

Effects of Settlement between a Local Company and a Host State in a Bilateral Investment Treaty Claim of Foreign Shareholders Arising From the Same Conduct

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Abstract

This work analyzes the different approaches adopted by ICSID tribunals regarding the effects that a settlement between a local company and the host State has on the bilateral investment treaty claim of foreign shareholders arising from the same conduct. It proposes a solution based on a distinction of the remedy pursued and the admissibility of the claim, finding support in the separation between treaty and contractual claims and in the civil law doctrine of unjust enrichment.

Key words: settlement, effects, local company, host State, foreign shareholders, treaty and contractual claims, unjust enrichment.

I. THE PROBLEM

Foreign investments can be subject at the same time to the obligations set forth in a bilateral investment treaty and in the specific contract of a particular enterprise, usually subject to the laws from the host State.¹ Thus, if the same conduct involves a breach of the treaty and the contract, two possible dispute resolution procedures can be initiated.

One of the possibilities to terminate a dispute of that kind is with a settlement between the local company and the host State. However, in some situations

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¹ Yuval Shany, *Notes and Comments: Contract Claims vs. Treaty Claims: Mapping Conflicts Between ICSID Decisions On Multisourced Investment Claims*, 99 AM. J. INT. LAW 837 (2005), available at <http://poseidon01.ssrn.com/delivery.php?ID=227111111064073015002117107064071086097034061055016020027103092099121005094010064096030000020103007009008113077021083065017055015011078049111087064126119073031052033004008003023080069000010071082065002121093088001069100008089014015004083103005&EXT=pdf>.

foreign shareholders may consider that the optimal way of preserving their rights is not through the commented settlement, but with the presentation of a claim under a bilateral investment treaty.

This work analyzes the effects that a settlement between a local company and the host State has on the bilateral investment treaty claim of foreign shareholders arising from the same conduct.

II. DIFFERENT APPROACHES TO THE PROBLEM

Investment treaty arbitration case law presents two different views regarding the effects that a settlement between a local company and the host State has on the bilateral investment treaty claim of foreign shareholders arising from the same conduct.² One states that the settlement does not prevent foreign shareholders to exercise a bilateral investment treaty claim,³ while the other affirms that a previous agreement regarding the conduct that originated the claim “. . . preclude the investor from proceeding with an international action against the State.”⁴

Both positions have their own advantages. The first approach correctly distinguishes between the personality of the foreign shareholders and the local incorporated company, recognizing that they could have different interests.⁵ In addition, it differentiates the rights that investors have under a bilateral investment treaty from those that the company has in the local jurisdiction where it operates.⁶ Furthermore, it safeguards the chance of foreign shareholders to defend themselves through a bilateral investment treaty claim in cases where the settlement was adopted in an improper way.⁷

² Daniela Paez-Salgado, *Effects of Settlements in Investor-State Arbitration*, KLUWER ARBITRATION BLOG (Feb. 24, 2015), <http://kluwerarbitrationblog.com/blog/2015/02/24/what-are-the-effects-of-a-settlement-agreement-between-the-locally-incorporated-company-and-the-host-state-on-the-foreign-shareholders-pending-bit-claim/>.

³ *Id.*

⁴ *Id.*

⁵ *Id.* (“[O]n a real case, the board of directors of El Triunfo Company in El Salvador fraudulently ratified a petition for bankruptcy before the local courts so that the company could enter into winding up proceedings to intentionally dismantle the investment of its shareholders”).

⁶ *Id.*

⁷ *Id.*

On the other hand, the second approach that precludes an investor's bilateral investment treaty claim after a settlement is reached might help avoid contradictory decisions between different tribunals, and it may also reduce the risk of double recovery that can occur with the exercise of two different judicial actions stemming from the same facts.⁸

Any potential solution to the commented problem must consider these conflicting interests.

III. ICSID CASE LAW

Three ICSID cases illustrate the positions adopted under investment arbitration case law regarding the effect a settlement between a local company and the host State has on the bilateral investment treaty claim of foreign shareholders arising from the same conduct.⁹ In the following lines a brief analysis of each one of them is conducted.

