

# ICSID's Jurisdiction over Arbitration of Transnational Investment Treaties of State-owned Enterprises—From “Beijing Urban Construction Group v. Yemeni Government” Case Concerning Jurisdiction

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**Abstract:** The case of "Beijing Urban Construction Group v. Yemeni Government" concerning jurisdiction is the first case in which China, as an applicant, initiated arbitration to ICSID arbitration tribunal and won the jurisdiction. Especially, the nature of the Chinese party as a state-owned enterprise is special and more representative. Through this case, three elements of ICSID jurisdiction are emphatically analyzed. The following points are analyzed one by one, i.e., whether the investor (i.e. the commercial nature of Chinese state-owned enterprises) is qualified, whether the state-owned enterprises, especially the state-owned enterprises under the socialist market economic system with Chinese characteristics have the investment behavior meeting the prescribed criteria, whether they are obliged to perform the legal procedures of the domestic laws of the host State, the standard of interpretation of disputes in the agreement between both parties involved, the issue of expropriation and compensation, (most-favored-nation status) MFN in bilateral investment protection treaties and the distinction between claims in basic transaction contracts and claims in treaties. Finally, it is suggested that the Umbrella Clause, the Fork-in-the-road Clause should be stipulated in the bilateral investment protection agreement, and the investment subject status of Chinese state-owned enterprises should be clearly affirmed.

## 1. Introduction

The parties to a transnational investment usually regulate their rights and obligations by concluding a bilateral investment protection agreement to protect their rights and interests, and the ultimate goal is to balance the rights and obligations of both parties. In the case of dispute settlement between the host State and the investor, a large part of the parties to the dispute will choose the ICSID arbitral tribunal to settle the dispute due to its objective and impartial status and the goal of establishing an ICSID. Therefore, more and more agreed dispute settlement clauses are used by the ICSID in bilateral investment protection agreements concluded by the parties. However, due to the different subjects and the specific circumstances of the contracting states, the scope and elements of the ICSID arbitration agreement are also different to a large extent. In this paper, the jurisdiction of ICSID arbitration tribunal will be analyzed through the case of Beijing Urban Construction Group v. Yemeni Government concerning jurisdiction.

## 2. Case Analysis

### 2.1 Review

The parties involved in this case are Beijing Urban Construction Group Co., Ltd. (hereinafter referred to as "Beijing Urban Construction Group") and the Civil Aviation Administration of Yemeni Government. On February 28, 2006, the two parties signed a contract for the construction of the terminal building of the International Airport of the Civil Aviation Administration of the

Yemeni Government by Beijing Urban Construction Group. Shortly after the beginning of the contract, there appeared a certain degree of contradiction and conflict between the parties. As these conflicts have not been settled, they gradually fermented over time. Until July 2009, the Yemeni government and its military and security agencies hired local armed forces to intervene, obstruct, harass and intimidate Beijing Urban Construction Group into the construction site, and illegally detained and violently attacked the staff of Beijing Urban Construction Group. As a result, Beijing Urban Construction Group was completely unable to fulfill the construction contract signed with the Yemeni government. Instead, it was recriminated by the Yemeni government and complained that it had not fulfilled its obligations under the contract. Since then, the project of Beijing Urban Construction Group has been suspended. Due to repeated unsuccessful negotiations between the two parties during the two years, the staff of Beijing Urban Construction Group have all withdrawn from Yemen after the difficulties and dangers, even risking their lives.

Beijing Urban Construction Group eventually submitted arbitration to ICSID in 2014 in accordance with the Washington Convention (i.e., the Convention on the Settlement of Investment Disputes between States and Nationals of Other States) and the bilateral investment agreement between China and Yemen. Since the date of filing the application, after three years of hard and long waiting, the Chinese side finally won the ICSID jurisdiction in 2017, which is a landmark case in the dispute settlement of China's overseas investment.

## **2.2 Focus of Case Dispute and Definition of Jurisdiction**

The premise of ICSID protection is that ICSID has jurisdiction over the case. The current work of ICSID is to ensure the fairness of the cases handled, to respond positively to the increasing number of cases, while maintaining low costs [1]. In accordance with Paragraph 1, Article 25 of the Washington Convention, disputes submitted should satisfy the three preconditions mentioned above: first, in terms of the subject, the parties to the dispute must satisfy the nationals of one country (the State party to the Convention) and another (discussing the approximate scope); secondly, in terms of the object (i.e. the content of the dispute): the dispute submitted must be a dispute arising directly from investment; finally, in terms of the procedures, the parties agree in writing to submit the dispute to ICSID. In the judgment process of this case, the Yemeni government separately raised objections to all the elements of the constituent elements.

