New Challenges to the Territorial Requirements of Investment Treaties: Can Social Platforms Be Protected?

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The explosive development of IT companies offering social platforms (social networking and instant messaging applications) over the past years has gifted us with many tools that we now use on a daily basis. Facebook, LinkedIn, Instagram, What's App, Skype, Telegram and many others services help us to stay in touch with people all around the globe.

These social platforms may use different methods to generate profit but evidently many of those methods would rely on their biggest asset – their users. A good example of that is advertisement and sponsored content – on Facebook or LinkedIn, the advertisements are almost inevitably tailored to interests and previous behaviour of the person using the account, making any form of commercial on social platforms quite attractive for advertisers.

The rapid development of social media and messaging has not escaped the attention of governments, many of which have been expressing concerns that unregulated use of social media and encrypted messaging may be dangerous.

One of the points of criticism voiced by the regulators revolves around the idea that in some cases it can be difficult even for the operator of the social platform to find out the real identity of the user; therefore, a platform can facilitate communication between criminals or impair security of personal data.

For example, Russia has lately prescribed that all IT companies operating social platforms in its territory must store personal data and users' correspondence on server infrastructure in Russia as well as make any encrypted communications exchanged on the social platforms accessible to law enforcement. Following failure to comply with some of regulations, LinkedIn has been banned on the entire Russian territory. Telegram, a popular messaging application has suffered the same fate last week. Ban on Facebook might also follow.

Another area of criticism is the recent *fake news* phenomena. One of the examples of related measures is Ukraine's ban on Russian companies operating search engines, social networks, news portals and rendering other ancillary services on Ukrainian territory. There is also an ongoing investigation against Russian nationals allegedly massively distributing misleading information through social platforms in the wake of the US presidential elections.

The examples given above demonstrate that states have a wide array of regulatory tools that can

complicate the life of IT companies. At the same time, if one would take a look at the simplified example of their business, the main assets of an IT company would likely to consist of applications (software products, related intellectual property rights and operating licenses), infrastructure (i.e. equipment used to run the software) and most importantly the clientele – users. Due to the specifics of the business those assets are not necessarily located in the same jurisdiction.

Hence, the question arises: could a tribunal, operating under the framework of an investment treaty, have jurisdiction in respect of investments of a company that has marginal amount of real assets on the host-state territory, but operates a social platform there?

For *prima facie* analysis, let's use a hypothetical example.

John Doe (JD) is a messaging application, enjoying worldwide popularity among the users. JD is operated by John Doe LLP (JD LLP), a British company. JD was launched on the Russian market in 2010 and does not have any physical assets in Russia. It has met all the local legal requirements necessary for its operation at the time of its launch. JD has also built server infrastructure in a third country in order service the Russian market.

JD's User agreement states that users will always enjoy free and secure use of JD and JD LLP can integrate any profit generating mechanism in JD application. JD's income on the Russian market derives from such profit generating mechanisms. After legislation prescribing disclosure of JD's encryption protocols to law enforcement is enacted in Russia, JD refuses to comply. Russia then prohibits access to JD's servers on its entire territory.

Since JD LLP is a British company, it can resort to the 1989 Agreement for the Promotion and Reciprocal protection of Investments between Russia and the UK (further referred to as the "**BIT**"). The BIT contains many features and definitions typical for treaties of its time.

The BIT extends its protections to *"[…] any corporations, companies, firms, enterprises, organisations and associations incorporated or constituted under the law in force in the territory of the that Contracting party"* (*N.B. – to the BIT*).

Its definition of investment is open-ended and asset based – "*every kind of asset and in particular, though not exclusively […] movable and immovable property […] rights conferred by law or under contract […] to undertake any commercial activity*".

The BIT also contains a territoriality requirement which can be deduced by systematic interpretation of its substantive treatment provisions (namely Articles 2, 3 and 5 of the BIT) and its preamble.

Upon initial examination JD LLP should meet the definition of investor under the BIT. The situation with the possible "investment" is more difficult in light of the location of some assets and territorial requirements of the BIT.

In our hypothetical, JD LLP will have three assets that could meet the definition of investment: firstly, the right to operate JD application and render services to its users in Russia conferred by law, secondly, portfolio of contractual rights arising under JD User agreement between the users and JD LLP, and, finally, the server infrastructure built for the Russian market.

Viewed separately, only part of those hypothetical assets can arguably pass the territoriality test necessary to qualify as an investment. However, all three assets serve same purposes – rendering of services to Russian users under JD User agreement and generation of profits. For that reason and for the purposes of qualifying the above-mentioned assets as an investment it might be useful to look at

the entire set of assets holistically.

A holistic approach to the identification of assets capable of qualifying as an investment has already been used in a number of cases, *inter alia,* in *SGS v. Philippines, Inmaris v. Ukraine* and *Alpha v. Ukraine* cases. Those cases also were resolved on the premise of similar treaty definitions of investment as the ones found in the BIT. [FN]*SGS Société Générale de Surveillance S.A. v. Republic of the Philippines, Decision of the Tribunal on Objections to Jurisdiction, Alpha Projektholding GmbH v. Ukraine, ICSID Case No. ARB/07/16, Inmaris Perestroika Sailing Maritime Services GmbH and Others v. Ukraine, ICSID Case No. ARB/08/8*[/FN]

In *SGS v. Philippines*, the Tribunal came to a conclusion that as *SGS* undertook costs to set up business structure aimed at provision of services to Philippines on the territory of Philippines in several jurisdictions. In *Alpha*, capital contributions necessary for renovation of a hotel in Kyiv were made outside of Ukraine, while the economic effect of those contributions has occurred in Kyiv and resulted in renovation works in the building of the above-mentioned hotel. Similarly, in *Inmaris*, payments resulting in augmentation of property on the Ukrainian territory were made outside of Ukraine. The tribunals in all cases found that there was an investment and it met the territorial requirements of the BIT even though considerable parts of the investment were carried outside of the host-state. In all of the cases tribunals have focused on the question of where the economic effect of the investment activity takes place.

Upon initial analysis, this economically essential part of performance of JD LLP's obligations takes place when Russian users of JD generate profit for JD LLP by using the application. Therefore, provided the analogy with the above-mentioned case law is sustainable, it can be argued that the economic effect of the investment takes place in Russia, so entire scope of assets can possibly be attributed to one asset of JD qualifying as an investment – for example contractual rights arising under JD User agreement between the users and JD LLP.

Of course, the holistic approach cannot be used to circumvent the definition of investment – in all above-mentioned cases the tribunals identified the assets that were capable of meeting the treaty definition of investment as well as their close economic link to the territory of the host state. Arguably, the main purpose of the holistic approach is to produce a plausible explanation as to why territorial requirements of a treaty are met by some assets of the investor if such assets were created outside of territory of the host-state for the purposes of the investment.

Despite all that, the real life situations might be more complicated and contain much less omissions than the hypothetical proposed above. It, therefore, remains to be seen whether any IT company finding itself in a difficult situation would want to bring a treaty claim against Russia, Ukraine, or else. It is, however, clear that the era of internet technologies and social platforms can potentially bring new challenges to old definitions of investment contained in the international investment treaties.