Exporting Capital, Importing Law*

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Abstract

How does capital mobility impact the relationship between plutocrats and the state? The interaction of offshore finance and international law changes the strategy and sites of political contestation. By routing their investments through offshore shell companies, plutocrats can become *de jure* foreign investors in their home markets. We find that plutocrats use the most tax efficient methods to route their investments but those tax havens frequently give them access to international investment treaties; these treaties allow plutocrats to file binding investor-state dispute settlement (ISDS) against their own governments. We examine the full wealth-chain for over 10,000 "roundtripped" investments and data on the beneficial ownership of entities involved in ISDS. We document that extraterritorial arbitrations make up 8% of ISDS cases yet account for 41% of the total damages claimed. The paper contributes to debates on the effects of globalization on political development and the emerging research agenda on the IPE of Oligarchy.

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1 Introduction

Offshore finance was key to Mikhail Khodorkovsky's success. He set up shell companies in places like the British Virgin Islands and the Isle of Man to ensure Yukos, his oil company, minimized its tax burden and accumulated hard currency. In 1999, amid a heated battle with minority shareholder and fellow billionaire, Kenneth Dart, Khodorkovsky hatched up a plan that would make even the most audacious accountants blush—he planned to invert the entire ownership structure of Yukos to turn it into a fully foreign company (Hoffman, 2011). He would leave Dart and Yukos's other creditors with an empty shell of a company. With that move, the second largest oil company in Russia would become a *de jure* foreign corporate. Khodorkovsky largely succeeded. But when he lost his political battle with Vladimir Putin, Yukos's complicated ownership structure provided an additional benefit: access to an international agreement designed to provide extra protections for foreign investors. Since Khodorkovsky used offshore shell companies to make Yukos appear to be a foreign company, his fellow Russian shareholders were able to sue the Russian state in international arbitration courts that were designed for foreign investors—they claimed nearly $100 billion dollars in damages.

We make two analytic wagers. First, when plutocrats protect their wealth using offshore vehicles, it changes the sites of conventionally domestic political contestation. When clashes occur between the state and plutocrats in emerging markets we still regularly see governments expropriate their rivals. Given the weak institutional environments, business owners that lose the conflict are often left with limited formal recourse as domestic courts will rarely be in a position to override the dictates of the government. But if a plutocrat has structured their business empire through offshore companies, and more specifically using entities in jurisdictions that have an investment treaty with their home state, the losers from the political clash can argue they are foreign investors and then attempt to use international arbitration venues to compensate for their losses. They can use the neutral venues designed for multinational corporations in order to extend the political conflict through international means, as Khodorkovsky's associates did against their home government, Russia. We label this phenomenon an "extraterritorial arbitration". We are the first to systematically examine its rise as a political insurance mechanism.

Second, plutocrats may actively plan to ensure they can initiate an extraterritorial arbitration. When making an investment, individuals can choose how to route the transaction. The most straightforward way would be to move money directly from their home location to where they intend to produce or sell goods. But plutocrats frequently route even their domestic investments through offshore shell or holding companies, sending the money abroad before sending it straight back to their home jurisdiction. This changes the *de jure* nature of their investments as it will now show up in national accounts as foreign investment. Plutocrats can even change nationality well after the initial investment decision by selling ownership rights over their companies to their own offshore vehicles, as Khodorkovsky did. Legally turning into a foreign investor makes it far more arduous to wholesale seize a plutocrat's assets as they can arbitrage the greater protections that are frequently afforded to foreign actors. Individuals may then choose their tax havens not only based on the potential for economic returns, but also as a mechanism to ensure access to investment treaties that can be used against their home state.

We assess our claims across different levels of analysis. We begin by using original data on investor-state dispute settlements (ISDS) that identifies the beneficial ownership of corporations involved in international arbitrations. We highlight that these cases involving "round tripped" entities, while similar to conventional foreign vs. host government disputes in terms of industry and rules, are far more likely to be initiated through a company located in a tax haven, and, given the domestic political stakes, are less likely to settle. Next, we examine whether plutocrats structure their wealth to ensure access to ISDS. To do so, we build, to our knowledge, the most comprehensive dataset on roundtripped investments, examining over 10,000 entities from 41 European home states and 65 offshore jurisdictions using information on the entire wealth chain. Contra our initial expectations, we find that plutocrats primarily focus on minimizing their tax burden. The analysis is consistent with the notion that ISDS becomes an *ex-post* insurance mechanism. Rather than acting as a deterrent to political conflict between domestic elites, the regime provides a mechanism for plutocrats to fight back.

The paper builds on a number of Political Economy debates. Most directly, it helps identify the distributional consequences of the international investment regime (Wellhausen, 2016). Research on Bilateral Investment Treaties (BITs) has generally focused on whether or not these treaties live up to their aims by increasing foreign direct investment. Here, we shift the analysis toward understanding how the regime does not just impact economic flows, but also changes political flows. The growth of extraterritorial arbitrations places BITs in the same theoretical space as many other international institutions, like financial soft law and the International Monetary Fund (Farrell and Newman, 2018; Vreeland, 2003), where strategic, *de facto* domestic actors can leverage international tools for their own domestic ends.

Moreover, our findings call for further work bridging the gaps between international regimes. While regime complexity has become a focal agenda for IR scholars, issue arenas are frequently theorized and assessed in isolation (Abbott et al., 2016; Clark, 2021). Far less attention is paid to how actions intended to benefit actors in one regime can spillover, and even change the purpose, of an alternate regime. The way oligarchs are able to exploit rules in the tax arena to access the resources of another regime indicates that regimes are more dynamic than our theories expect (Thrall, 2021). Moreover, it suggests that when a regime relies on nationality as a key access criteria, it is likely to create new opportunities to outsource domestic conflicts.

Finally, the paper illustrates one way that the rules of the global economy bolster the power of plutocrats (Cooley and Sharman, 2017). While the institutionalization of international trade and finance has no doubt improved living standards, the gains have not been distributed equally. A wave of recent scholarship across subfields examines the apparent backlash to globalization's imbalanced outcomes. But to comprehensively understand the populist wave we need to fully theorize the winners from the status quo. Emerging market oligarchs is a class of winners that are rarely discussed in such scholarship, but we hope that the paper continues building momentum around a research agenda focused on the IPE of Oligarchy (Cooley and Heathershaw, 2017).

2 The Political Economy of Extraterritorial Arbitration

We start from the premise that two systemic features distinguish emerging markets from their developed peers. First, ownership in large firms tends to be substantially more concentrated in emerging markets where single individuals or families have controlling ownership stakes in the majority of a country's most lucrative companies (Freund, 2016). This is a broadly agreed upon stylized fact in political economy scholarship and has important political implications. Rather than a purely profit motivated firm being the key player in the economy, individuals with large amounts of wealth are frequently part of the economic and political elite and directly impact both nominally independent systems. The second distinction is the relative weakness of the institutional environment. Emerging markets, beyond simple definitions of GDP per capita, usually have fewer checks and balances, weaker property rights, and weaker courts. While billionaires, and personalistic CEOs, are becoming a central feature of politics in developed economies, stronger institutions and competitive elections are regarded as the elements that prevent wholesale capture by economic elites. By contrast, in emerging markets, billionaires are in a position to more effectively wield their wealth to attain political power, creating a class of oligarchs or plutocrats (Winters, 2011).

But the weaker institutions cut both ways, as they imply that the state is often in a position to expropriate, directly through seizure or indirectly through cumbersome taxation or regulation, the wealth of elite business people (Haber and Razo, 2003; North et al., 2013; Arel-Bundock, 2017). How plutocrats resolve this threat is one of the main research agendas for comparative political economy scholars who have found plutocrats, and their firms, can leverage a variety of non-market strategies. We frequently see plutocrats try to directly align themselves with state actors, substituting formal institutional protections with informal political connections (Haber and Razo, 2003). In major economic powers like China and Russia, we even see plutocrats run for office themselves, with substantial economic returns for the firms they control (Szakonyi, 2020). The bulk of scholarship has focused on the domestic tools that plutocrats use to protect their property but recent work has turned to the transnational tools at a plutocrat's disposal. Oligarchs can try to team up with with foreign firms to gain additional political allies, and they can list their companies abroad to garner more attention and alter corporate governance rules (Betz and Pond, 2019; Markus, 2016; Logvinenko, 2019).

2.1 Offshore Finance and Property Protection

The move toward studying the transnational sources of property protection is an important step forward but has generally developed independent of debates on the role of offshore finance in global politics.[1] This is unsurprising given that much of comparative and international political economy scholarship on offshore finance is fundamentally focused on economic arbitrage. The biggest winners from offshore havens are generally regarded as multinational corporations (MNCs) who, with the aid of the major accounting firms, are able to efficiently route their investments and claim their profits in low tax jurisdictions like Ireland, Luxembourg, and the Cayman Islands (Arel-Bundock, 2017; Hearson, 2018). But a variety of recent work documents that emerging markets tend to see the most amount of money moved to offshore sites. Countries like Russia, Venezuela, and Saudi Arabia have seen the largest proportion of domestic wealth moved into tax havens despite many emerging markets already operating with low corporate taxes (Tørsløv, Wier and Zucman, 2022; Zucman, 2014).[2]

Part of this pattern can certainly be explained by economic arbitrage. Consider the choice set of an Indian oligarch when deciding to build a new factory at home. They could simply pay money to domestic construction companies and materials suppliers through their onshore balance sheets. Or they could move the money to Mauritius that has a highly favorable tax treaty with their home government, and then move the money back to India. Because of how it is routed offshore the money will show up in India as foreign investment and lock in a lower tax rate for the construction project. This "roundtripping" is rampant across emerging markets and helps explain why Mauritius is historically one of the top sources of FDI for India and why Cyprus continues to take a higher spot for investments into Russia (Aykut, Sanghi and Kosmidou, 2017; Ledyaeva, Karhunen and Whalley, 2013). In line with the work of academics like Katarina Pistor (2019) and journalists like Oliver Bullough (2018), roundtripping illustrates that the consequences of capital are a result of how it is legally constructed. By changing its *de jure* location, plutocrats can reap substantial economic returns even when only *de facto* investing in their home market. Such actions have been shown to heavily bias many of our core macroeconomic indicators and thereby distort our understanding of global politics. More generally, it indicates that plutocrats, much like multinational corporations, can create a portfolio of nationalities by choosing how to route their investments and where they place their wealth (Cooley and Sharman, 2017).

But a number of researchers have called attention to the political gains from placing money abroad, and in particular how it facilitates institutional arbitrage (Sharman, 2012). By moving money into tax havens, investments become *de jure* governed by the laws of the foreign jurisdiction. Plutocrats may gain access to the domestic courts in these jurisdictions and if a rival, be it a fellow oligarch or a state, wants to seize one's wealth that is placed abroad, they would need to go through the domestic legal system of the tax haven. Not only does that add greater transaction costs, and generally ensure more liberal treatment compared to the home legal system, the opacity of these jurisdictions often mean that rivals may not even know the money has been placed there. It is often "hidden" wealth. Most importantly, for our purposes, systematic quantitative work has confirmed the insights of

[1] For a detailed historical account on the development of offshore finance see Palan (2006).