A. **Sempra Energy International v. Argentine Republic**

Sempra Energy International was a U.S. company that invested in two Argentinean firms: Sodigas Pampeana S.A. and Sodigas Sur S.A. In turn, these companies were the principal owners of two Argentinean gas distribution firms: Camuzzi Gas Pampeana and Camuzzi Gas del Sur.¹⁰

In 2002, after changes were made to the regulatory framework applicable to their investment, Sempra presented a request for arbitration to the ICSID, invoking the provisions contained in the 1991 bilateral investment treaty between Argentina and United States.¹¹ The tribunal found that the regulatory measures adopted by the respondent breached both the fair and equitable treatment standard and the umbrella clause established in the treaty, and thus awarded damages to the claimant based on the loss of fair market value of its equity.¹²

In what concerns this work, during the course of the allegations the Argentinian Republic asserted that Sempra Energy International had no right to present a claim because Camuzzi Gas Pampeana and Camuzzi Gas del Sur had

⁸ *Sempra Energy International v. Argentine Republic*, ICSID Case No. ARB/02/16, Original Proceeding, Award (Sep. 28, 2007), paragraph 228.

⁹ Paez-Salgado, *supra* note 2.

¹⁰ *Sempra Energy International v. Argentine Republic*, ICSID Case No. ARB/02/16, Original Proceeding, Award (Sep. 28, 2007).

¹¹ *Id.* at paragraph 5.

¹² *Id.* at paragraph 440 and number 1 of the decision of the Tribunal.

negotiated a new tariff regime with the Argentinean government.¹³ In other words, there was already an agreement between the local companies and the host State settling the controversy. On its side, the US firm alleged that it had not participated in the said agreement, and therefore, it was not obliged by it.¹⁴

The tribunal declared the admissibility of the claimant's allegations, deciding that Sempra Energy International was still an investor whose interests were protected by the bilateral investment treaty between Argentina and United States, stating in paragraph 227 of the award the following:

“[T]he Claimant is still an investor whose interests are protected by the Treaty, it cannot be bound by an agreement between different entities to the extent that those interests have not been adequately satisfied. The agreements are to this effect *res inter alios acta*.”¹⁵

As it can be observed, the tribunal held that a settlement between a local company and the host State could not affect a party that: (1) was not part of the agreement; and (2) whose interests have not been adequately protected. Along this line, it is also possible to argue that a third party could be bound by a settlement if their interests have been “adequately satisfied.”

Regarding the potential beneficial outcomes to the shareholders -arising from the agreement between the host State and the local company-, the tribunal held that they should be considered in the valuation of damages, as appreciated in paragraph 228 of the award:

“[T]he agreements do have consequences for the Claimant in view of the fact that there are objective outcomes that benefit the Licensees to an extent... objectively the agreements will improve the business of the Licensees and to that extent the Claimant will also benefit as a shareholder... will be examined... in the context of valuation.”¹⁶

In conclusion, in order to determine whether a settlement between a local company and the host State binds foreign shareholders, the tribunal of this case distinguished whether the said agreement affected the shareholder's interests positively or negatively. It seems that the arbitrators left the door open to a

¹³ *Id.* at paragraph 225.

¹⁴ *Id.* at paragraph 225.

¹⁵ *Id.* at paragraph 227.

¹⁶ *Id.* at paragraph 228.

bilateral investment treaty claim in both scenarios because they sustained that even when the settlement benefited the shareholders, it should be considered in the “context of valuation,” a task that is proper of a tribunal, thus implying the admissibility of the claim.¹⁷

B. SAUR International S.A. v. Argentine Republic

In this case,¹⁸ the claimant was the French company Sauri,¹⁹ who controlled 100% of the shares in Aguas de Mendoza S.A., which in turn acquired 32.08% of Obras Sanitarias de Mendoza, a corporation with an administrative concession for the service of drinking water in the Mendoza province in Argentina.²⁰ The claimant alleged that some conducts of the Argentinean government amounted to a violation of a bilateral investment treaty signed with France in 1991.²¹

Relevant to this work, the tribunal forced Sauri to suffer the effects of an agreement between Obras Sanitarias de Mendoza (the local company) and an agent of the Argentinean government: the Mendoza province, called the “Second Letter of Understanding.”²² In this regard, the arbitrators stated in paragraph 358 of the decision on jurisdiction and liability the following:

“The subjective effect of *res judicata* affects in the first place the parties that reached the transactional agreement: OSM and the Province. But its effects applies also to Sauri, the shareholder that controls OSM because Sauri cannot treat as causing an expropriation those measures which its own subsidiary has considered as settled.”²³

In summary, the tribunal stated that a settlement between a local company and the host State bound the foreign shareholders, departing from what was held in *Sempra Energy International v. Argentine Republic*, where the arbitrators

¹⁷ *Id.* (Indeed, damages are only going to be evaluated in the context of a claim that was already admitted, otherwise it would not be necessary to discuss their valuation).

