

# Kluwer Arbitration Blog

## ICSID Arbitration: Should a State be Liable for the Conduct of a State University?

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Whereas cases of direct expropriation have become relatively rare in international investment arbitration and claims of breach of fair and equitable treatment obligation or indirect expropriation are currently more common, the profile of respondents in ICSID arbitration proceedings has also changed. However, if both investors and host governments are likely to agree that States may be held responsible for the actions of the governmental authorities, it remains controversial whether States may be held liable for the acts of, for example, a state university.

The issue of attribution of the conduct of Taras Shevchenko National University of Kyiv (“the University”) to Ukraine was considered in the recent ICSID Award of 25 October 2012 in *Bosh International, Inc and B&P Ltd Foreign Investments Enterprise v. Ukraine* (ICSID Case No. ARB/08/11) where the tribunal rejected the allegations of the Claimants – Bosh, a US-registered company, and its Ukrainian subsidiary, B&P – that Ukraine breached certain provisions of the *Treaty between the United States of America and Ukraine concerning the Encouragement and Reciprocal Protection of Investment*, entered into force on 16 November 1996 (“US-Ukraine BIT”). The dispute related to a partnership contract for the renovation and operation of a Science-Hotel Complex (“Contract”) entered into between B&P and the University. The University later terminated the Contract following the alleged breaches by B&P of its contractual and legal obligations.

The highlight of the tribunal’s decision in *Bosh case* was the conclusion it reached with respect to the attribution of the University’s conduct to Ukraine. To begin with, the tribunal briefly noted that it could not agree that the University was a State organ within the meaning of Article 4 (Conduct of organs of a State) of the *International Law Commission Draft Articles on Responsibility of States for Internationally Wrongful Acts* (“ILC Articles”). Thus, the real question to be answered was whether the University’s conduct could be attributable to Ukraine under Article 5 (Conduct of persons or entities exercising elements of governmental authority) of the ILC Articles, which required to establish, cumulatively, that: (1) the University was empowered by the law of Ukraine to exercise elements of governmental authority; and (2) the conduct of the University related to the exercise of that governmental authority. (Award, para. 164)

In the tribunal's opinion, the first condition of this test was satisfied since the provision of higher education services and management of state-owned property constituted forms of governmental authority that the University was empowered to exercise, although the University was a separate legal entity with a large degree of autonomy. (Award, paras 172-173) With respect to the second limb of the test, the tribunal noted that the commentary to the ILC Articles explains that "[i]f it is to be regarded as an act of the State [...], the conduct of an entity must accordingly concern governmental activity and not other private or commercial activity in which the entity may engage". (ILC Articles with commentaries, Article 5, para. 5) However, under the Ukrainian Law and the University's Charter, the University was entitled, in its own right and without the need for any particular authorization by Ukraine, to enter into the Contract, which was a private or commercial activity aimed at securing commercial benefits for both parties. (Award, para. 177) As the University's conduct in entering into and termination of the Contract did not relate to the exercise of the University's governmental authority, the tribunal concluded that it was not attributable to Ukraine. (Award, para. 178)

Similar line of reasoning was adopted by the ICSID tribunal in *EDF (Services) Limited v Romania* (ICSID Case No. ARB/05/13), Award of 8 October 2009. There the tribunal, guided by Article 4 of the ILC Articles, found that neither Bucharest Airport ("AIBO") nor Romanian National Airline Company ("TAROM") can be considered State organs, as they both possessed, under the Romanian law, legal personality separate and distinct from the State. Also, Article 5 of the ILC Articles did not support the attribution of the conduct of AIBO and TAROM to Romania. The tribunal found that the auctions organized by AIBO, the exercise by AIBO and TAROM of their rights as shareholders in joint venture companies established with EDF, ASRO and SKY, and AIBO's and TAROM's contractual relations with EDF were not exercises of delegated governmental authority as those actions were done "in pursuit of the corporate objects of a commercial company with the view to making profits". (Award, para. 197)

However, in the *EDF case*, the tribunal held the conduct of AIBO and TAROM attributable to Romania under Article 8 (Conduct directed or controlled by a State) of the ILC Articles. The tribunal found that the conduct of AIBO and TAROM as shareholders of ASRO and SKY was under the direction and control of the State, and it was carried out in order to bringing the contractual arrangements with EDF and ASRO to an end. To the contrary, in the *Bosh case* no argument under Article 8 of the ILC Articles was made.

Another issue is whether a claim against the host State under such circumstances may be made on the basis of an **umbrella clause**. For instance, the US-Ukraine BIT provides that "each Party shall observe any obligation it may have entered into with regard to investments." (Article II(3)(c))

In the *Bosh case*, the tribunal concluded that the term "Party" in the umbrella clause refers to any situation where the Party is acting *qua* State. (Award, para. 246) Thus, it is only where the conduct of an entity can be attributed to the Party, such entity may be considered to be "the Party" for the purposes of the umbrella clause. (Award, para. 246) Even though an umbrella clause may make a claim arising out of a contract justifiable under a treaty, in none of the past cases was the contract entered into by an

investor with an entity similar to the University. (Award, para. 248) For instance, in *Eureko v Poland*, the contract was concluded with the State Treasury of Poland; in *Noble Ventures, Inc v Romania* - with the Romanian State Ownership Fund; in *Azurix Corporation v Argentine Republic* - with the Province of Buenos Aires; etc. (Award, para. 248) Because in the *Bosh case* the University's conduct with respect to entering into and termination of the Contract was not attributable to Ukraine, the Tribunal ruled that the Claimants' allegation on the breach of the umbrella clause should fail. (Award, para. 249)

Overall, the recent award in the *Bosh case* suggests that the ICSID tribunals may be hesitant to broaden the scope of the BITs by attributing the conduct of entities such as a university to a State. The issue of attribution is likely to be addressed on case-by-case basis, with the ILC Articles serving as guidelines. Furthermore, in cases where the conduct of an entity is non-attributable to the State, claimants may not be able to seek relief on the basis of an umbrella clause.

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