investors is closely tied to their ability to access investor-state arbitration. Whether SOEs can initiate claims depends on the treaty provisions that define which investors are covered. If treaties explicitly include SOEs, they can pursue arbitration. Otherwise, SOEs might still have standing if tribunals interpret the investor definition to include state-owned entities. Some scholars support SOE standing, while others are cautious about endorsing SOE claims, particularly when SOEs act in a governmental capacity.

New-generation investment agreements, such as the CPTPP and the USMCA, explicitly include SOEs as qualified investors. The CPTPP introduces specific limitations on ISDS, including distinctions between different types of investors and more precise definitions of treaty standards. Similarly, the USMCA imposes exclusions on certain SOEs from accessing ISDS based on their association with non-market economies, aiming to prevent potential government influence. Despite these developments, the

[4] Emphasis added.

[5] In the case of the USMCA and unlike the CPTPP, the definition of "investor" includes additional requirements related to the nationality and residency of a natural person.

[6] The sole distinction is that the CPTPP uses the phrase "any entity" and "any… similar organization," while the USMCA uses "an entity" and "a… similar organization."

[7] Emphasis added.

issue of SOE standing in investor-state arbitration remains complex and underexplored, with ongoing scholarly debates and the need for further analysis in this area.

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