¹⁸ SAUR International S.A. v. Argentine Republic, ICSID Case No. ARB/04/4.

¹⁹ A wholly owned subsidiary of another French company, called Société d'Aménagement Urbain et rural S.A., or SAUR. SAUR International S.A. v. Argentine Republic, ICSID Case No. ARB/04/4. Decision on Jurisdiction and Liability (June 6, 2012), paragraphs 25 and 26.

²⁰ *Id.*

²¹ SAUR International S.A. v. Argentine Republic, ICSID Case No. ARB/04/4. Award (May 22, 2014), at paragraph 80.

²² *Id.* at paragraphs 65-67.

²³ Paragraph 358 of Decision on Jurisdiction and Liability (June 6, 2012) at SAUR International S.A. v. Argentine Republic, ICSID Case No. ARB/04/4.

sustained that foreign shareholders were not obliged by an agreement that negatively affected their interests.

C. Hochtief AG v. Argentine Republic

In this case,²⁴ the claimant was Hochtief Aktiengesellschaft and the respondent was the Argentine Republic.²⁵ As part of a consortium, Hochtief Aktiengesellschaft was adjudicated a concession to construct, maintain, and operate a toll highway and a bridge.²⁶ In order to perform the concession contract; the firm formed the corporation Puentes del Litoral S.A.²⁷ The claimant alleged breach of provisions contained in a bilateral investment treaty between Argentina and Germany.²⁸

In what concerns this work, the tribunal made a clear distinction between contract claims derived from the concession contract and treaty claims, whose source was the bilateral investment treaty between Argentina and Germany,²⁹ and to which even minority shareholders were entitled.³⁰ This has been explained in the following terms:

In the same way, the tribunal in Hochtief had to address a very similar issue when the majority of members in a consortium settled a claim with the government and the claimant did not. The tribunal recognized two independent causes of action, one under municipal law and another one under treaty law. Then, the tribunal concluded that the “question must be addressed within the particular context of the BIT, and not by proceeding from principles of municipal company law.” The decision reasoned that since there was no evidence that the claimant’s rights under the BIT were transferred to the local

²⁴ Hochtief AG v. Argentine Republic, ICSID Case No. ARB/07/31, Decision on Liability (Dec. 29, 2014).

²⁵ *Id.*

²⁶ *Id.* at paragraph 1.

²⁷ *Id.* at paragraph 68.

²⁸ *Id.* at paragraph 1.

²⁹ Paez-Salgado, *supra* note 3.

³⁰ Paragraph 171, Hochtief AG v. Argentine Republic, ICSID Case No. ARB/07/31, Decision on Liability (Dec. 29, 2014). In this regard the tribunal stated the following: “The Tribunal will first address the argument that the Tribunal should not admit a claim made by Claimant in respect of rights that belong to PdL. As was noted in the Decision on Jurisdiction, Article 1(1)(b) of the BIT is unequivocal in stipulating that an investment includes “Shares, stocks in companies and other forms of participation in companies.” Further, the Protocol to the BIT specifies that the definition of an investment includes “specifically those capital investments that do not entitle their holders to voting or control rights.” Minority shareholdings are thus clearly included.”

company to take action in his own name, the claimant retained his standing to bring claims with respect to the treatment of his shareholding under the BIT.³¹

Later, the tribunal addressed the issue of double recovery, which could have occurred in this case because Hochtief Aktiengesellschaft was protected by the bilateral investment treaty between Germany and Argentina and was also part of the concession contract.³² Regarding this matter, the arbitrators explained in paragraph 180 of the decision on liability that even assuming that the double recovery existed, “it [was] a matter concerning the remedy rather than the claim . . . To the extent that there may be a possibility of double recovery, that is a matter to be taken into account in the context of the need to prove and to qualify loss . . .”³³

Summing up, the tribunal sustained that foreign shareholders were in a position to exert their treaty rights even if there had been a previous agreement between the local company and the host State. If that is the case, the said settlement shall have to be considered in the valuation of damages, particularly “in the context of the need to prove and to qualify loss.”³⁴

IV. THE PROPOSED SOLUTION: A DISTINCTION BETWEEN THE REMEDY PURSUED AND ITS ADMISSIBILITY

The cases analyzed in section III of this work (first “Sempra”, then “Saur,” and, finally, “Hochtief”) illustrate that when it comes to the effects of a settlement by a local company and the host State in the bilateral investment treaty claims of foreign shareholders arising from the same conduct, it is possible to distinguish between the remedy pursued by the said claim and the admissibility of it.