[2] On the international rules dealing with money-laundering and financial flows from corrupt behavior see Sharman (2011, 2017). For experimental evidence on the effectiveness of international approaches to money laundering see Findley, Nielson and Sharman (2014).

a number of early offshore finance scholars. Bayer et al. (2020) show that more offshore companies are registered in tax havens when the threat of expropriation rises in an emerging market. Using a variety of micro data, Earle et al. (2019) find that Ukrainian oligarchs with the weakest political connections are most likely to obfuscate their wealth through tax havens. As one lawyer told us, "[Offshore structures] are an instrument of survival."[3]

We link these two schools of thought on offshore finance to help us better understand how plutocrats can protect their wealth in weakly institutionalized settings. Tax havens all generally offer zero tax rates and strong institutions, but they are not created equally. They vary in terms of their international engagement, and that has important consequences for the *international* property protections they can provide. More specifically, they have different degrees of integration into the international investment regime, which should condition the strategic toolkit of plutocrats.

2.2 The Investment Regime and the Internationalization of Intra-Plutocratic Conflict

Since its inception in the late 1950s, the modern international investment regime has grown to be comprised of 3,000 bilateral investment treaties (BITs). When two states sign a BIT, they make a commitment to apply a certain set of protections to each other's foreign investors; for example, they promise not to expropriate assets without compensation or pass domestic regulations that discriminate against their partner state's investors. Further, if a BIT-protected foreign investor believes that the host government has violated one of these protections, they are able to sue for damages in international arbitration courts through a process called investor-state dispute settlement (ISDS). ISDS awards are binding; if governments fail to pay, investors may lawfully seize state-owned assets to recoup damages.[4]

By giving foreign investors the ability to sue their host governments, the general aim of these treaties was to spur foreign direct investment in emerging markets (Wellhausen, 2019; Simmons, 2014). However, existing evidence suggests that BITs have failed to meaningfully affect firms' investment decisions, and the regime has come under increasing scrutiny from mainstream political parties and civil society groups (Brada, Drabek and Iwasaki, 2020). Most cases in the past decade have not dealt with outright expropriation claims that the regime was designed to deter, but instead focus on indirect situations where governments attempt to pass new (often democratically supported) regulations (Pelc, 2017). Arbitration has turned from an economic tool to a political tool for many MNCs, as they file cases against one state in order to deter other states from adopting similar rules ("regulatory chill") (Moehlecke, 2019).

[3]Author interview with London-based lawyer February 2018

[4]For example, Scottish energy firm Cairn Energy is currently attempting to seize airplanes owned by Indian state-owned enterprise Air India following the Indian government's failure to pay a $1.2B USD ISDS award. See Benjamin Parkin, George Parker, and Nathalie Thomas, "Cairn Energy sues Air India over $1.2bn arbitration award", *Financial Times*, 16 May 2021.

Under the regime states have limited recourse against infringements by multinational corporations, and seminal work on the regime suggests that states did not fully understand what they were signing up for (Poulsen, 2015, 2010). The playing field is made even more asymmetric because of offshore finance and tax planning. As scholars like Gray (2020) and Thrall (2021) have documented, MNCs exploit their multi-jurisdictional structure to treaty shop—they can use their subsidiaries to file cases against a host government even if their main home government does not have an investment treaty with its host state. For example, when Czech businessman Vladimir Beno was prosecuted by the Czech government on tax evasion charges, he sold some of his assets to an Israel-headquartered firm called Phoenix Action and filed a dispute against the Czech Republic under the Israel-Czech Republic BIT (Gray, 2020, 20). Firms who adopted multi-jurisdictional structures primarily in order to lower their tax burdens can also benefit from third-party investment treaties; Thrall (2021) gives the example of an American firm, Columbia Capital LLC, that routed its Indian assets through a Mauritian subsidiary (CC/Devas). Adopting this structure allowed the parent firm to lower its withholding tax rate from 20% to 10%, and—when a dispute arose with the Indian government—Columbia Capital used its Mauritian subsidiary to file an ISDS case against India.

Such "shopping" is possible because of 2 interacting features. The key governing principal of the investment regime is discrete nationality (van Os and Knottnerus, 2012); if you are registered in a jurisdiction, you gain access to its investment treaty provisions independent of how the rest of your business may be structured. Second, MNCs by definition have a portfolio of nationalities, which are already set up for normal business or tax purposes, which they can then choose to file cases with. As we've discussed, emerging market plutocrats also frequently create such portfolios and they even take advantage of offshore structures for de facto domestic investments. Our contention is that plutocrats from emerging markets, and their legal teams, recognize the potential for international institutional arbitrage that MNCs exercise when they treaty shop. Routing investments through offshore vehicles can give them access to international treaty provisions that their home states lack. More importantly, roundtripping investments puts plutocrats in a position to challenge their home state. Because of the investment regime's nationality principal, disputes that are *de facto* domestic can then be adjudicated via international venues.

The gains from choosing an offshore haven that has an investment treaty with a plutocrat's home government go above and beyond those from simply placing money offshore. A plutocrat's wealth would likely still be obfuscated regardless of the location choice, and they are going to have access to stronger domestic institutions. But when a conflict arises with the home state—the primary threat to most plutocrats' wealth—many offshore sites would leave them with limited recourse. A case filed against a sovereign state in places like the British Virgin Islands or Singapore courts would almost certainly fail on jurisdictional grounds because of sovereign immunity. But by claiming to (legally) be a foreign actor, and using the provisions contained in 95% of modern BITs,[5] plutocrats can sidestep those issues through international arbitration venues.

[5] Source: author calculations based on data from the IIA Mapping Project.

We label this phenomenon, when a plutocrat turns a conflict with their home state into an international arbitration via nationality portfolio, an extraterritorial arbitration (or EA). These situations are unlikely to occur for common disputes between the state and the wealthy such as a fight over taxation rates since extraterritorial arbitration will not come without costs. By initiating a case, plutocrats will be guaranteeing they spend millions on lawyers and potentially tying themselves into years of arbitration. Moreover, filing a case against the state could alert other plutocrats who may not have offshored their wealth to follow in a filer's stride, thereby reducing the power the state may have over economic elites. This could increase the risk of retaliation from the state.

Instead, we expect extraterritorial arbitration can potentially serve a political insurance mechanism. In line with our assumptions, and a variety of work in comparative politics, the power of plutocrats coupled with the weak institutionalized environment creates a commitment problems between the state and the economic elite. The lack of institutional safeguards can lead to political clashes, the end result of which is frequently expropriation by the state. While historically many of these intra-elite battles would end at this stage, the combination of offshore finance and the investment regime may extend the conflict. Now plutocrats have the option to outsource political clashes to the international stage via extraterritorial arbitrations. The state is likely to be aware of this option, but since these legal battles can take years and have no guarantee of turning out in a claimant's favor, the international protections are unlikely to serve as a sufficient deterrent. Since the physical assets are still in the state's territory, the state still has the upper hand - they can seize and take advantage for years before any legal challenge ends.

In sum, we expect a perversion of the international property protection regime. MNCs have led the charge, taking advantage of their multi-jurisdictional structures to treaty shop. But the necessary nationality portfolios are also a common part of the emerging market plutocrat's toolkit. They recognize that moving assets abroad can give them international institutional protections. Round tripping investments, which are generally viewed as a source of economic arbitrage, creates political gains by allowing plutocrats to protect themselves against their own sovereigns through treaties designed for foreign investors. When conflicts emerge between plutocrats and their home state, we then see political clashes extend beyond their borders into the tribunals and arbitration venues of the international investment regime.

2.3 Observable Implications

The rest of the paper is dedicated to testing two sets of observable implications derived from our theory. The first set concerns oligarchs' decisions about where to store their offshore wealth: why select one tax haven over another? We expect that the international investment regime matters; havens that have BITs with the oligarchs' home state are desirable, as investments routed through them gain additional protections under international law. We therefore expect that oligarchs will be more likely to locate their offshore holdings in havens that have an active investment treaty with their home state.

The second set of observable implications concerns oligarchs' use of the ISDS mechanism to sue their own governments in international courts, engaging in what we call extraterritorial arbitration. While anecdotal evidence confirms that extraterritorial arbitration occurs, ours is the first study to identify and analyze all such cases. We expect instances of extraterritorial arbitration to differ systematically from standard ISDS cases involving *de facto* foreign investors. While we compare the two sets of cases on a variety of metrics, our theory suggests that: first, extraterritorial arbitrations should be more likely to be filed by firms incorporated in tax havens. While some standard ISDS cases may see MNCs treaty shop, seeking additional property rights protection through offshore sites should be less likely compared to plutocrats who incorporate the value of both tax and investment regimes when structuring their wealth.

Second, since EA cases are often continuations of domestic conflicts rather than attempts to dispassionately recoup losses, we expect that they should be less likely to end in negotiated settlements than other ISDS cases. In general, governments should want to avoid ISDS because arbitrating can cost substantial sums of money and drag out for years while also deterring future investments into the country. In EA, the incentives are broadly reversed. Plutocrats may want to quickly settle, since they may struggle to win on jurisdictional or enforcement grounds. Yet they may want to extend the the conflict to shine more of a spotlight on the government's actions and inflict further economic damage on the government as these cases could deter foreign investment. Regardless, for the government the incentives are clear. If it settles, it could be directly enriching a political rival who will then be armed with new funds to mount a challenge. If the rival wins it could also further incentivize other potential defectors to take up arms as they will be assured in their ability to still be compensated via international venues even if they lose the domestic political game.

3 Extraterritorial Arbitration

The international investment regime was designed to promote economic development by protecting the property rights of Multinational Corporations in emerging markets. Outsourcing authority over economic disputes to international arbitration venues would dissuade host governments from expropriation. By giving *de jure* ownership of their domestic assets to their offshore shell companies, oligarchs can become "foreign" investors in their own home states; as foreign investors, they gain the ability to take their own government to court under the investor-state dispute settlement mechanism. The ability to file ISDS against their own governments (extraterritorial arbitration, or EA) provides oligarchs the ability to seek compensation for government mistreatment in international courts that are likely more unbiased than their domestic counterparts. The most famous example of the phenomenon comes from the so-called "Yukos Affair."

In 2003, Mikhail Khodorkovsky was the richest man in Russia with a $16 billion war chest. Arguably the biggest winner of the infamous "loans for shares" privatization process, he was the largest shareholder of the oil giant Yukos. That wealth, and how he was using it, turned into a source of conflict between the company and the Russian state. Despite repeated attempts by the Putin regime to bring the oligarchs in line, Khodorkovsky continued to challenge the changing nature of business-government relations, funding political parties across the aisle and building up his own independent power base (Sakwa, 2014; Sixsmith, 2010). With major elections on the horizon, Yukos found itself under investigation for tax avoidance. Khodorkovsky was forced behind bars, and Yukos was eventually found guilty of illegally exploiting domestic onshore shell companies (Stephan, 2013). That would come with a $28 billion bill. Although the major shareholders of the company repeatedly tried to settle the claim, the pursuit by the Russian state was incessant (Sixsmith, 2010). The general journalistic and academic consensus is that Khodorkovsky and his cadre were never going to be able to keep the company (Judah, 2014; Sixsmith, 2010; Sakwa, 2014); this was a political battle to remove the revenue streams of the Kremlin's biggest challenger. It is broadly considered the fundamental turning point in Putin's control over the plutocracy.