### **2.2.1 Is the "Investor" Qualified in this Case?**

The basis of the Yemeni government's argument is that they believed that the identity of Beijing Urban Construction Group in this case is a state-owned enterprise, which can be directly regarded as a "state-owned entity" and, to a certain extent, an "agent" of the government. Based on the 2001 Draft Articles on Responsibility of States for Internationally Wrongful Acts, it argued that because Beijing Urban Construction Group exercises the government's rights and accepts the leadership, command and control of the government, it does not comply with the "other nationals of the State party" as stipulated in Article 25 of the Washington Convention. In order to expand jurisdiction and make the Washington Convention flexibly applicable, ICSID only made the following provision for the requirement of "nationals of another State party", that is, natural or legal persons belonging to another Contracting State as long as after a certain period of time are within the scope of this provision. There are no regulations or restrictions on state-owned enterprises peculiar to China and other countries or regions. This was a foreshadowing and hidden danger in whether the Beijing Urban Construction Group can obtain the jurisdiction of the ICSID under the Washington Convention.

Beijing Urban Construction Group held that in this project, the act was not controlled by the Chinese government, nor was it an agent of the Chinese government. This was a purely commercial act and still met the qualifications of the "other nationals of the contracting parties" under the Convention. In this regard, we can adopt a precedent-based approach, which is, referring to the previous case of *Cescoslovenska Obchodni Banka, A.S. v. The Slovak Republic* ("CSOB"), the application of the Broches standard is as follows: it is undeniable that for most of its existence, CSOB acted on behalf of the State to promote or implement international banking transactions and

foreign commercial activities that the State wishes to support, and the State's control of CSOB requires it to implement national competition in this regard. However, in determining whether CSOB performs government functions in the performance of these functions, the focus must be on the nature of these activities, rather than on their purpose. Although CSOB was undoubtedly promoting government policies or purposes in carrying out these activities, the activities themselves were essentially commercial rather than governmental. The final result of CSOB case was that CSOB could obtain ICSID jurisdiction. Secondly, Beijing Urban Construction Group won the bid because of its professional and commercial value, not its relationship with the Chinese government. Accordingly, the arbitral tribunal ultimately supported the views of the Beijing Urban Construction Group.

### **2.2.2 Does the Project Contracting Behavior of Beijing Urban Construction Group Belong to the “Investment” Behavior in This Case?**

On the basis of the above argument, the Yemeni government believed that since Beijing Urban Construction Group is a state-owned enterprise, according to the way of socialist governance with Chinese characteristics, its actions must also be state-controlled, so it cannot be regarded as a dispute arising directly from investment. According to the Washington Convention, there is no clear definition and scope for "investment behavior", but the content is given to the member states as parties, and they themselves define the scope of "investment" according to the needs of individual circumstances. "There is no clear and consistent definition of international treaties or international customs"[2]. Therefore, in this case, the arbitral tribunal needs to make a final judgment by understanding the Bilateral Agreement between China and Yemen. According to Paragraph 1, Article 1 of the Bilateral Agreement Between China and Yemen: "In this Agreement, 1. "Investment" means all assets and shares directly or indirectly invested by the investors in the territory of the other State party in accordance with the laws and regulations of the other State party, in particular, but not limited to: (1) chattel, real estate and all other property rights, such as mortgage and pledge, physical security, usufruct and similar rights;" According to the provisions of this clause, the project contracting behavior of Beijing Urban Construction Group has first met the first scope, belonging to "all assets and shares directly or indirectly invested by one State party in the territory of the other State party in accordance with the laws and regulations of the other State party ". On the other hand, the project contracting act is a right related to real estate stipulated in the first paragraph of this article. The project contracting act of Beijing Urban Construction Group belongs to qualified investment behavior, either in terms of the provisions of the Washington Convention or the contents of the Bilateral Agreement between China and Yemen.

