Phoenix Action Ltd. v. The Czech Republic, ICSID Case No. ARB/06/5, Award of April 15, 2009 – Concept of investment under the ICSID Convention revisited

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In a decision rendered on April 15, 2009, a three-member tribunal composed of Brigitte Stern as chairperson, Andreas Bucher and Juan Fernandez-Armesto rejected Phoenix Action Ltd's ("Phoenix") claims against the Czech Republic.

By way of background, Phoenix is an Israeli company which purchased two Czech companies, Benet Praha ("BP") and Benet Group ("BG"), in 2002 while these two companies were involved in ongoing legal disputes – BG with a private party, BP with the Czech fiscal authorities. The Czech Republic challenged the jurisdiction of the Tribunal on the basis that Phoenix was an *ex post facto* sham Israeli entity created by a Czech national in order to establish diversity of nationality. The Czech Republic specifically asked the Tribunal to decide whether a foreign entity could be created for the sole purpose of establishing diversity of nationality, thus triggering ICSID jurisdiction.

In its decision, the Tribunal revisited the often-cited "*Salini* test" which attempts to determine whether there is an investment for the purposes of Article 25 of the ICSID Convention. The *Salini* test sets out four criteria for an investment to qualify as such under the ICSID Convention, i.e. (a) a contribution of money or other assets of economic value, (b) a certain duration, (c) an element of risk, and (d) a contribution to the host State's development.

The Tribunal refused to rely exclusively on the *Salini* test. Instead, the Tribunal concluded that for an investment to benefit from the international protection of ICSID, the following six elements had to be taken into account:

"1 – a contribution in money or other assets;
2 – a certain duration;
3 – an element of risk;
4 – an operation made in order to develop an economic activity in the host State;
5 – assets invested in accordance with the law of the host State;
6 – assets invested *bona fide*."

The purpose of this blog entry is to focus on the fifth element developed by the Tribunal, *i.e.* assets invested in accordance with the law of the host State.

As a preliminary matter, it is of note that the Czech Republic in its objections to jurisdiction did not raise an argument on the grounds of a violation by the claimant of a rule of the Czech Republic legal order.

Nevertheless, the Tribunal devoted a portion of its award to the fact that only investments made in accordance with the laws of the host State may have access to the ICSID dispute settlement mechanism.

Interestingly, the Tribunal noted that the conformity of the establishment of the investment with the national laws was implicit "even when not expressly stated in the relevant BIT." This position confirms the position adopted in *Plama v. Bulgaria*, where the tribunal was faced with the silence of the relevant treaty on the necessary conformity of a protected investment with the laws of the host country. The *Plama* tribunal found that even if the Energy Charter Treaty did not contain a provision requiring the conformity of the investment with a particular law, the substantive protections of the Energy Charter Treaty could not apply to investments made contrary to law.

In practice, a tribunal assessing the conformity of the investment with the host State's law will generally take into account the laws in force at the moment of the establishment of the investment. Of course, the Tribunal noted, the host State may not modify the scope of its legislation or what qualifies as an investment under its laws to escape liability under the relevant treaty.

The criterion of whether an investment is made in accordance with the law of the host State is decisive to determine whether the investment will be "protected". An operation otherwise qualifying as an investment but made in violation of the laws of the host State may not qualify for protection under a particular treaty.

The Tribunal stated that if it is manifest that the investment has been performed in violation of the law, this will constitute a bar to the tribunal's jurisdiction. This development is in line with other decisions of ICSID tribunals, notably the *Fraport v. Philippines* decision where the tribunal denied its jurisdiction on the grounds that Fraport had intentionally structured its investment in a way which it knew to be a violation of the host State's legislation. Notably, however, that case contained an "accordance with law" requirement in the applicable BIT.

The *Phoenix Action* decision is novel insofar as the Tribunal ruled that even absent any provisions to that end in the relevant treaty, an investment will benefit from the protections of the treaty, and hence a tribunal will have jurisdiction, only if the investment is made in accordance with the law of the host State.

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