While Khodorkovsky was imprisoned in Russia for a decade, most of his inner circle was able to leave Russia with some of their wealth intact. Although they were nominally in trouble for the exploitation of domestic tax havens, they had long been using offshore structures for both their business and personal protections. As per a number of lawyers who have worked on Russian legal disputes, the "magnificent seven" shareholders that controlled Yukos had planned for such a political fallout by structuring parts of their business through offshore vehicles.[6] And it appears they chose these locations strategically as it eventually led to the most notorious ISDS case, an extraterritorial arbitration between the main Yukos shareholders and Russia, which was filed under the Energy Charter Treaty using their holding companies registered in British territories. The end result was a a $50 billion victory in favor of Yukos in 2014 after a tribunal spent roughly 5 years deciding the outcome (Nougayrede, 2015).[7]

The case is still the largest monetary victory given out under the investment regime, making it well-known amongst participants and observers. The political stakes and sums of money are easy to write off as an aberration, but our contention is that it largely symbolizes a broader pattern of extraterritorial arbitrations that turns ISDS into an intra-plutocrat battleground. We find that 58 of the 723 ISDS cases filed between 1987 and 2015 are extraterritorial arbitrations. This means that, in 8% of all known cases, the nominally foreign investor is actually a domestic plutocrat who has routed ownership of their investments through a foreign company. Further, due in large part to the behemoth Yukos cases,[8] extraterritorial arbitrations compose 41% of the total damages claimed despite making up only 8% of cases.[9]

These figures are based on recently collected data from Thrall (2021) that identifies and

[6] Author Interviews with London-based Lawyers, February 2018.

[7] 2 years later a Dutch district court ruled that the tribunal should not have taken up the case because of conflicts with Russian constitutional law. That ruling was in turn reversed 4 years later by a Dutch appeals court.

[8] In *Hulley Enterprises v. Russia*, the claimants sought $91B USD in damages—the largest sum ever sought in an ISDS case.

[9] Even without the Yukos cases, extraterritorial arbitrations still account for 24% of all damages claimed in ISDS. Note that damages claimed do not reflect damages awarded.

Table 1: **Top 10 nationalities of firms filing ISDS: extraterritorial arbitration vs. all others**

Extraterritorial	Other
Cyprus* (15)	**United States** (153)
Netherlands (14)	Netherlands (80)
United States (7)	Germany (66)
Luxembourg* (6)	Spain (56)
Spain (4)	Canada (50)
United Kingdom (4)	France (48)
Barbados* (3)	**United Kingdom** (48)
Poland (3)	Italy (37)
Italy (2)	Luxembourg* (36)
Panama* (2)	Ukraine (26)

Bolded states are havens used by Mossack Fonseca. Asterisk indicates that the state appears on one of the two lists of tax havens contained in Table **??**.

examines all cases of extraterritorial arbitration between 1987 and 2015. For each firm that was listed as a claimant in every ISDS case filed through 2015, Thrall searched business databases, corporate registries, case documents, specialized news outlets, and other sources in order to identify whether the firm was owned by another firm or individual; if so, Thrall coded the nationality of the ultimate owner. For example, if a case was filed by a Dutch firm, but the Dutch firm was in turn a subsidiary of a US multinational, the ultimate owner would be coded as American. Using this data, we identify extraterritorial arbitrations as cases in which the nationality of the ultimate owner is the same as the nationality of the host government.[10]

As noted previously, we expect that extraterritorial arbitrations are qualitatively different from standard ISDS cases in which a (de facto) foreign investor files a dispute against a host government. First, we would expect that the companies that oligarchs use to file extraterritorial arbitration should be incorporated in tax havens at a substantially higher rate than companies involved in other ISDS cases (because EA is function of roundtripping). This expectation appears to be borne out in Table 1, which ranks the top 10 claimant nationalities for extraterritorial vs. non-extraterritorial cases. While claimants in non-EA cases tend to come from the world's largest economies, as we might expect, firms that file EA cases tend to be incorporated in low-tax and high-secrecy jurisdictions such as Cyprus, Luxembourg, Barbados, and Panama. This provides further evidence that oligarchs use their offshore shell companies both to avoid taxation and to gain access to investment treaty protection.

It is also instructive to compare EA and non-EA cases on the basis of which governments are most frequently the target of investors' claims. Table 2 shows that Argentina and Venezuela are among the most common recipients of non-EA claims, due largely in part

[10]These cases are a subset of what Thrall (2021) calls proxy arbitration, in which the ultimate owner's nationality is different from that of the firm that is filing the case.

Table 2: **Top 10 recipients of ISDS claims: extraterritorial arbitration vs. all others**

Extraterritorial	Other
Russia (7)	Argentina (58)
Czechia (6)	Venezuela (35)
Egypt (6)	Spain (28)
Turkey (6)	Czechia (27)
Spain (5)	Canada (25)
Venezuela (4)	Mexico (23)
Kazakhstan (3)	Poland (23)
Ukraine (3)	Ecuador (21)
Panama (2)	Egypt (20)
Albania (1)	India (16)

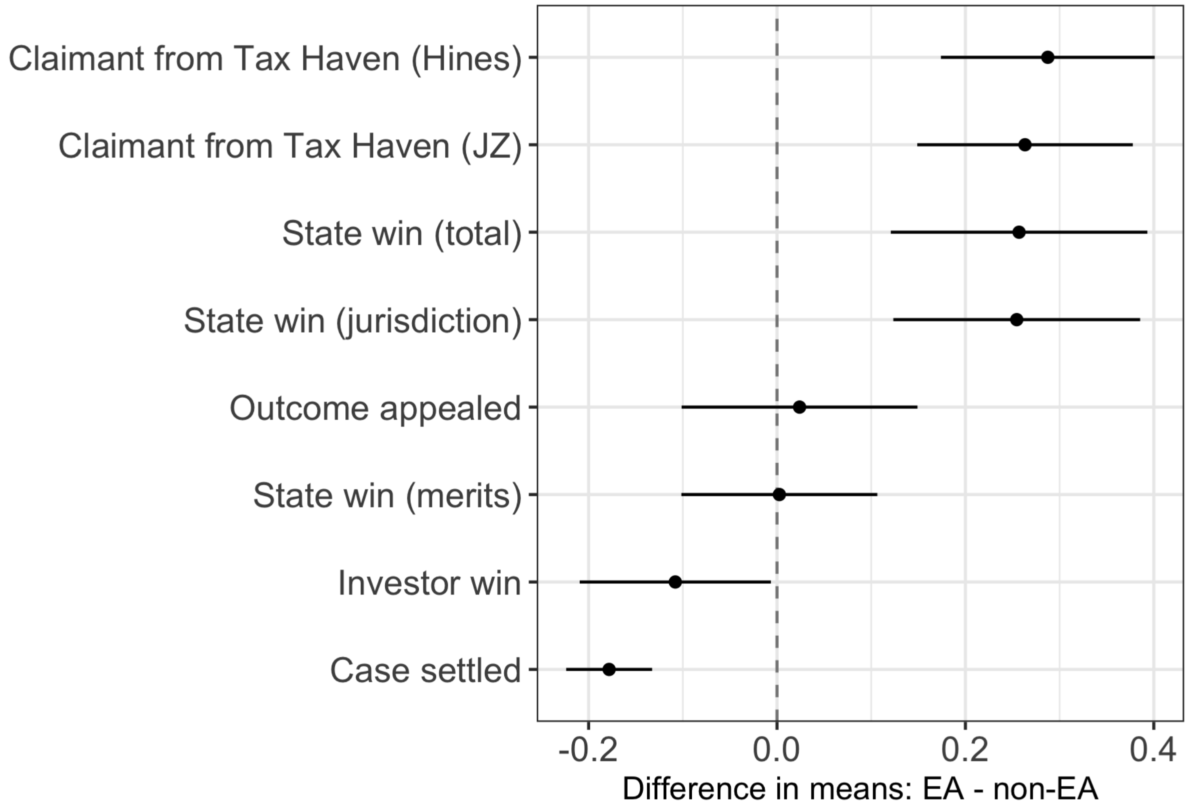
to the frequency with which they expropriate foreign investors, default on sovereign debt, and impose capital controls. On the other hand, EA cases—in which a state is sued by its own nationals—are dominated by post-communist states (Russia, Czechia, Kazakhstan, Ukraine, Albania) and other countries with relatively powerful oligarchies such as Egypt and Turkey. While governments like Saudi Arabia can be characterized as having control over their plutocrats, and those in places in like Indonesia are generally considered captured by oligarchs, states that face EA claims are jurisdictions where domestic politics are characterized by frequent power struggles among competing plutocrats. These competitions can be internationalized via extraterritorial arbitration.

In addition to the Yukos Affair, Russia was the respondent in a claim from Sergei Pugachev who was frequently referred to as the "Kremlin's Banker." After a public fallout with the regime, he claimed that his bank was expropriated and thereby sought $12 billion in damages (*Pugachev v. Russia*) (Belton, 2020). But as Table 2 indicates, this is not a solely Russian phenomenon. Mukhtar Ablyazov was the primary challenger to Kazakhstan's multi-decade ruler Nursultan Nazarbayev. After being imprisoned in the early 2000s, he struck a bargain with the state, leaving the country to re-build his wealth. He returned a handful of years later as the chairman of BTA Bank. The latter was eventually nationalized in the midst of the great financial crisis, which Ablyazov claims was a veneer for the regime to dispose of its clearest threat (Cooley and Heathershaw, 2017; Burgis, 2020). Ablyazov used thousands of offshore vehicles to protect his wealth (Nougayrede, 2017), and settled on using a shell company in the Netherlands to make an ISDS claim worth $1.5 billion (*KT Asia v. Kazakhstan*).

Similarly, after clashing with Erdogan in the early years of his tenure, the Turkish Uzan family may have inspired Khodorkovsky. They used the Energy Charter Treaty to strike back against their home government, seeking 3.5 billion for the cancellation of electricity concessions and the seizure of their conglomerate's assets (*Uzan v. Turkey*).[11] These addi-

[11] For details, see the Award on Respondent's Preliminary Objection:

Figure 1: **Difference in means tests: EA vs. Non-EA ISDS cases**



tional examples highlight how political clashes become extended through ISDS. They further illustrate that EA is not a silver bullet to an oligarch's financial woes—Pugachev and the Uzans lost out on jurisdictional grounds while Ablyazov's case was resolved in favor of the state. Still, extraterritorial arbitration offers oligarchs the ability to impose large litigation costs

To more systematically assess the implications of our theory, we conduct a series of basic difference-in-means tests comparing extraterritorial arbitrations to all other ISDS cases on a range of factors. The results of these tests are plotted in Figure 1. First, as predicted, EA cases are much less likely to end in a negotiated settlement when compared to non-EA cases. Not only will governments be less inclined to pay a settlement to their political rivals, as they could use the money to continue posing a threat, but oligarchs themselves may want to prolong the litigation in order to maximize the costs inflicted on the government. Oligarchs can punish antagonistic governments by filing a number of lawsuits that cost the state significant time, money and legal resources, even if their probability of winning the case is low.[12] The longer the cases run, the longer they could garner attention from international

https://www.italaw.com/sites/default/files/case-documents/italaw8642.pdf.