This case can refer to the Salini standard extended from the Salini v. Morocco case in 2001, which can be used as a precedent providing some inspiration and reference, and was concluded that the investment stipulated in paragraph 1, Article 25 of the Washington Convention should meet the exact definition that four elements must be met simultaneously: investment, a certain duration of contract performance, the assumption of transaction risks, and the sustained contribution to the economic development of the host State. In this case, these four elements are very helpful for Beijing Urban Construction Group to support its claim. First of all, Beijing Urban Construction Group had invested a lot of money in the early stage of the project, even in the preparatory stage, for the purchase of equipment, etc. for the smooth development of follow-up work. Secondly, from the signing of the contract between the two sides in 2006 to the employment of armed forces by the Yemeni government in 2009 when the project suspended, the construction behavior of Beijing Urban Construction Group had lasted for three years, meeting a certain duration of contract performance. Thirdly, from the beginning of signing the construction contract, Beijing Urban Construction Group had undertaken commercial and political risks, and even risked the lives of its employees. Finally, the project contracted by Beijing Urban Construction Group is the construction of the terminal building of Yemen International Airport which, as a national infrastructure construction project, promotes not only the tourism industry, but also the domestic freight and trade industries. Therefore, there is no doubt that the construction of this project is conducive to the

economic development of the host State. Although there are certain risks and uncertainties in applying the precedent, and the “continuous contribution to the economic development of the host state” in the standard is still controversial [3], in this case, it has great value and advantages to select a good reference for our country.

### **2.2.3 Is the Breach of Contract by Yemeni Government a Breach of Contract or a Breach of Treaty?**

This issue is also one of the factors influencing the jurisdiction of ICSID arbitral tribunal. If the nature of the dispute is ultimately considered to be a contractual dispute, then the Yemeni government may argue that the dispute is not subject to the jurisdiction of the ICSID arbitral tribunal and that it is irrevocable once submitted, and that the dispute may then be settled in accordance with the relevant domestic laws and regulations of the host State (Yemen), which is extremely unfavorable to Beijing Urban Construction Group. The important clauses involved in this issue are the Umbrella Clauses. In recent years, China has basically stipulated Umbrella Clause in bilateral investment protection agreements with other countries, which are used to stipulate that a State party should abide by its specific commitments to the other State party. If the parties agree on this clause in the bilateral investment protection agreement, the conduct in the contract performance will not only constitute a breach of contract, but may also be a breach of treaty. However, because the Bilateral Agreement between China and Yemen was signed earlier, the two sides did not agree on the Umbrella Clause therein, so the key to distinguish between contract breach or treaty breach laid in whether the Yemeni government had actually taken the "expropriation act". As the ICSID arbitration tribunal said in its ruling, the Yemeni government did not adopt a positive and friendly attitude to negotiate and resolve conflicts between the two sides. Instead, it directly adopted serious violence. Faced with such a situation, the Yemeni government still ignored the diplomatic notes sent to it by the embassy and insisted on its own actions, constantly threatening the lives and property security of staff of Beijing Urban Construction Group. This series of actions led the arbitral tribunal to conclude that the dispute was not only a "contract dispute" but also a "treaty dispute". Finally, the ICSID arbitration tribunal had the jurisdiction over the case, and Beijing Urban Construction Group won the case.

### **2.2.4 Can the MFN Clause Agreed in the BIT Also Apply to Dispute Settlement?**

MFN status is a common rule in international social interactions and is basically universally applicable. The International Law Commission of the United Nations defines MFN status as: "the country which is the recipient of this treatment must nominally receive equal trade advantages as the "most favoured nation" by the country granting such treatment. In effect, a country that has been accorded MFN status may not be treated less advantageously than any other country with MFN status by the promising country." Applying MFN status to BIT may involve the following two issues: first, if the BIT can be cited by the parties to the dispute, then whether one of the parties can ask the other party to grant the same rights under the treaty with other countries in accordance with the MFN clause agreed in the BIT [4], which is also reflected in this case: based on the MFN clause in the bilateral investment protection agreement signed between Yemen and the United Kingdom, the Chinese party requires the Yemeni government to grant Beijing Urban Construction Group the right to equate to the MFN status enjoyed by other countries. However, the arbitral tribunal did not ultimately support this request. Secondly, can the other party under bilateral investment protection agreements signed by the country with other countries have more preferential rights under other treaties, including dispute settlement clauses? In the *Murphyzni* case, for example, *Murphyzni* (Argentine Investor) argued that the MFN clause agreed in BIT could be applied to dispute settlement. He had the right to cite the more favourable dispute settlement clause in the bilateral investment protection agreement between Spain and Chile, because he could directly submit the dispute to the ICSID arbitral tribunal for a more objective and fair settlement, in order to protect his own interests.