Regarding the remedy, the tribunals agreed that a settlement by a local company and the host State could affect the content of what a party may be awarded, particularly the quantity of the alleged damages. Indeed, in Sempra the

³¹ Paez-Salgado, *supra* note 2.

³² Hochtief AG v. Argentine Republic, ICSID Case No. ARB/07/31, Decision on Liability (Dec. 29, 2014), paragraph 180.

³³ *Id.*

³⁴ *Id.*

arbitrators found that the positive effects of an agreement between third parties should be considered at the moment of valuating the damages suffered by shareholders arising from the conduct of the original claim.³⁵ In turn, in Saur the tribunal forced the shareholders to suffer the effects of an agreement called the “Second Letter of Understanding.”³⁶ Finally, in Hochtief the arbitrators affirmed that the issue of double recovery was “a matter to be taken into account in the context of the need to prove and to qualify loss...”³⁷

However, the identified ICSID procedures addressed in different ways the effects that a settlement by a local company and the host State has on the admissibility of a bilateral investment treaty claim by the foreign shareholders arising from the same conduct. Indeed, while the tribunal in Saur established that the *res judicata* effects of a transaction bound the shareholders,³⁸ in the other two cases the arbitrators estimated that bilateral investment claims were admissible even with the existence of previous agreements; always in Hochtief, and when the interests of the shareholders were negatively affected in Sempra, as appreciated from the analysis conducted before.

It seems that the position adopted in Hochtief is the most suitable to protect both the interests of foreign shareholders and the host States. Indeed, the clear separation of contract claims and treaty claims made by the tribunal allows foreign shareholders to always assert their bilateral investment treaty rights, while the consideration of previous agreements in the valuation of damages prevent host States from being condemned twice for the same conduct.

It is true that the tribunal in Sempra seems to reach similar conclusions, but the fact that the award used the expression “. . . to the extent that those interests have not been adequately satisfied . . .”,³⁹ allows arguing that if a particular agreement is beneficial for the foreign investors, they might be bounded by it. Thus, the conceptual distinction between contract claims and treaty claims is not

³⁵ Paragraph 228, *Sempra Energy International v. Argentine Republic*, ICSID Case No. ARB/02/16, Original Proceeding, Award (Sep. 28, 2007).

³⁶ *SAUR International S.A. v. Argentine Republic*, ICSID Case No. ARB/04/4. Decision on Jurisdiction and Liability (June 6, 2012), paragraph 358.

³⁷ *Hochtief AG v. Argentine Republic*, ICSID Case No. ARB/07/31, Decision on Liability (Dec. 29, 2014), paragraph 180.

³⁸ Paragraph 358 *SAUR International S.A. v. Argentine Republic*, ICSID Case No. ARB/04/4. Decision on Jurisdiction and Liability (June 6, 2012)

³⁹ *Sempra Energy International v. Argentine Republic*, ICSID Case No. ARB/02/16, Original Proceeding, Award (Sep. 28, 2007), paragraph 228.

drawn as clearly as in Hochtief, seeming to be conditioned to the outcome – positive or negative- of the settlement between the local company and the host State.

In sum, the decision in Hochtief illustrates that it is not necessary to forbid the presentation of a bilateral investment treaty claim in order to avoid double recovery after a settlement is reached; it is enough to consider the effects of the said agreement in the valuation of the alleged damages. This is the better way to preserve both the interests of the foreign shareholders and the host States.

V. BASIS FOR THE SOLUTION PROPOSED

The solution proposed implies that contract claims are different from the claims that arise from a bilateral investment treaty. Otherwise, the settlement reached by the host State and the local company would preclude any further action regarding the same conduct. In addition, it requires the existence of a law principle forbidding a party to benefit twice from compensations arising from the same facts.⁴⁰

A. Distinction Between Treaty And Contractual Claims

Currently the differentiation between treaty and contractual claims is a “standard feature of recent investment arbitrations.”⁴¹ As further evidence of their importance, scholars have even developed tests in order to distinguish them.⁴² Therefore, a settlement reached between the local company and the host State does not preclude the actions available under a bilateral investment treaty.