[12] In response to Russia's expropriation of Yukos Oil Company, the leader of Yukos' largest shareholder group vowed to pursue a "lifetime of litigation" against the government. See "A lifetime of litigation—the fall of Yukos", *Law.com*, 09 July 2010. This is also related to work by Moehlecke (2019) and Pelc (2017) on

audiences, putting pressure on governments to retrench the efforts they use to suppress the economically powerful.

Second, in line with our earlier results, the companies that are used to file EA cases are substantially more likely to be incorporated in a tax haven than companies that file non-EA cases. This provides evidence that oligarchs use their offshore shell companies to gain both tax benefits and BIT protection. EA cases are more likely to end in a state victory than non-EA cases, but this difference is driven almost completely by the fact that EA cases are much more likely to be thrown out due to lack of jurisdiction. Finally, conditional on the case being ruled on the merits, EA claimants are no more likely to appeal the verdict than non-EA claimants.[13]

A regime designed to deter the expropriation of foreign investment and thereby catalyze economic development has been disrupted by offshore finance. Plutocrats can and do roundtrip their investments that allows them to de jure act as foreign claimants to sue their own sovereigns. These cases are not aberrations, but they are distinct from the conventional MNC-host state disputes. Their political stakes lead to lower rates of settlement as they can serve as a mechanism for oligarchs to fight back after political losses at home. The next section examines whether plutocrats actively structure their wealth accounting for the potential of BIT protection or whether the interaction of the tax and investment regimes leads ISDS to turn into a political insurance mechanism.

4 Evidence from Round-tripped Investments

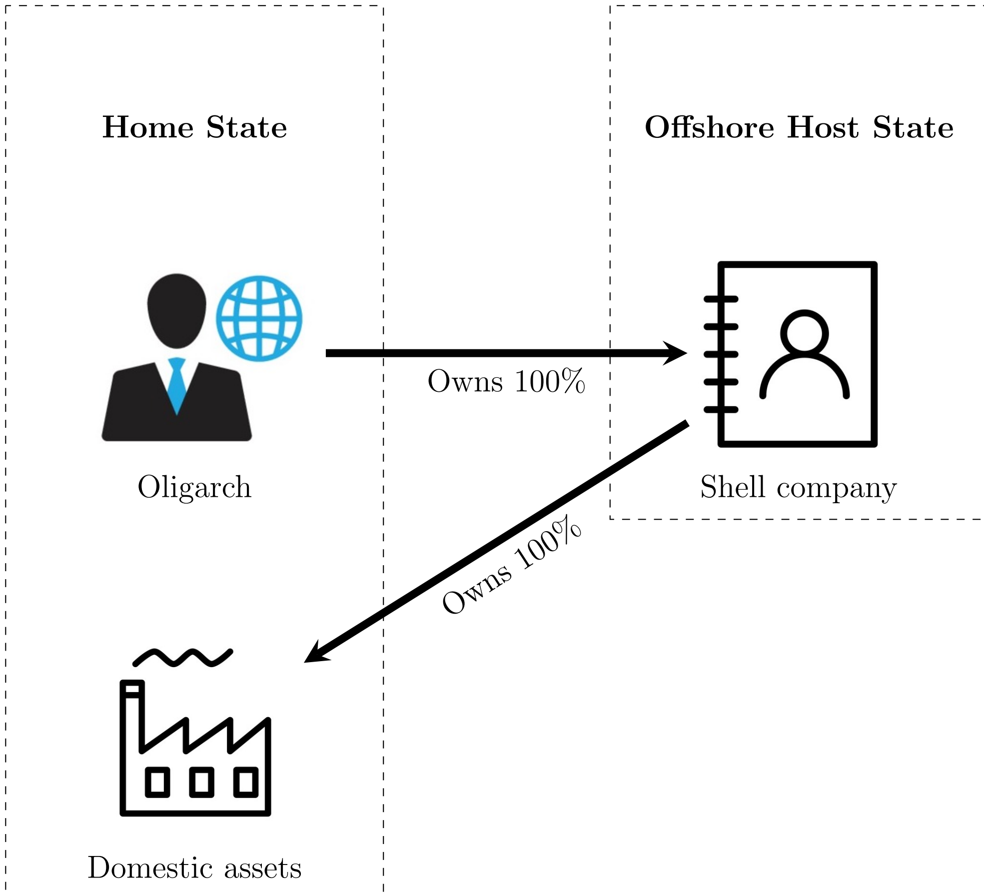
Our primary analytical goal is to determine why oligarchs choose to place their capital in certain foreign jurisdictions as opposed to others; we expect that states that have a BIT with the oligarch's home state are more likely to be selected. However, an oligarch who simply holds assets in a BIT partner state does not gain the ability to file an ISDS case against his own home state; rather, the invest*ment* must be located in the home state, and the invest*or* must be located in the BIT partner state. Therefore, our theory should apply to cases in which oligarchs own offshore companies that are themselves used to hold ownership of assets in the oligarchs' home states: this practice is known as "round-tripping."

Figure 2 illustrates how round-tripped investments work. First, an oligarch creates a shell company in another state (often a tax haven, or at least a tax-favorable jurisdiction). Characteristically, these firms tend to consist of little more than a bank account, a mailbox, and a stack of legal documents; they are merely legal entities through which the oligarch can act. Next, the shell company is given ownership of the oligarch's domestic assets: companies, real estate, and so on. This structure generates two primary results: first, the oligarch's *de*

regulatory chill in ISDS.

[13] We note that this null result may be driven by the fact that oligarchs often prefer to file new cases, using different offshore companies, rather than appeal old rulings. The lack of binding precedent in investment arbitration means that different tribunals can reach completely different conclusions when ruling the same exact case; for the example of *Lauder v. Czech Republic* and *CME v. Czech Republic*, see Kerner (2009).

Figure 2: **Anatomy of a round-tripped investment.**



facto domestic assets become *de jure* foreign investments, meaning that they are covered by BIT protections (if a BIT exists between the home and offshore states). Second, while the oligarch himself does not become a *de jure* foreign investor in his own home state, he does become a *de facto* foreign investor through his complete control of the offshore shell company. This means that, in the presence of a BIT, the oligarch could file an ISDS claim against his home government through the "corporate veil" of his offshore shell company.

Round-tripping is an extremely common practice: Kerner (2018) notes that Spanish firms are the second-largest (ultimate) source of Spain's inward FDI flows, and that half of all Russian FDI consists of round-tripped investments. Round-tripping offers oligarchs other benefits besides BIT access, such as access to the bilateral tax treaty network and to low tax jurisdictions (Thrall, 2021), the ability to skirt regulations regarding domestic ownership (Aykut, Sanghi and Kosmidou, 2017), and access to more favorable financing conditions (Coppola et al., 2021), among others. However, we also know that the oligarchs who did ultimately file ISDS cases against their own governments were (by definition) engaging in round-tripping. It is therefore plausible that these investors purposefully sought out offshore jurisdictions that offered BIT access (in addition to other benefits), and that this is indeed a common strategy among all oligarchs who engage in round-tripping. We now describe the data and econometric strategy with which we will test this proposition.

4.1 Data: European Round-Tripped Investments

Identifying round-tripped investments is inherently challenging, as it is necessary both to link a domestic oligarch or firm to an offshore company *and* to link the offshore company back to domestic assets. To build a sample of round-tripped assets, we draw on Bureau van Dijk (BvD)'s Amadeus dataset. The Amadeus dataset, which contains financial and ownership information about millions of European public and private firms, is useful in that it also contains information about the firms' intermediate and ultimate owners.[14] We identify round-tripped investments by filtering this data to include all subsidiaries (assets) with the same nationality as their ultimate owner (the oligarch) but with a different nationality from their intermediate owner (the offshore shell company). This exercise produces a sample of roughly 10,300 round-tripped investments made between the years of 1980-2019. To our knowledge, we are the first to use the Amadeus data to identify and study round-tripped investments in a rigorous way.

What do these investments–and their investors—look like? We find that the majority (60.4%) of the round-tripped assets are ultimately owned by an individual (e.g., MR. RESSLER WOLFGANG) rather than a corporate entity.[15] Consistent with the assumption that most of the intermediate owners are offshore shell companies, rather than (for example) regional subsidiaries with legitimate business operations, we find that 81% of the intermediate firms have five or fewer employees; 64% have no listed employees at all. The median annual revenue among the likely shell companies is approximately $365,000, though only 23% reported their revenue.

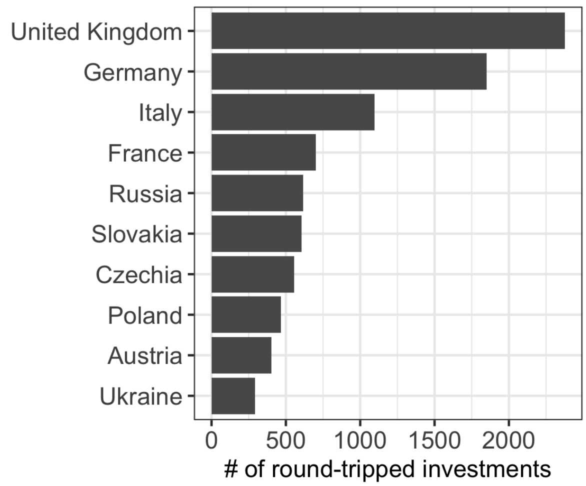
Figure 3 contains information on the top sources and offshore destinations of round-tripped investments. First, Panel (a) plots the states who are home to the largest number of round-tripped investments. Note that, while the top five states are Europe's largest economies, several of the other top home states (such as Slovakia, Czechia, and Ukraine) punch above their economic weight. When GDP is adjusted for in Panel (b), it becomes even clearer that smaller, Eastern European economies with developed oligarchies are more frequently home to round-trip investors. Finally, Panel (c) plots the top offshore states through which investors route their round-tripped investments. Well-known "conduit" hubs such as Luxembourg, Cyprus, and the Netherlands occupy the top positions; note also the close correspondence between this list and the list of top claimant nationalities in extraterritorial arbitrations (Table 1).

[14] Note that, while all subsidiaries are European firms, the intermediate and ultimate owners have a wide range of national origins (U.S., U.K., China, Japan, etc).

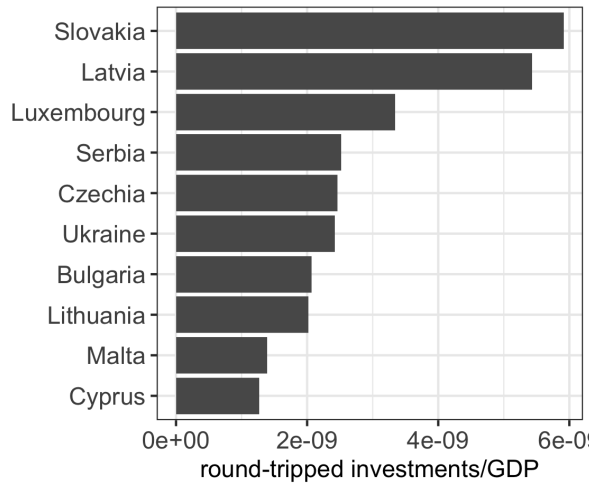
[15] Oligarchs commonly operate through commercial vehicles, however, so we do not discard investments that are ultimately owned by a firm.