### **3. Suggestions on Remedy of State-Owned Enterprises Through Icsid Arbitral Tribunal**

#### **3.1 Agreement on Umbrella Clause and Fork-in-the-road Clause in Bilateral Investment Protection Agreement**

The Umbrella Clause mainly concerns the distinction between contract claims and treaty claims for underlying transactions. The result of differentiating contract claim from treaty claim will directly affect any breach of contract by the parties to the dispute, which may turn to the breach of BIT signed by both parties, and then the ordinary breach of contract will turn to the breach of obligations at the level of international law. However, it should be noted that not all breaches of ordinary contractual obligations will turn into breaches of BIT. Only when one party breaches the contract and simultaneously breaches the obligations of BIT, it is possible to be a breach of international law obligations. At this time, the breaching party will be liable for violations of international law at this time, not just simple contract breaches. The parties to the dispute in this case did not agree on the Umbrella Clause in BIT, so they can only distinguish contract claims from treaty claims by judging the expropriation behavior of the Yemeni government.

The Fork-in-the-road Clause refers to the right of foreign investors to choose one way of dispute settlement for local remedies and international investment arbitration in the host State, and once chosen, it is final and no other way of remedy can be sought, which is often used in conjunction with the principle of exhaustion of local remedies, but its essence is the opposite. The essence of the Fork-in-the-road Clause is that foreign investors can only choose one way to make a claim. If the result is not satisfactory, foreign investors can only accept and cannot seek other means of relief again. To some extent, the operation of this clause solves the problem of waste of resources, so that the relief period of the case is no longer lengthy. This clause is a variant of the traditional principle of exhaustion of local remedies. The traditional way of remedy in international investment is that foreign investors must exhaust all local judicial resources of the host State and still can not obtain remedy before they can submit the dispute to the arbitration body agreed in the treaties of the two parties for arbitration. One of its drawbacks is that it is more in line with the development needs of the host State. Especially for developing countries as capital importing countries, it is naturally best to resolve disputes within their own territory. However, this is inevitably unfair to foreign investors to a certain extent who usually will go through the process of local remedies in a hasty way, which wastes the judicial resources of the host State in vain. Therefore, although there are many disputes in practice, the Fork-in-the-road Clause is of value.

#### **3.2 Definitely Affirming the Investment Subject Status of Chinese State-owned Enterprises in Bilateral Investment Protection Agreements**

Through the above analysis, although the state-owned enterprise in this case won the jurisdiction, the process is extremely arduous. It is not only necessary to interpret the provisions of the Washington Convention itself in favor of itself, but also need to convince the arbitral tribunal to make decisions in favor of itself through indirect means with the judgment criteria of other cases and case awards. The result of the award in this case is to some extent a very contingent case, because most of the controversial factors do not have a clear conclusion in the field of international commercial arbitration. According to the composition of each arbitration tribunal, the same case may get a contrary award. In this case, the individual coping style of Beijing Urban Construction Group can indeed provide an excellent template for similar cases in the future, but there is no doubt that the adjudication process of such cases cannot be used as a basis for effectively protecting the interests of Chinese state-owned enterprises as foreign investors. Therefore, in the case of Chinese state-owned enterprises as foreign investors, when signing bilateral investment protection agreements with the host State, they should, as far as possible, clarify the status of “qualified investors” in the articles, so as to reduce the occurrence of such disputes, which is more conducive to protecting the interests of state-owned enterprises outside.

#### **4. Conclusions**

According to the Washington Convention, ICSID's jurisdiction over transnational investment disputes requires three elements: firstly, the parties to the dispute must be nationals of one State party and another State party; secondly, the acts leading to the dispute are legal acts and fall within the scope of "investment" stipulated in bilateral investment protection agreements signed by both parties; finally, both parties have given written consent to submit the dispute to ICSID arbitration tribunal without specific formal requirements.

In this case, Beijing Urban Construction Group won the ICSID arbitral tribunal's jurisdiction as a special foreign investment subject. In order to protect the legitimate interests and demands of the increasing number of Chinese state-owned enterprises in transnational investment as special business entities in the future, and to cope with or even prevent disputes from arising, when signing bilateral investment protection agreements between state-owned enterprises and host States, besides agreeing on favorable terms such as Umbrella Clauses, attention should be paid to qualifying their own positions.

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