B. The Civil Law Doctrine Of Unjust Enrichment

The principle of unjust enrichment is an equitable concept created to remedy injustices that occur where one person makes a contribution to the property of another without a valid cause.⁴³ As stated, “consistent reliance supports the idea

⁴⁰ For instance, if treaty claims are not precluded after a settlement is reached, the host State could face the risk of paying twice for the same conduct: the first time through the said settlement and the second time because of a condemnation under a treaty claim.

⁴¹ Christoph Schreuer, *The Dynamic Evolution of the ICSID System*, in THE INTERNATIONAL CONVENTION ON THE SETTLEMENT OF INVESTMENT DISPUTES (ICSID) 15-30 (Rainer Hofmann & Christian J. Tams ed., 2007), available at http://www.univie.ac.at/intlaw/wordpress/pdf/85_cspubl_86.pdf.

⁴² HEGE ELISABETH KJOS, *APPLICABLE LAW IN INVESTOR-STATE ARBITRATION: THE INTERPLAY BETWEEN NATIONAL AND INTERNATIONAL LAW* 111 (2013)

⁴³ This is a simple definition given only for the purposes of this article. However, the truth is that defining unjust enrichment is not an easy task. As one author noted, “Unjust enrichment eludes definition, its imprecise nature simultaneously lending itself to and

that unjust enrichment is a general principle of international law,” and it could be an important tool in the context of international investment arbitration if “used precisely and sparingly.”⁴⁴

Under the aforementioned concept, a party cannot become richer without a valid justification.⁴⁵ Therefore, the principle of unjust enrichment allows a party to be compensated only once from the damages suffered by a particular set of facts, thus avoiding the risk of double recovery.

However, a question remains of “when” the principle should be applied during a procedure. The decisions in *Hochtief* and *Sempra* can be used to support that the principle of unjust enrichment should play a role at the moment that the tribunal determines the quantum of the damages. Indeed, in *Hochtief* the tribunal affirmed that the issue of double recovery was “a matter to be taken into account in the context of the need to prove and to qualify loss...”,⁴⁶ while in *Sempra* the arbitrators sustained that the positive effects of a settlement between third parties should be considered at the moment of valuating the eventual damages suffered.⁴⁷

Summing up, the principle of unjust enrichment could be useful to avoid the risk of double recovery derived from the separation between treaty claims and contract claims, being possible to recognize at least one procedural moment in which it could be applied: the valuation of damages by the arbitrators.

CONCLUSION

A settlement between a local company and the host State does not preclude the right of foreign shareholders to exercise a bilateral investment treaty claim,

defying misapplication.” Ana Vohryzek-Griest, Comment, *Unjust Enrichment Unjustly Ignored: Opportunities and Pitfalls in Bringing Unjust Enrichment Claims Under ICSID*, YALE LAW SCHOOL LEGAL SCHOLARSHIP REPOSITORY 6 (2008), available at http://digitalcommons.law.yale.edu/cgi/viewcontent.cgi?article=1072&context=student_papers.

⁴⁴ *Id.* at 1, 4.

⁴⁵ As explained by an author, “the law repudiates the enrichment of somebody at the expenses of other without a valid cause”. Daniel Peñailillo, *El enriquecimiento sin causa. Principio de derechos y fuentes de obligaciones*, REVISTA DE DERECHO UNIVERSIDAD DE CONCEPCIÓN, 5 (1996), available at file:///C:/Users/usuario/Downloads/2575.pdf

⁴⁶ *Hochtief AG v. Argentine Republic*, ICSID Case No. ARB/07/31, Decision on Liability (Dec. 29, 2014), paragraph 180.

⁴⁷ *Sempra Energy International v. Argentine Republic*, ICSID Case No. ARB/02/16, Original Proceeding, Award (Sep. 28, 2007), paragraph 228.

but the said settlement has to be considered by the tribunal at the moment of determining an eventual compensation in order to avoid double recovery. The aforementioned is supported by the ICSID decision in *Hochtief*, the assented distinction between treaty and contractual claims and the applicability of the civil law principle of unjust enrichment in the field of international investment arbitration.