Figure 3: **Who round-trips their capital in Europe, and where do they send it?**

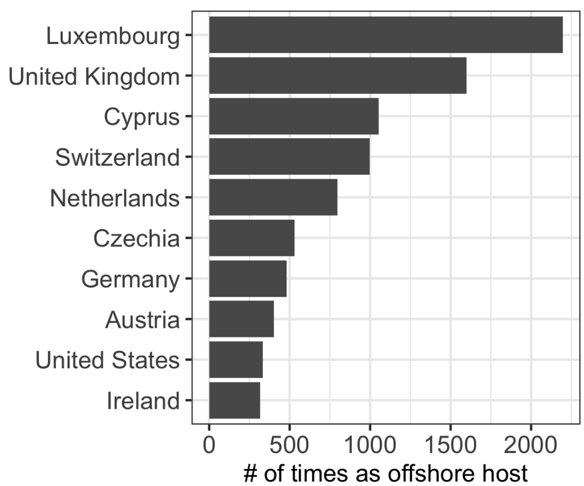
(a) Top round-trip home states



(b) Top round-trip home states (GDP-adj)



(c) Top round-trip offshore host states



4.2 Research Design and Results

Our primary analytical goal is to learn about why oligarchs choose to round-trip their domestic investment through certain offshore states and not others. Our wager is that international institutions—particularly BITs—matter, and that oligarchs will be more likely to choose offshore states that have a BIT with their own home state.

To test this proposition more rigorously, we model the choice among *potential* offshore states for each round-tripped investment in our sample.[16] Adopting a design used by Dyreng

[16]Note that we limit the sample to investments for which the offshore firm is a likely shell company,

Table 3: **Data structure: offshore host location models**

ID	Ultimate owner	Home state	Offshore host (actual)	Offshore host (potential)	Chosen
1	MR. ABC	Czechia	Luxembourg	Algeria	0
1	MR. ABC	Czechia	Luxembourg	Angola	0
⋮	⋮	⋮	⋮	⋮	⋮
1	MR. ABC	Czechia	Luxembourg	Luxembourg	1
⋮	⋮	⋮	⋮	⋮	⋮
2	MS. XYZ	Germany	Netherlands	Algeria	0
2	MS. XYZ	Germany	Netherlands	Angola	0
⋮	⋮	⋮	⋮	⋮	⋮

et al. (2015) and Thrall (2021), we generate a list of 155 potential offshore states through which each investment could have been routed. This design leverages the fact that shell companies have no real business activity, meaning that they are not tied to any particular state due to (for example) consumer markets or natural resource availability. Therefore, modeling investors' choice among many equally viable offshore states allows us to learn about which state- or bilateral-level political institutions investors find most valuable.

Our dependent variable is therefore a binary indicator for whether or not each potential offshore location was indeed selected by the investor; Table 3 illustrates the intuition. Our key independent variable is the presence of an active BIT between the investor's home state and the potential offshore state. We access BIT data from UNCTAD, and use additional BIT-level data from the IIA Mapping Project to ensure that we capture only BITs that provide ISDS access.[17] If the coefficient on the BIT variable is positively signed, it would suggest that oligarchs do indeed seek out offshore locations that provide them access to international arbitration against their own governments.

Since tax avoidance is the primary existing explanation for the round-tripping of capital, and previous work has shown that BITs and favorable tax institutions may be correlated (Thrall, 2021), it is important that we control for multiple tax factors. First, we measure the statutory corporate income tax rate in each potential offshore state; a lower income tax rate should make a potential location more favorable. Second, we measure the withholding tax rates that would be levied on transfers of capital (dividends, royalties, and interest payments) between home and potential offshore states. Low withholding tax rates reduce the cost to investors of conducting international business (Arel-Bundock, 2017), and we expect investors to seek out the lowest rates possible. Finally, we measure the existence of a bilateral taxation treaty between the home state and the potential offshore state. Tax treaties carry several benefits for investors, including lowering withholding tax rates and providing access

meaning that it has five or fewer employees (or no listed employees at all).

[17]Note that the vast majority (over 95%) of BITs do provide access to ISDS.

Table 4: **Modeling round-trip investors' choice among potential offshore locations.**

	DV: Chosen as offshore location					
	(1)	(2)	(3)	(4)	(5)	(6)
BIT	-0.005***	-0.003***	-0.008***	-0.008***	-0.008***	-0.003***
	(0.001)	(0.000)	(0.001)	(0.001)	(0.001)	(0.001)
Corp. Income Tax Rate			0.003***	0.004***	0.003***	-0.002**
			(0.001)	(0.000)	(0.000)	(0.001)
Tax Treaty			0.001	-0.001	0.001***	0.002***
			(0.000)	(0.001)	(0.000)	(0.001)
With. Tax Rate (Dividends)			-0.002***	-0.004***	-0.002***	-0.000
			(0.000)	(0.001)	(0.000)	(0.000)
With. Tax Rate (Interest)			-0.006***	-0.007***	-0.006***	-0.001
			(0.001)	(0.001)	(0.001)	(0.001)
With. Tax Rate (Royalties)			-0.002	-0.002	-0.002	0.000
			(0.002)	(0.002)	(0.002)	(0.001)
GDP per cap (offshore state)			0.004***	0.004***	0.004***	0.003***
			(0.000)	(0.000)	(0.000)	(0.001)
English Legal Origin			0.005***	0.004***		
			(0.001)	(0.001)		
Home state FE	No	Yes	No	Yes	No	Yes
Offshore state FE	No	Yes	No	No	No	Yes
Incorp. year FE	No	Yes	No	Yes	No	Yes
Num.Obs.	1,152,128	1,152,128	653,628	653,628	671,358	671,358
R2	0.001	0.129	0.025	0.027	0.025	0.143

* $p < 0.1$, ** $p < 0.05$, *** $p < 0.01$

to a tax dispute settlement mechanism.

We also control for the GDP per capita in each potential offshore state, and in some models we also include a control that measures whether each state's legal system is based off of English Common Law, which has been shown to be more favorable to capital (La Porta et al., 1998). Finally, we include year of incorporation, home state, and offshore state fixed effects to account for unobserved heterogeneity, and we cluster standard errors on the ultimate owner.

Figure 4 presents the results of six OLS models, each with various sets of controls and fixed effects. Model (6), which contains all time-varying controls as well as all fixed effects, is our preferred specification. Surprisingly, we find a robust *negative* and significant relationship between BITs and round-tripping. Across all six models, investors appear to be *less* likely to route their assets through states that have a BIT with their own home state. Further, the magnitude of this relationship is nontrivial; the average value of the dependent variable is 0.006, meaning that a coefficient of -0.003 (in Model 6) is relatively large.

The baseline regression results do not accord with our theoretical expectation and recent findings on the importance of BITs. Moreover, they are puzzling given the empirical reality that oligarchs have often used their offshore companies to file ISDS against their own governments. To ensure the robustness of this unexpected negative relationship between BITs and round-tripping, we conduct several additional analyses. First, we account for the fact that some BITs may be more favorable to round-trip investors than others by adjusting for treaty-level factors such as access to the premier arbitral forum (ICSID) or the inclusion of language that limits use of the treaty to certain types of entities.[18] Second, we replicate the main results while controlling for the sovereignty level (territory/dependency vs. non-territory/dependency) of each potential offshore location.[19] Third, to examine whether results may be biased by the inclusion of corporate (non-individual) investors, we replicate the results when limiting the sample to investments owned by individuals.[20] Finally, we use Imai, Kim and Wang (2020)'s PanelMatch estimator to model the change in incorporations at the bilateral level following the creation of a new BIT.[21] In each of these tests, we confirm the negative, signficant, and substantive relationship between BITs and the choice of offshore jurisdiction.

5 What Explains Extraterritorial Arbitration?

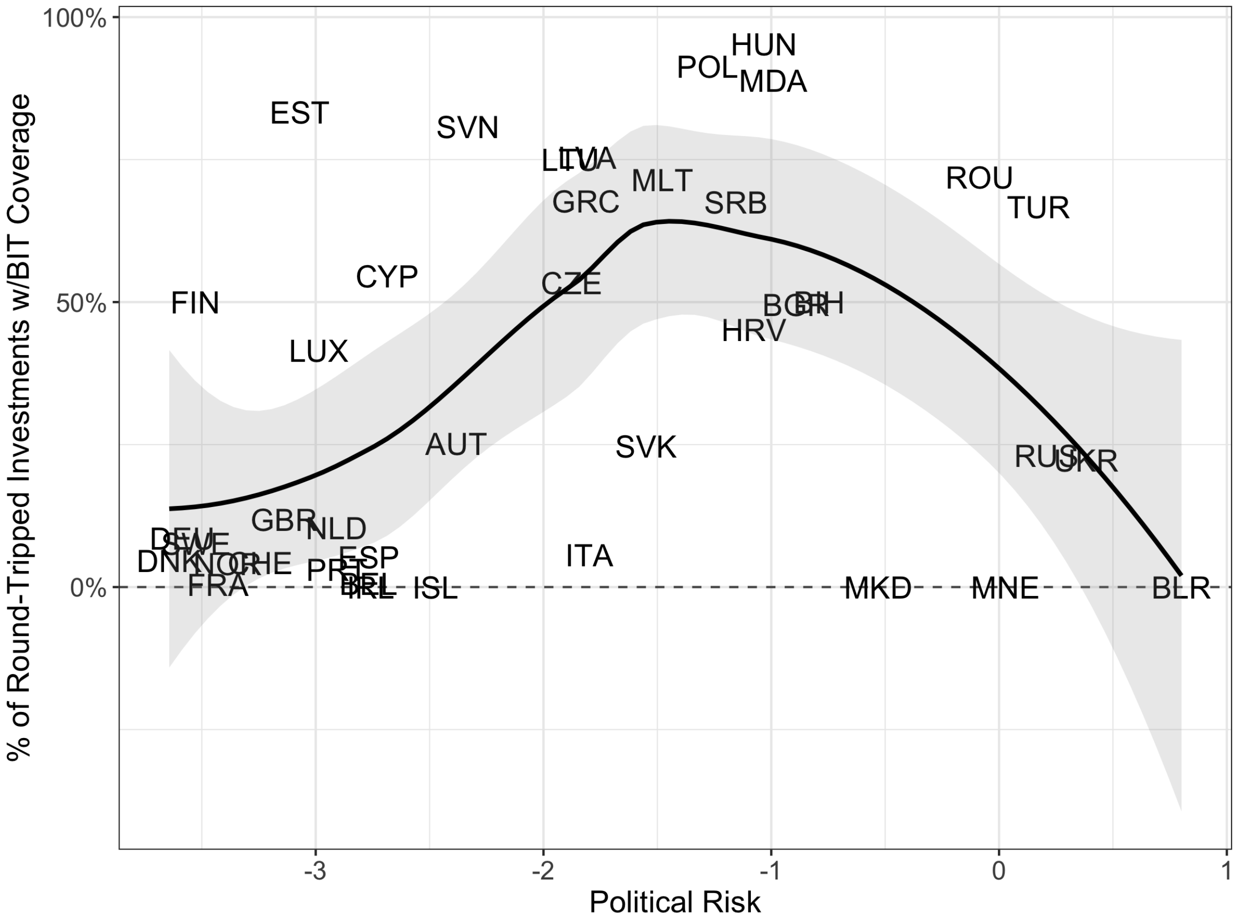
The primary motivation for this analysis is the descriptive observation that, in nearly 60 cases, oligarchs have been able to sue their own home governments for tens of billions of dollars using a system of international treaties that was designed for foreign investors. Extant cases of extraterritorial arbitration were made possible by round-tripped capital, e.g. oligarchs using foreign shell companies to hold ownership of their domestic assets. Yet, in the previous section, we find no systematic evidence that round-trip investors seek out offshore states that give them access to BIT protection, and indeed we find the opposite relationship. This is puzzling: if round-trip investors do not seek out offshore states that give them access to extraterritorial arbitration, why do these lawsuits continue to occur? We discuss and provide evidence for two possible alternative explanations.

5.1 Spillover Effects

First, we consider the applicability of Thrall (2021)'s Spillover Effects theory. In the context of multinational firms' foreign investments that are routed through intermediate shell companies, Thrall makes the argument that firms primarily care about tax treaty access rather than BIT access; however, since the bilateral tax and investment treaty networks overlap significantly, many firms who sought tax treaty access will gain investment treaty

[18] These results can be seen in Models 1-3 in Table A.1.
[19] These results can be seen in Model 4 in Table A.1.
[20] These results can be seen in Model 5 in Table A.1.
[21] These results can be seen in Figure A.1.

Figure 4: **Investors from medium-risk states have greater access to BITs through round-tripping.** Trend line estimated via LOESS with 95% CIs.



access as a side benefit. The consequence is that many firms gain the ability to file ISDS cases against their host states using their shell companies' BITs, even though they did not structure their investment with the explicit intention of gaining BIT access.

This argument could also be extended to the setting of oligarchs' round-tripped investments. Indeed, despite our finding that BITs have a negative impact on round-trip location after controlling for tax variables, we note that 22% of the investments in our sample are nevertheless routed through states that have a BIT with the investor's home state. Further, of these 22% of investments with BIT access, 94% also gain access to a bilateral tax treaty. Even more notably, BIT access through round-tripping appears to be correlated with the level of political risk—defined as the government's ability to arbitrarily enact and selectively enforce policies[22]—in the investors' home states. Figure 4 shows that investors from states in the middle of the political risk distribution (such as Poland, Hungary, and Czechia) fre-

[22] We operationalize political risk using the v2cltrnslw variable from the V-Dem dataset, which measures stability, predictability, and transparency in policy enactment and enforcement. We invert this variable such that less stability equals more risk.

quently gain BIT access in over half of all round-tripped investments, while investors from low-risk states like France and Germany rarely ever gain BIT access.[23] Since states with higher political risk are more likely to take actions that trigger ISDS cases, it is plausible that past extraterritorial arbitrations can be explained by oligarchs in these mid-to-high risk states repurposing shell companies that were created to avoid taxation.

The inverted-U in the figure could instead be explained by how business-government relations generally operates in different risk settings (Kalyanpur, 2020). In low risk environments, which correlate with highly institutionalized countries, plutocrats generally amass their wealth via conventional business activity. The government is usually dependent on private actors to stay in power - both instrumentally through campaign contributions and structurally by needing the economy to do well to stay in power (Hellman, Jones and Kaufmann, 2003; Lindblom, 1982). Risks of expropriation or unexpected regulatory change that could damage business is then unlikely, mitigating the need for BIT access against one's own government. By contrast, in high risk settings, there is usually only one avenue to becoming a plutocrat - aligning with the state (Evans, Haggard and Kaufman, 1992; Maxfield and Schneider, 1997). If an individual is part of the government's coalition that also reduces the need for potentially taking the state to an international forum - as you are part of the inner circle you are unlikely to be targeted even if the overall environment is risky. In other words, the commitment problem that under girds business-government relations in emerging markets subsides if one group is able command substantially more resources (North et al., 2009).

But in the middle, plutocrats may be part of that coalition relying on state contracts to build up their net-worth, or they could have garnered their wealth themselves . A relatively powerful independent set of plutocrats can threaten the state and its ruling coalition as the those with the independently wealthy could attempt to take over the government. Those independent actors will be aware of the potential threat they pose, and even if they do not plan to challenge the state, will need to take precautions because they will struggle to credibly commit to not wanting power. They would need to either give up their wealth, which plutocrats on the outside of a ruling coalition would not do without assurances. Those assurances would usually take the form of building up institutions that create predictability, but that would weaken the state's autonomy. The uncertainty then pushes the risk for the wealthiest higher, plausibly leading to them needing to seek foreign protections.

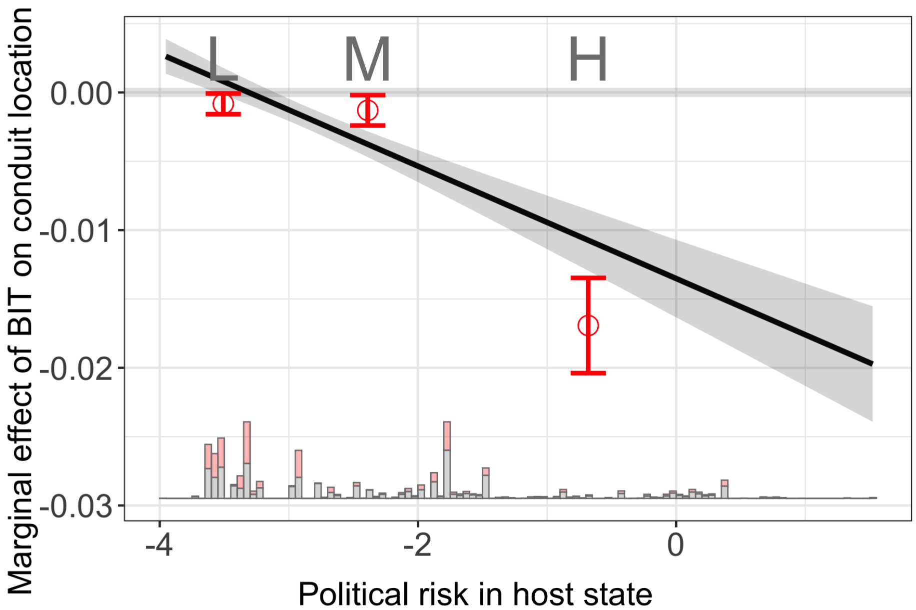
Is this evidence in favor of the spillover effects theory, or does it suggest that oligarchs' preference for BIT access may simply be stronger in states with higher political risk? To parse between these interpretations, we use Hainmueller, Mummolo and Xu (2019)'s binning estimator to model how round-trip investors' demand for BITs and tax treaties change according to the political risk environment.[24] What we find is consistent with the spillover effects theory: Figure 5 shows that, in states with higher levels of political risk, round-trip

[23] This is not driven by differences in the size of states' BIT portfolios: see Figure A.2.

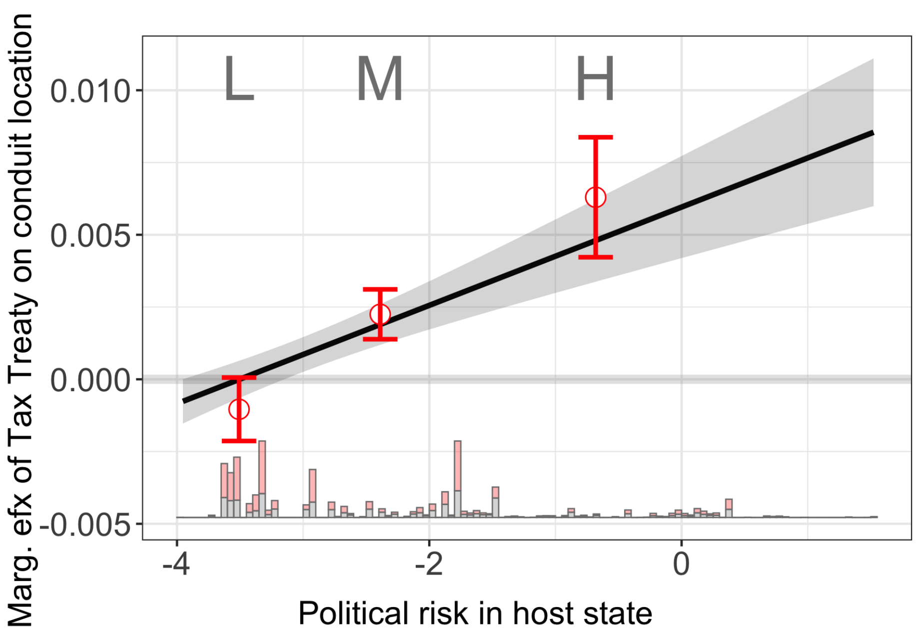
[24] The binning estimator calculates marginal effects by splitting the data into three equal-size bins according to the value of X (political risk, in this case), then estimating marginal effects at the median value of each bin. This allows for nonlinearity in marginal effects and prevents over-extrapolation.

Figure 5: **Round-trip investors in high-risk states seek out tax treaties, not BITs.**

(a) BITs



(b) Tax Treaties



investors are more likely to seek access to tax treaties and *less* likely to seek access to BITs.[25] This suggests that the relationship between political risk and BIT access presented in Figure 4 cannot be explained by higher demand for BIT access in high-risk states; rather, it is

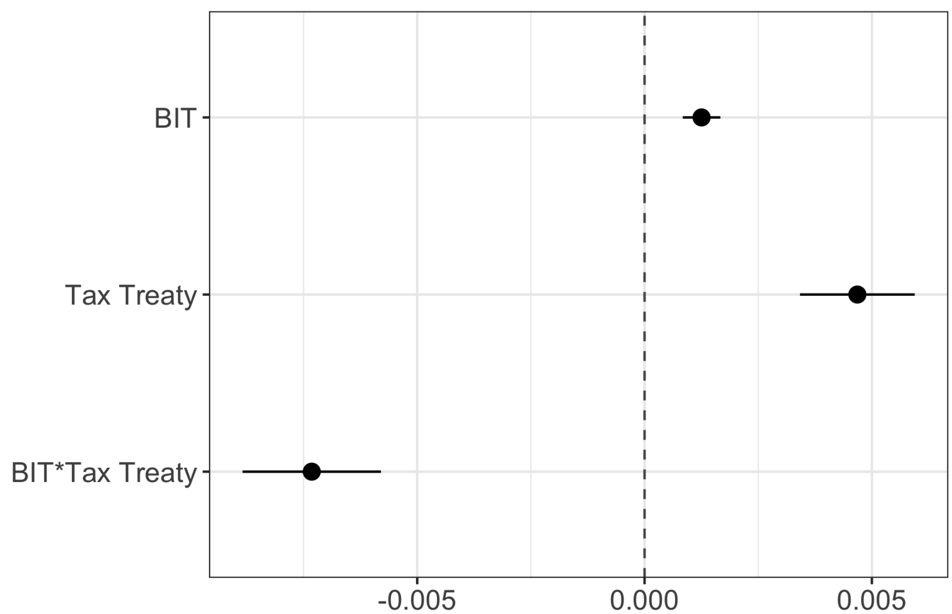
[25]Both models contain all controls and fixed effects from the baseline specifications.

more likely to be driven by the combination of (1) higher demand for tax treaty access in high-risk states, and (2) the overlap between tax and investment treaty networks. According to this interpretation, oligarchs may engage in round-tripping without taking the BIT network into consideration, then realize that they have BIT protection (and therefore access to extraterritorial arbitration) only after a dispute with the government arises.

5.2 Oligarch-level Risk

In the previous section, we found a negative relationship between political risk and BIT-shopping at the state level. However, we also know that some oligarchs are much more likely to be the target of state predation than others, even within the same country; factors such as political ideology, source of wealth, and personal connections (Earle et al., 2019; Markus and Charnysh, 2017) likely influence the risk that any given oligarch faces from their government. By using explanatory variables that are measured at the country-year level, we may be overlooking these *oligarch*-level variables that predict demand for BIT protection.

Figure 6: **When investors round-trip through a state that does not provide tax treaty access, they are more likely to select a state that provides BIT access.** Results from full model can be seen in Table A.2.



Unfortunately, resource constraints mean that we are unable to collect these types of individual-level data for all of the oligarchs in our sample. However, we take two steps towards evaluating the plausibility of oligarch-level explanations. First, to determine whether or not there is some subset of oligarchs who do seek out BIT access, we re-estimate Model 6 from Table 4 with the inclusion of a BIT-tax treaty interaction term. We focus specifically on the marginal effect of the BIT variable when there is no tax treaty between the oligarch's home state and the potential offshore state; the logic is that if an oligarch chooses to deviate from what is tax-optimal by selecting an offshore state that does not provide tax treaty access, they likely have a non-tax incentive for round-tripping their capital (such as gaining BIT access). Thus, if there is heterogeneity in oligarchs' preferences for political risk protection, we should see a positive sign on the BIT coefficient after including the interaction term.

Figure 6 presents the coefficient estimates for the key variables. The results indicate that, despite the spillover effects detailed in the previous section, there is also some separation between oligarchs who seek out tax optimal offshore locations and those who seek BIT access; both the BIT and tax treaty terms are positive and significant, but the interaction term is negative, significant, and large in magnitude. This provides suggestive support for the oligarch-level risk explanation: there is a subset of our sample that valued political risk protection over tax minimization. But who are these individuals?

To shed some light on this question, we examine the 99 round-tripped investments in our sample that provided the investor with BIT access but not with tax treaty access. First, as a face validity check, we note that 26% of these investments (by far the largest share) were made by Russian investors; as Table 2 shows, Russian oligarchs have also filed the greatest number of extraterritorial arbitration cases.

Second, we find that the owners of these firms have often been involved in politics. For example, Serhii Kasianov, who incorporated a Panamanian shell company in 2014, served in the Ukrainian Parliament from 2002-2006;[26] Bikov Artyom Elbrusovich, who incorporated an Austrian shell company in 2005, held multiple positions in the Soviet and post-Soviet Russian governments, and campaigned (unsuccessfully) to serve in the Duma in 1995.[27] Likewise, other oligarchs in this sample have been involved in public disputes with the government; for example, it includes Russian billionaire Sergej Gljadelkin, who was implicated in multiple construction scandals.[28] Others were involved with the management of state-owned enterprises; for example, Slobodan Stamenkovic served as Chief Commercial Officer of Air Serbia from 2014-2015, creating his offshore shell company in the same year as his departure.[29] These individual-level factors—political involvement, scandal, employment at an SOE—arguably increase the probability that an oligarch is expropriated by their own government. When structuring their offshore assets, these higher-risk individuals may find it rational to sacrifice some tax benefits in order to gain access to BIT protection.

In sum, we find some suggestive evidence in support of the hypothesis that oligarch-level factors are important predictors of demand for BIT protection through round-tripping. These preliminary findings underscore the importance of studying political risk and autocratic politics at the micro level (Earle et al., 2019; Hassan et al., 2019; Markus and Charnysh, 2017); we hope this spurs more research examining the intersection of the wealth protection

[26] See https://www.wikidata.org/wiki/Q12109007.

[27] See https://tadviser.com/index.php/Person:Bikov_Artem_Elbrusovich.

[28] See Mark Thomas, "Who is the Russian investor behind the biggest investment in Dubrovnik tourism," *The Dubrovnik Times*, 23 November 2016.

[29] See https://www.linkedin.com/in/slobodan-stamenkovic.

strategies of individuals and the operation of international regimes .

6 Conclusions

In *The Hidden Wealth of Nations* and his accompanying work, Gabriel Zucman provides us with the most comprehensive analysis of offshore financial flows to date (Zucman, 2015). By reconciling national macroeconomic data, he documents that roughly 8% of global wealth is stashed offshore,[30] some $ 7 trillion, with more than 20% of the wealth from numerous emerging markets stashed abroad. In this manuscript, we examine how this offshore wealth is generating new venues for traditionally domestic political battles.

Plutocrats can and have taken advantage of tax havens to exploit the international investment regime. Setting up shell or holding companies offshore and then routing the money back home de jure turns a domestic plutocrat into a foreign investor. When those tax havens have a bilateral investment treaty, plutocrats can then sue their own governments using treaty provisions intended for foreign corporations. We document the rise of such extraterritorial arbitration, showing that they represent 8% of all known ISDS cases and yet constitute roughly 41% of the total damages claimed under the regime. Further, we find that 22% of existing round-tripped investments are routed through an offshore state that has a BIT with the investor's home state, giving the investor access to extraterritorial arbitration in the event of a dispute with the government.

While resembling conventional MNC-host state cases in terms of sectors and governing rules, extraterritorial arbitrations are qualitatively different. The political stakes are higher, as they frequently involve oligarchs who have fled their home country taking on their political rival, leading cases to rarely settle. At one level, this re-purposing of the investment regime could be applauded as it gives actors a chance to respond to illiberal opponents, as the investment regime broadly seeks to do. But those claiming damages are usually individuals who themselves have taken advantage of weak institutions in their home country to get to the point where they could have the means to take on their sovereigns. Moreover, they gain access to these institutional tools by avoiding the basic expectations of citizenship, paying taxes. These are the inevitable contradictions of having illiberal actors embedded within an economic order that relies on nationality as a central feature dictating one's rights. They will exploit the gaps.

Contra our initial expectations, plutocrats do not appear to actively structure their wealth to gain access to BIT protections against their sovereign. One explanation of the ineffectiveness of BITs in spurring economic development is that there exists an information problem: the average corporation may not be aware of the BIT network, or at least may not be aware of its potential benefits (Poulsen, 2010). We doubt this explains the decision-making of plutocrats who face threatening environments on a daily basis and usually have an army of international lawyers at their disposal. Moreover, our analysis of the most comprehensive round-tripped investment data suggests that the super elite actually appear less likely

[30] A figure that is updated to 10% in later work; see Alstadsæter, Johannesen and Zucman (2018).

to stash their wealth in havens that have an investment treaty with their home country. Political economy research emphasizes the political resources business in emerging markets need to develop to fortify their wealth. When it might be rational for plutocrats in weakly institutionalized settings to avoid guarding themselves presents an important future research agenda.

We expect that focusing on the signaling effects of seeking protection could be a fruitful avenue. When an individual sends their money abroad, they can bury its location through a web of companies, and no one but their accountants are likely to know the details. But when an individual roundtrips an investment, the government is aware of at least part of the wealth structure - it shows up in the government's national accounts. By putting yourself in a position to file a claim against your sovereign by choosing a haven with a BIT, your actions might invite aggression by the government as it will make the state wonder why you think you need protection. Using offshore finance too strategically might (inadvertently) signal to the state you are planning a challenge. If a fight does arise, you can always attempt an ISDS via an *ex-post* conflict created shell company in a BIT protected haven, as some corporations have recently successfully manged to do.

A number of theories of political development expect plutocrats to be the driving force behind political development, be it liberalization or democratization (North and Weingast, 1989; North et al., 2013; Albertus and Menaldo, 2014). The general logic is that the development of the rule of law and competitive elections will bind the state from expropriating the wealth of the plutocracy. But we illustrate the way globalization allows elites to arbitrage the institutions that they traditionally pressured the state to provide. This should plausibly reduce their incentives to fight for reform in their home jurisdictions. We are not the first to indicate a potentially deleterious effect between capital mobility and political development (Milanovic, 2016; Pistor, 2019; Sharafutdinova and Dawisha, 2017). But prior work has not incorporated the role of global (investment) institutions in this process. That is critical when plutocrats can access property protections as a spillover of "normal" business practices like minimizing their taxes as our findings suggest. We hope that the manuscript pushes other scholars to continue developing and testing theories that factor the international institutional environment into models of domestic elite conflict (Farrell and Newman, 2014).

Finally, the analysis points toward a need to better under the globalization of the individual (Cooley and Sharman, 2017). One of the starting points of our theory is that individual plutocrats in emerging markets are able to build nationality portfolios in a fashion that mimics MNCs. Their ability to build such portfolios are supported by a host of "enablers" - lawyers, accountants, wealth managers, estate agents - whose economic and political incentives merit further research (Harrington et al., 2017). But incorporation is only one path in nationality diversification and thereby legal arbitrage; plutocrats can buy "golden visas" and passports in the burgeoning mobility market. The plutocratic toolkit continues to expand even as we see the growth of populist movements. In short, the findings call for more academic work on how economic interdependence empowers the superwealthy by fostering institutional inequalities.

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Appendix

A Additional Analyses

Table A.1: **Five robustness tests of the baseline results.**

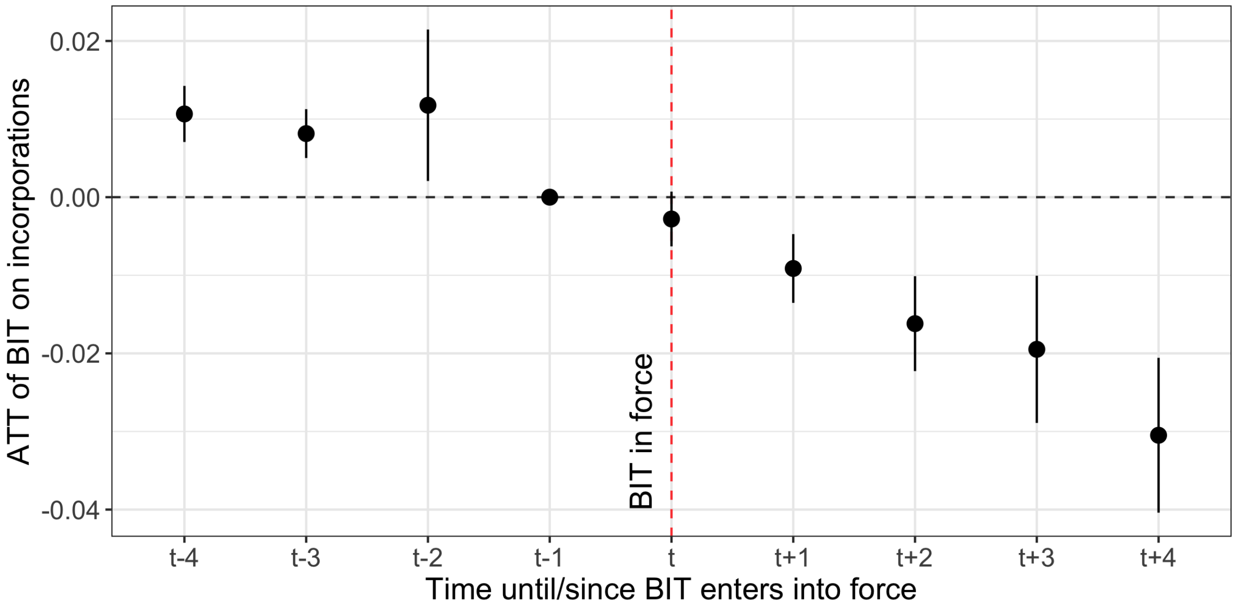
	Model 1	Model 2	Model 3	Model 4	Model 5
BIT			-0.005***	-0.004***	-0.005***
			(0.001)	(0.001)	(0.001)
BIT (w/ICSID)	-0.002***				
	(0.000)				
BIT (w/o ICSID)	-0.011***				
	(0.002)				
BIT (w/Activity Reqs)		-0.007***			
		(0.001)			
BIT (w/o Activity Reqs)		-0.003***			
		(0.001)			
Activity Reqs			-0.005***		
			(0.001)		
Define Ownership			0.000		
			(0.000)		
Denial of Benefits			0.001		
			(0.001)		
ICSID access			0.002***		
			(0.001)		
Corp. Income Tax Rate	-0.003**	-0.003**	-0.003**	-0.003**	-0.006***
	(0.001)	(0.001)	(0.001)	(0.001)	(0.001)
Tax Treaty	0.002***	0.002***	0.002***	0.002***	0.001**
	(0.000)	(0.000)	(0.000)	(0.000)	(0.001)
With. Tax Rate (Dividends)	-0.001*	-0.001*	-0.001*	-0.001*	-0.003***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.001)
With. Tax Rate (Interest)	-0.001***	-0.001**	-0.001**	-0.001**	-0.002***
	(0.001)	(0.001)	(0.001)	(0.001)	(0.000)
With. Tax Rate (Royalties)	0.000	0.000	0.000	0.000	0.001*
	(0.001)	(0.001)	(0.001)	(0.001)	(0.000)
GDP per cap (offshore state)	0.003***	0.003***	0.003***	0.003***	0.006***
	(0.001)	(0.001)	(0.001)	(0.001)	(0.001)
Home state FE	Yes	Yes	Yes	Yes	Yes
Offshore state FE	Yes	Yes	Yes	Yes	Yes
Incorp. year FE	Yes	Yes	Yes	Yes	Yes
No territories	No	No	No	Yes	No
Indiv. owners only	No	No	No	No	Yes
Num.Obs.	808532	808532	808532	793752	459422
R2	0.136	0.135	0.135	0.135	0.129

* $p < 0.1$, ** $p < 0.05$, *** $p < 0.01$

Table A.1 presents the results of four models that test the robustness of the baseline results presented in Table 4. Models 1-3 test for heterogeneity across different types of BITs. First, Model 1 disaggregates the BIT variable into BITs that provide access to ICSID—the most dominant arbitration forum, and one that is thought to be preferred by investors (Betz, Pond and Yin, 2021)—and those that do not. While the magnitude of the relationship is smaller for BITs that provide ICSID access, as expected, it remains negative and significant. Model 2 likewise disaggregates the BIT variable into BITs that include a requirement that investors maintain "substantial business activity" in both partner states in order to invoke the BIT's protections and those that have no such clause; since round-tripping involves the use of shell companies, who by definition have no substantial business activity, we may expect investors to seek out BITs that do not have activity requirements. Again, however, the coefficient on both types of BITs is negative and significant.

Model 3 includes the BIT variable as well as four additional indicators that may affect round-trip investors: in addition to ICSID access and activity requirements, we include variables that capture whether a BIT has a denial of benefits clause and whether it includes a definition of legal ownership (both aspects that we would assume to be unfavorable for round-trip investors). Again, while most of these aspects affect location choice in the ways that we would expect, the coefficient on the BIT variable remains negative and significant. Model 4 re-estimates the baseline model while dropping all potential offshore jurisdictions that are only partially sovereign (territories, crown dependencies, etc) and results are unchanged. Finally, Model 5 simply re-estimates the baseline model on a sample that includes only individual (rather than corporate) ultimate owners; while confidence intervals are wider due to the smaller sample, results are ultimately highly similar to the baseline models.

Figure A.1: **PanelMatch results: new BITs decrease round-trip incorporations**



Our primary research design models the choice between potential offshore locations for individual investments. However, another strategy is to look at the aggregate yearly incorporations of shell companies in offshore state j by owners in home state i, and to estimate how these incorporations change once states i and j sign a BIT together. This is akin to a difference-in-differences design with staggered treatment timing, since different pairs of states sign BITs at different times. We therefore use the PanelMatch estimator, which Imai, Kim and Wang (2020) developed for exactly this type of design.

The PanelMatch estimator requires two pre-processing steps prior to estimation: first, each treated observation it is matched with a set of other observations M_{it} that had the same treatment status as it for the previous L time periods but were *not* treated at time t.[31] Next, to ensure that the observations in the matched sets can serve as a plausible counterfactual for the corresponding treated observations, the matched sets are pruned (or "refined") to remove or downweight observations that have covariate or outcome histories that are too different from those of the treated observations. Once the matched sets have been refined, the following estimator is applied:

$$\hat{\delta}(F, L) = \underbrace{\frac{1}{\sum_{i=1}^{N} \sum_{t=L+1}^{T-F} D_{it}} \sum_{i=1}^{N} \sum_{t=L+1}^{T-F} D_{it}}_{\text{Average over all treated observations}} \underbrace{\Big\{ (Y_{i,t+F} - Y_{i,t-1}) - \sum_{i' \in M_{it}} w_{it}^{i'} (Y_{i',t+F} - Y_{i',t-1}) \Big\}}_{\text{Treated observation-specific diff-in-diff estimate}} \tag{1}$$

Each matched set serves as counterfactual group for the corresponding treated observation, allowing for the calculation of treated observation-specific difference-in-difference esti-

[31] L is a researcher-determined parameter.

mates. The PanelMatch estimate is simply the average of these treated observation-specific estimates. We set $L = 4$ and report estimates for each value of F (the number of years post-treatment after which the effect is measured) between -4 and 4. We use propensity score weighting to refine the matched set. Covariates used for the refinement include all of the variables from Model 6 in Table 4, as well as home state regime type, GDP per capita, and political risk.

Figure A.1 presents the results. Note that, as soon as a BIT enters into force between two states i and j, round-tripped investments from $i \rightarrow j \rightarrow i$ decline relative to the pairs of states in the matched set that are similar on a wide range of other variables. These results increase our confidence in the negative relationship identified in the baseline models.

Figure A.2: **Investors from medium-risk states have greater access to BITs through round-tripping, even after adjusting for # of BIT partners.** Y-axis measure is calculated for each state as follows: [Proportion of round-trip partner states have a BIT with the home state] − [Proportion of all potential partner states that have a BIT with the home state].

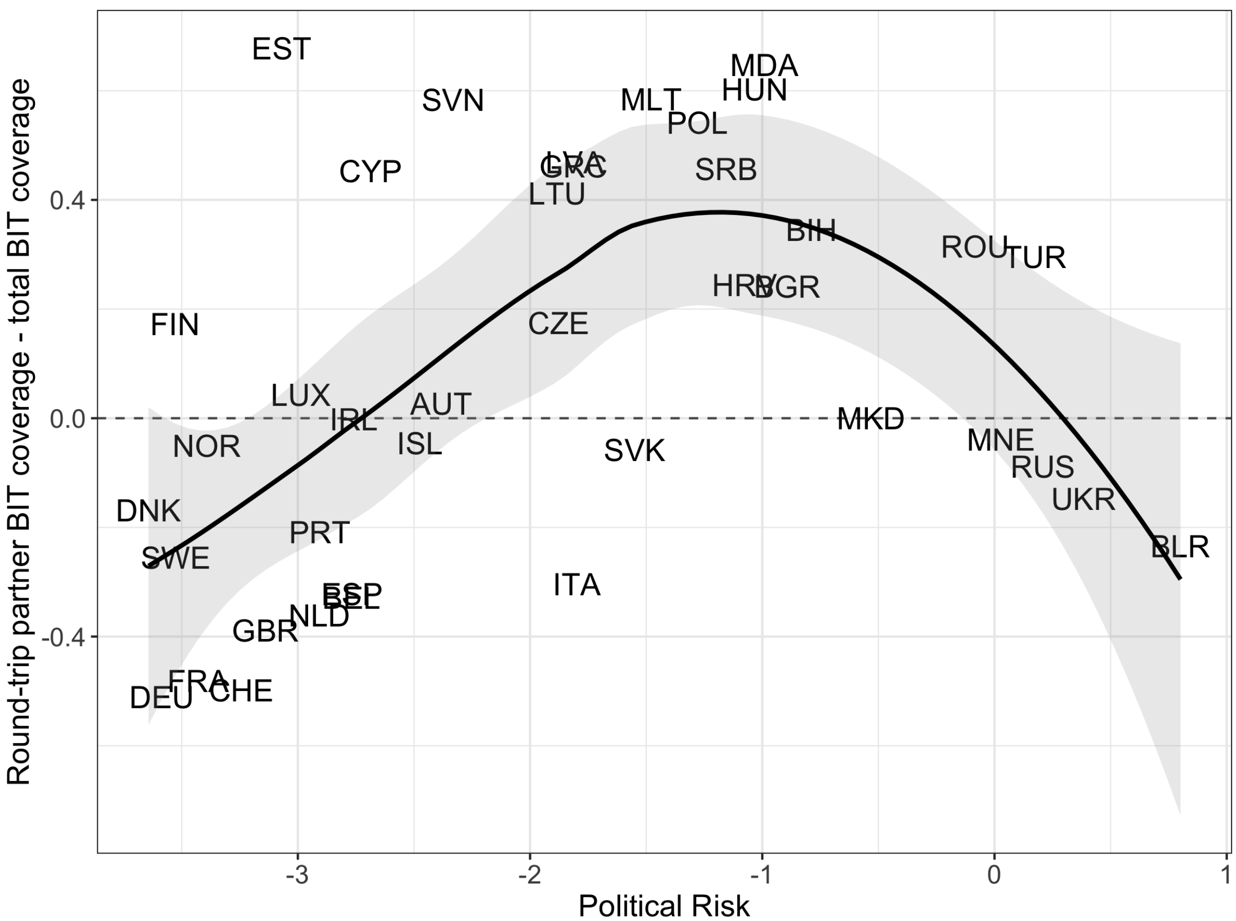


Table A.2: **Model with BIT × Tax Treaty interaction**

	Model 1
BIT	0.001***
	(0.000)
Tax Treaty	0.005***
	(0.001)
BIT × Tax Treaty	-0.007***
	(0.001)
Corp. Income Tax Rate	-0.003**
	(0.001)
With. Tax Rate (Dividends)	-0.001*
	(0.000)
With. Tax Rate (Interest)	-0.001**
	(0.001)
With. Tax Rate (Royalties)	0.000
	(0.001)
GDP per cap (offshore state)	0.003***
	(0.001)
Home state FE	Yes
Offshore state FE	Yes
Incorp. year FE	Yes
Num.Obs.	808,532
R2	0.136

* $p < 0.1$, ** $p < 0.05$, *** $p < 0.01$